



The Euro after 10 years

Achievements, Challenges & Implications for Asia

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Manila, 25 June 2009

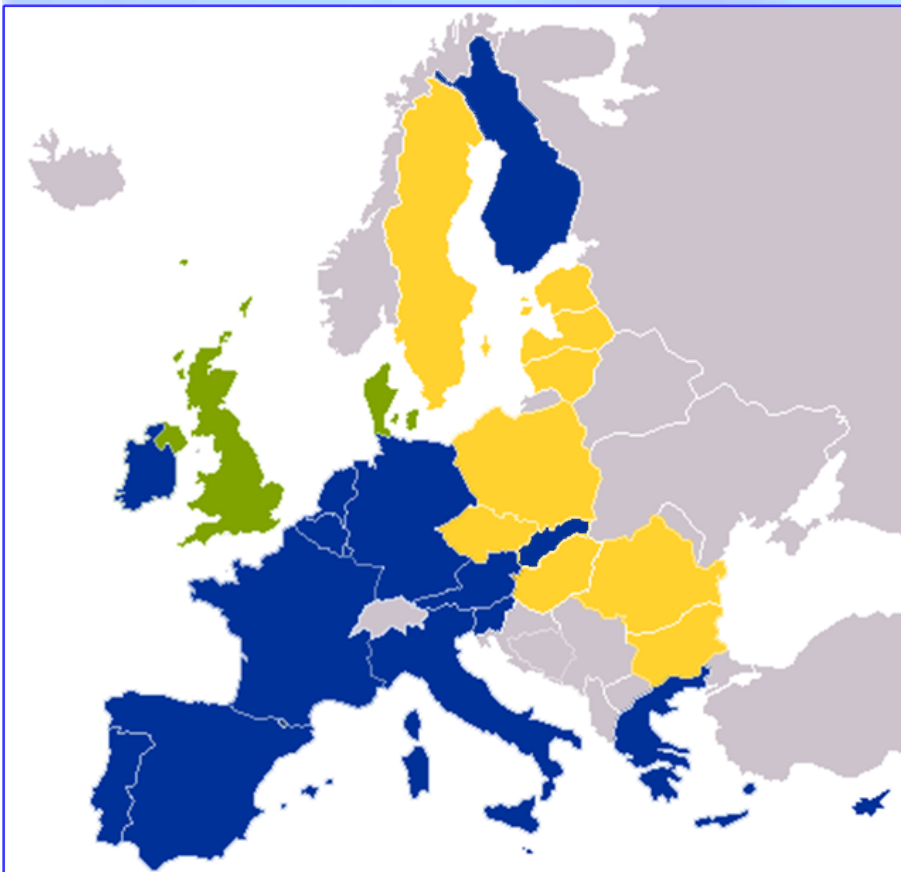
1 January 1999: a defining moment in European history

- ❖ The euro became the currency of 300 million people in eleven countries.**
- ❖ A unique stability-oriented policy framework was created with centralized monetary policy and decentralised fiscal policies.**
- ❖ The biggest change in the international monetary system since the end of the Bretton-Woods system**

Outline

- 1** What is EMU? Why and how did it happen?
- 2** The first decade
- 3** Current and future challenges
- 4** Lessons for Asia?

What is Economic and Monetary Union (EMU)?



- ❖ **16 Member States of the EU have the euro as single currency**
- ❖ **2 have “opt-outs” (Denmark, United Kingdom)**
- ❖ **9 Member States do not yet fulfill the criteria for joining**

What is Economic and Monetary Union (EMU)?

- 1. A single currency – the euro**
- 2. Centralised monetary policy**
- 3. Common exchange rate**
- 4. National economic policies coordinated at EU level (fiscal & structural policies)**

The euro area in the world (2007)

	Euro Area (15)	EU-27	US	Japan	China
Population (millions)	320	496	302	128	1329
Share of World GDP (% at PPP)	16.4	22.5	21.6	6.7	10.9
Share of World Trade (% of goods excluding intra-EU trade)	16.3	21.1	11.2	7.1	11.9

Source: European Commission and IMF

Why?

- ❖ To create stability
- ❖ To complete the Single Market
- ❖ To avoid intra-European exchange rate turmoil
- ❖ To stimulate trade, capital flows and a pan-European financial market
- ❖ Ultimately: To generate growth and employment

Scepticism...

