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Economic Changes in Western and Eastern Europe



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I came to the Wissenschaftskolleg with great aspirations, none of which were realized, and numerous projects, none of which were completed. That unanticipated yet fruitful undertakings got in the way is, I suppose, one indication of a successful sabbatical year.

My arrival in Europe came on the heels of the September 1992 crisis in European financial markets, when Italy and the U.K. were forced to abandon the European Monetary System, Spain, Portugal and Ireland to devalue their currencies. Much as doctors study disease as a way of understanding the operation of healthy organisms, economists study crises for the insight they provide into the normal functioning of markets. The events of September induced me to agree to write, for an American journal, a "short" report on the crisis in the European Monetary System and its implications for the Maastricht Treaty and the monetary unification project. That brief report evolved into a 100 page opus, co-authored with Charles Wyplosz of INSEAD (in Fontainebleau, France). Perhaps reflecting the influence of a year spent in Europe, its conclusions are very different from the assumptions with which I began. I believed that the construction of a single European market in commodities, capital and labor was an entirely different matter than monetary unification; one could have the former and its undeniable benefits, I supposed, without also embracing the latter. I ended up concluding that, for political if not eco-

conomic reasons, Europe must have both a single market and a monetary union if it is to have either. In highly integrated markets, exchange rate swings are simply too painful for the impacted firms to bear; currency depreciation abroad will lead them to lobby for protection against foreign firms suddenly able to undersell them in domestic markets. More likely than not they will succeed, in which case the resulting policies will thwart efforts to complete the internal market.

Monetary union, which rules out exchange rate changes, is therefore necessary to make factor- and commodity-market integration economically palatable and politically viable.

The question that remains — and that was pointed out by the September crisis — is how to complete the treacherous transition from the present position to the nirvana of monetary union. My co-author and I offer a controversial suggestion: that a tax on foreign exchange transactions be imposed to discourage speculation, thereby stabilizing European exchange rates until monetary union is achieved. The piece containing this proposal lives in infamy as the paper that sank the peseta. The Governor of the *Banca de Espana* alluded to our proposal in a speech in April. But suggesting doing something along these lines rather than actually doing it proved counterproductive; the next day currency traders sold pesetas in order to beat the possible future imposition of a tax. The peseta collapsed on foreign exchange markets, forcing massive intervention by the *Bundesbank* and the *Banque de France*, followed eventually by another devaluation.

This notoriety earned us an invitation to summarize our proposal in a column in *The Economist Magazine*, subjecting Frau Sanders at the Wissenschaftskolleg's reception to an avalanche of faxes.

An economist cannot spend a year in the heart of Central Europe without thinking about the transformation process in the East. Contact with scholars and policymakers from Eastern Europe and the former Soviet Union prompted me to extend some previous research and to begin new work contrasting post-World War II Western European reconstruction with post-Cold War Eastern European transformation. Much of this research was concerned with the economic consequences of the Marshall Plan. I concluded, as fellows will recall from my colloquium, that a Marshall Plan for Russia, comparable in scale to that of the 1940s, is unlikely to be productive under present circumstances, but that Western aid might be constructively devoted to underwriting a social safety net, to financing privatization, and to sponsoring technical assistance. I wrote a short piece elaborating my work on the Marshall Plan for the *Deutsches Institut für Wirtschaftsforschung* in Berlin, which specializes in, among other things, economic analysis of Eastern European transformation. A longer paper

examined an offspring of the Marshall Plan, the European Payments Union, and asked whether an EPU-like arrangement would be suitable for rebuilding economic relations among the former Soviet republics. Finally, I wrote a brief report describing the labor market programs set up by the German government to deal with the mass redundancies caused by economic restructuring in the eastern *Bundesländer*. The success or failure of those policies is interesting not just for Germany, since other countries, notably Russia, anticipate redundancies of the same sort and are interested in lessons, positive and negative, from German experience.

This last paper was co-authored with Ansgar Rumler, my research assistant for the year, who died so tragically in a skiing accident this spring. Ansgar was deeply involved in the other projects as well. He understood quickly what I was trying to accomplish, often before I did. It is hard to articulate the importance of his contributions.

The opportunity to get to know Ansgar was one of the best parts of my Wissenschaftskolleg experience. Other fellows will know of his generosity. Instances I recall include his meeting me at Tegel upon my arrival, the television he loaned me in a futile effort to encourage me to learn German, and the Saturdays when we were both in the office — his presence unprompted — when he would get us a pizza to share for lunch. This same generosity, and considerable intellectual gifts, enabled him to have, I believe, a quite remarkable impact on the Wissenschaftskolleg as a whole. Ten or fifteen years younger than even the younger fellows and without their advanced degrees, he had not the slightest trouble interacting as a colleague, over the luncheon table, at the colloquium and in the corridors. He easily held his own intellectually, and his personal warmth enabled him to quickly surmount all barriers of age and professional status.

Ansgar will be missed by all who knew him, and I certainly will not be able to look back on my year at the Wissenschaftskolleg without thinking about his friendship and mourning his loss.

Publications mentioned:

"The Unstable EMS" (with Charles Wyplosz), *Brookings Papers on Economics Activity* (1993.1)

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"A Precis of German Labor Market Policies" (with Ansgar Rumler),
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