- ❖ Fear of higher inflation and debt
- ❖ How to deal with country-specific stocks?
- ❖ Many predicted collapse

True: monetary union involves cost

How?

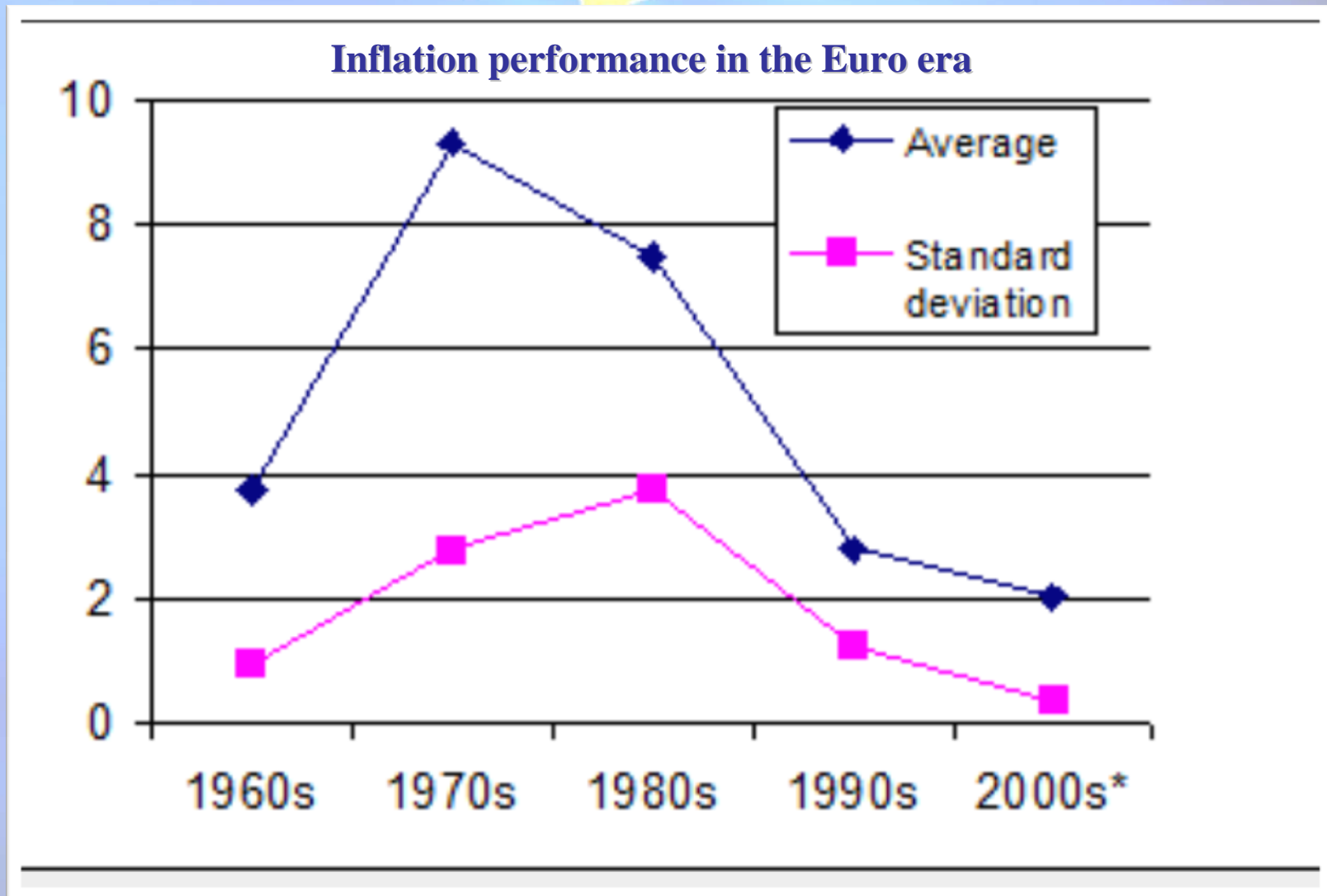
- 1970** **Werner Report – 3-stage process for creating EMU by 1980**
- 1979** **Launch of the European Monetary System (EMS)**
- 1989** **Delors Report - Plan for EMU in 3 stages, with a single currency and a single central bank.**
- 1992** **Treaty of Maastricht - implements the Delors Plan**
- 1997** **Adoption of the Stability and Growth Pact**
- 1998** **European Council decision on the introduction of the euro in 11 Member States (May 1998)**
- 1999** **Introduction of the euro as ‘book money’.**
- 2002** **Euro cash changeover – note and coins replace national currencies**

After a decade: a success

“I think the euro has been an unqualified success and Europe is better off and more powerful because of it”

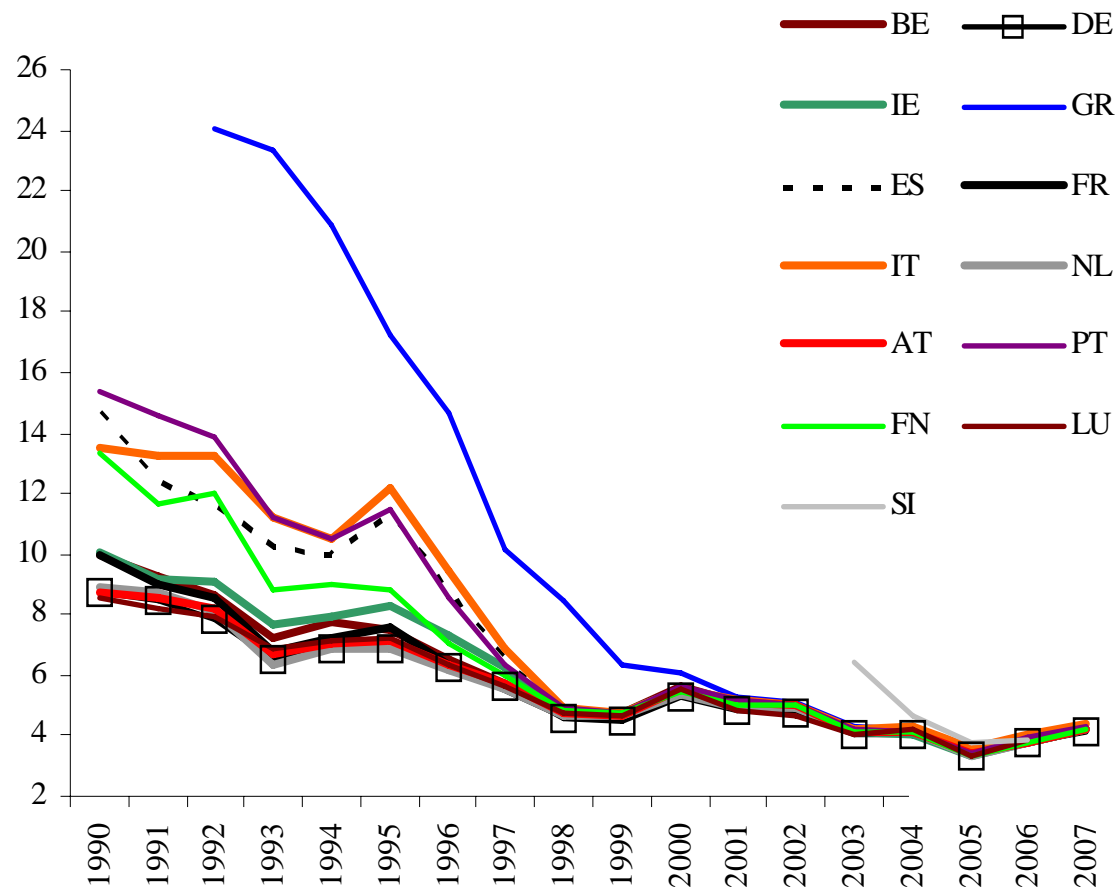
R. Mundell, July 2008

Price stability



Low interest rates

Evolution of 10-year government bond yields (in percent, annual data)

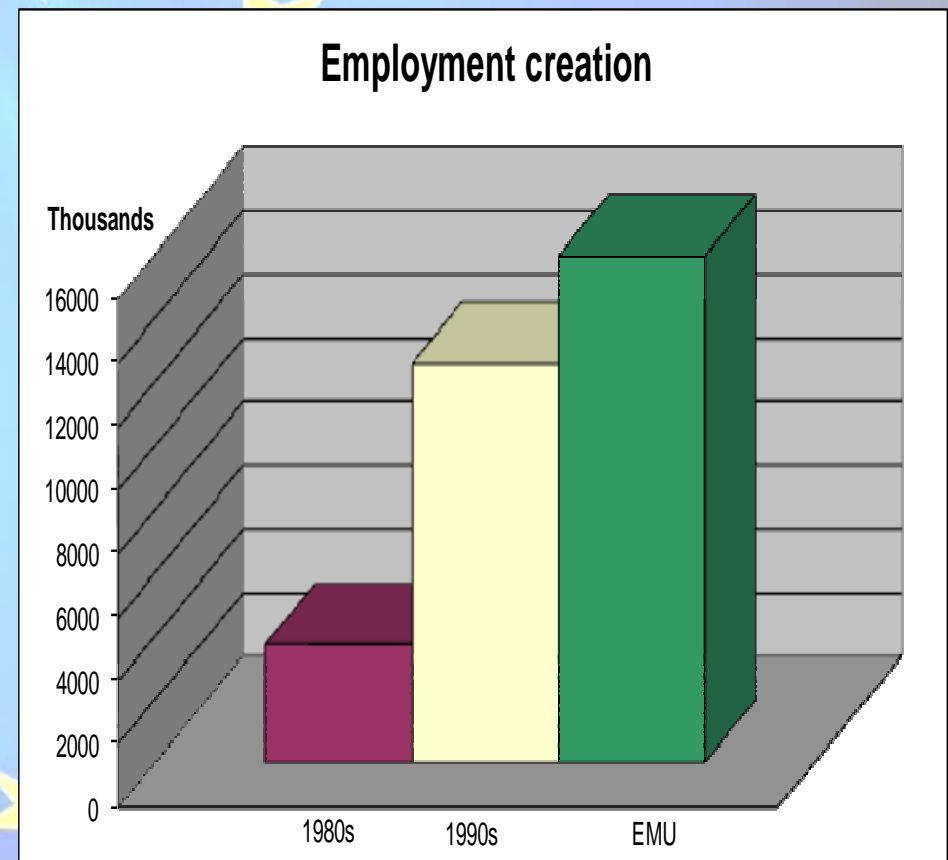


Source: Eurostat

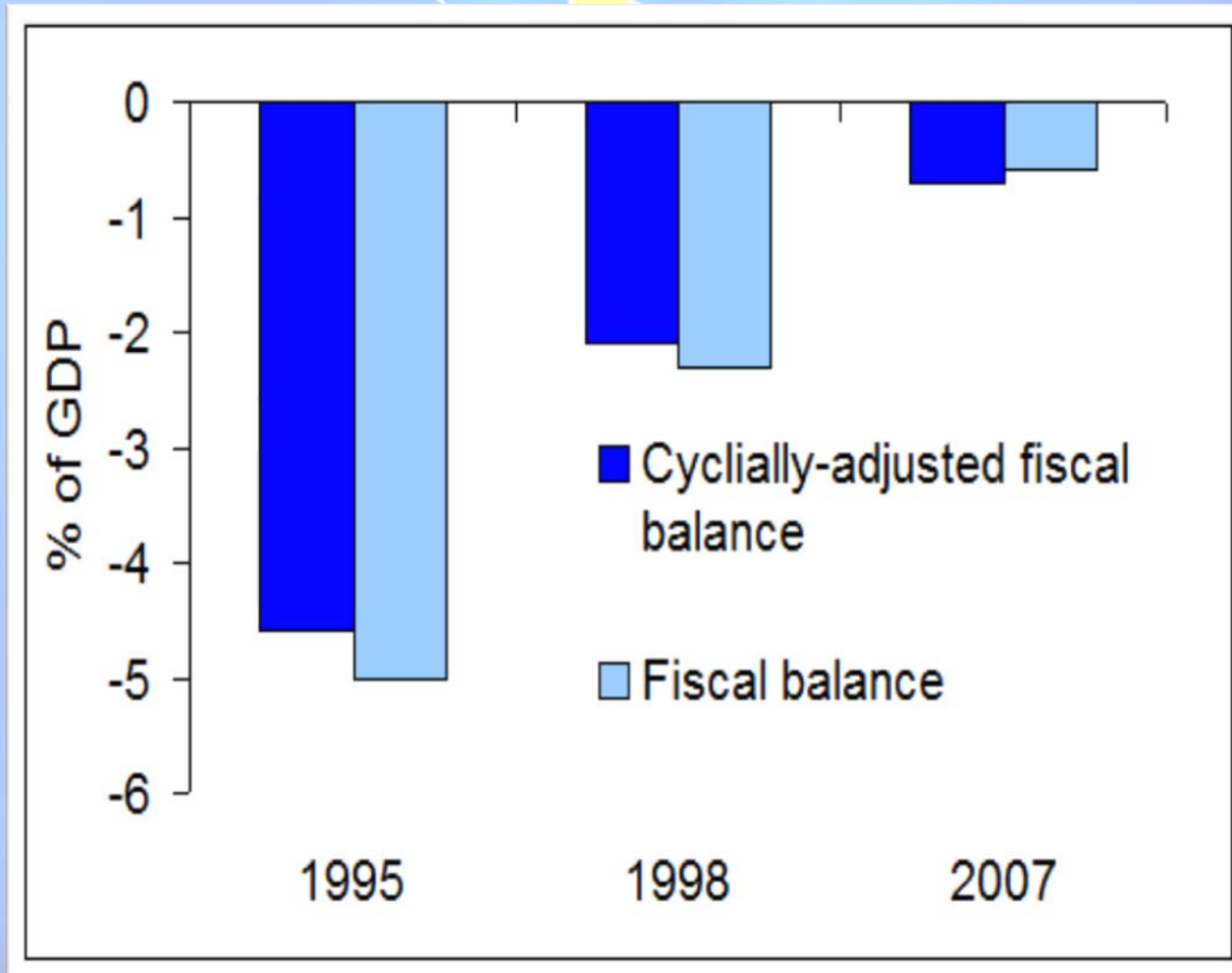
Jobs and growth

During the first decade

- ❖ **16 million jobs created**
- ❖ **2 % economic growth, same as the preceding decade**
- ❖ **GDP growth-per-capita was 1.5% (same as in the US)**

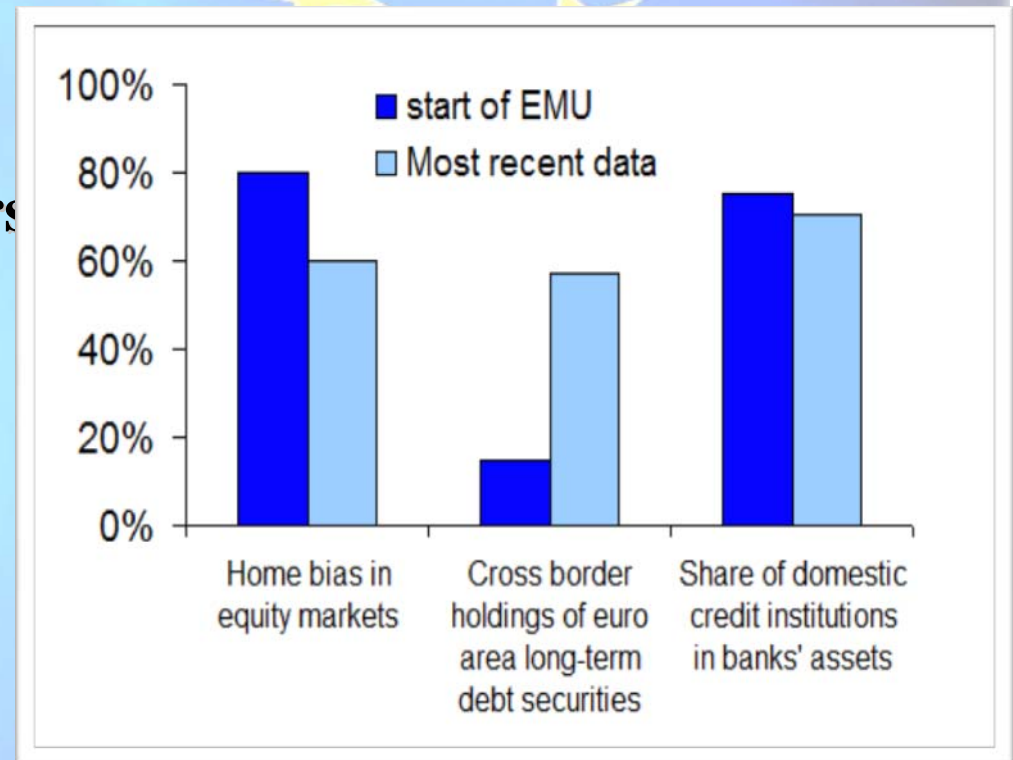


Fiscal Positions dramatically improved



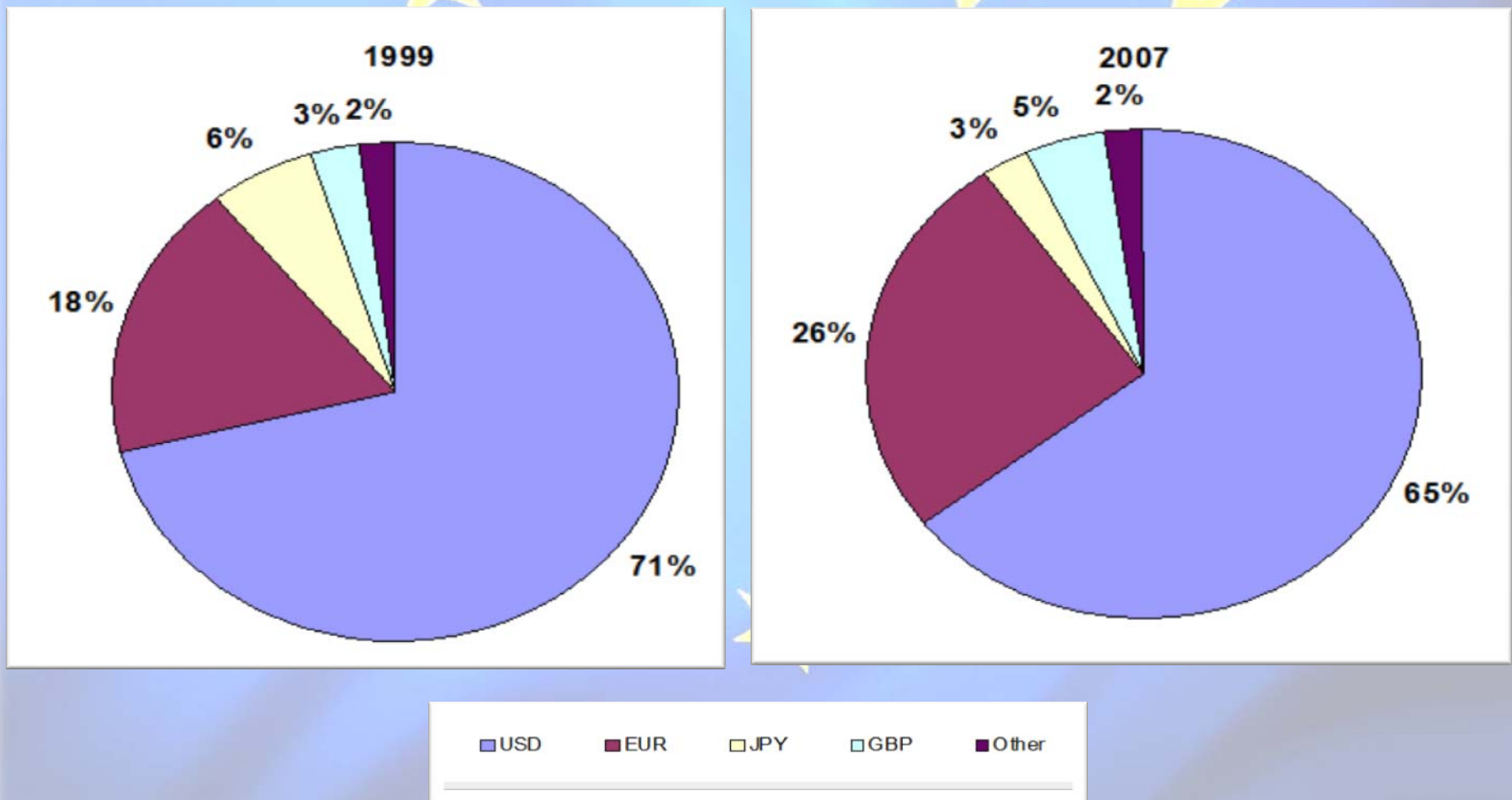
Financial markets

- ❖ **Financial markets integrated, capital has been flowing freely across borders as exchange rate risk disappeared.**
- ❖ **Risk sharing contributed to better synchronisation of business cycles.**



The global role of the euro

Currency shares in foreign exchange reserves



Enlargement has worked

From 11 to 16 in a decade

- ❖ *Greece in 2001*
- ❖ *Slovenia in 2007*
- ❖ *Cyprus and Malta in 2008*
- ❖ *Slovakia in 2009*

Euro area is not a closed-shop.

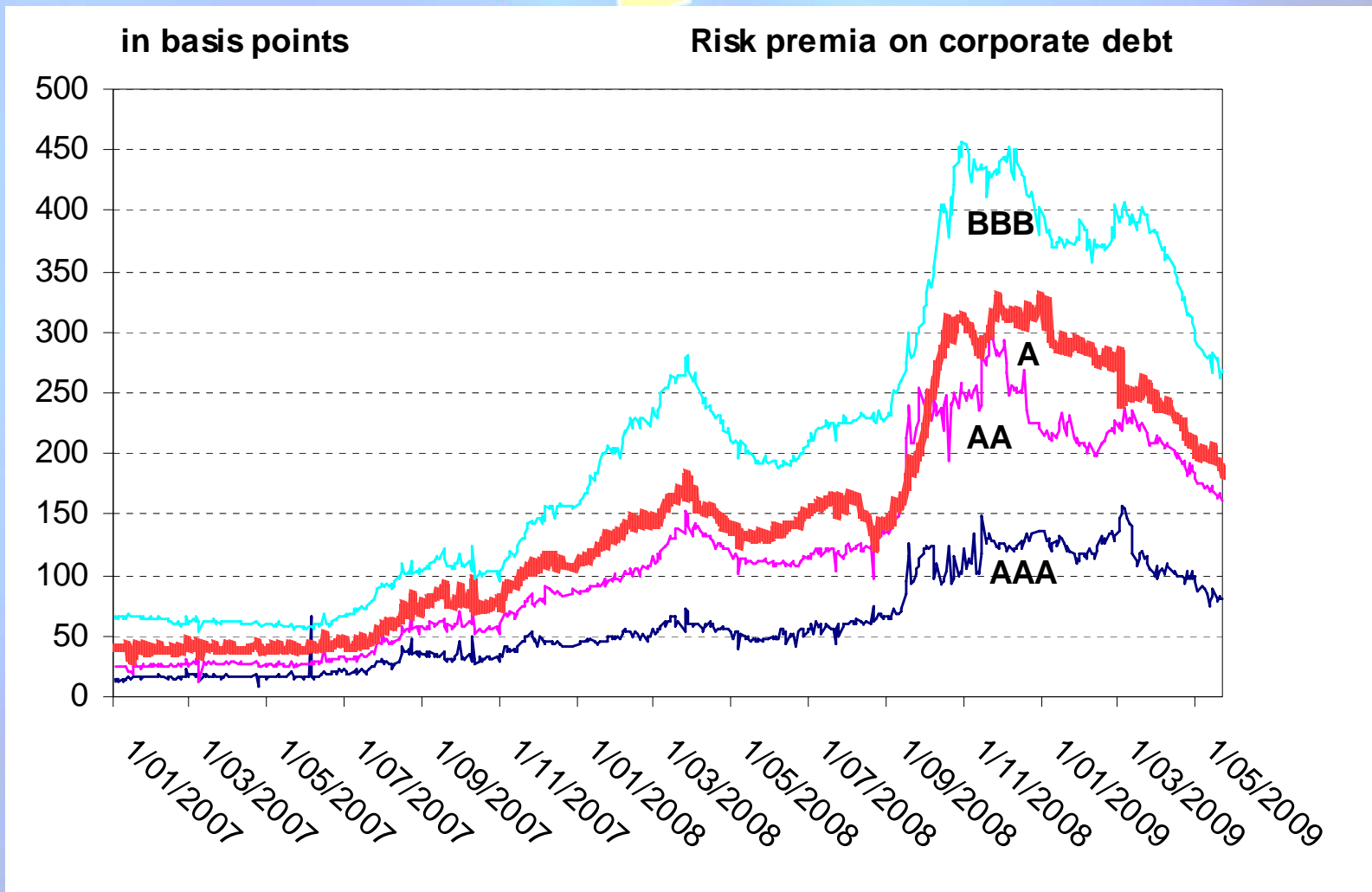
The background of the slide is a stylized representation of the European Union flag, featuring a blue field with twelve yellow five-pointed stars arranged in a circle. The text is centered over this background.

Current and future Challenges

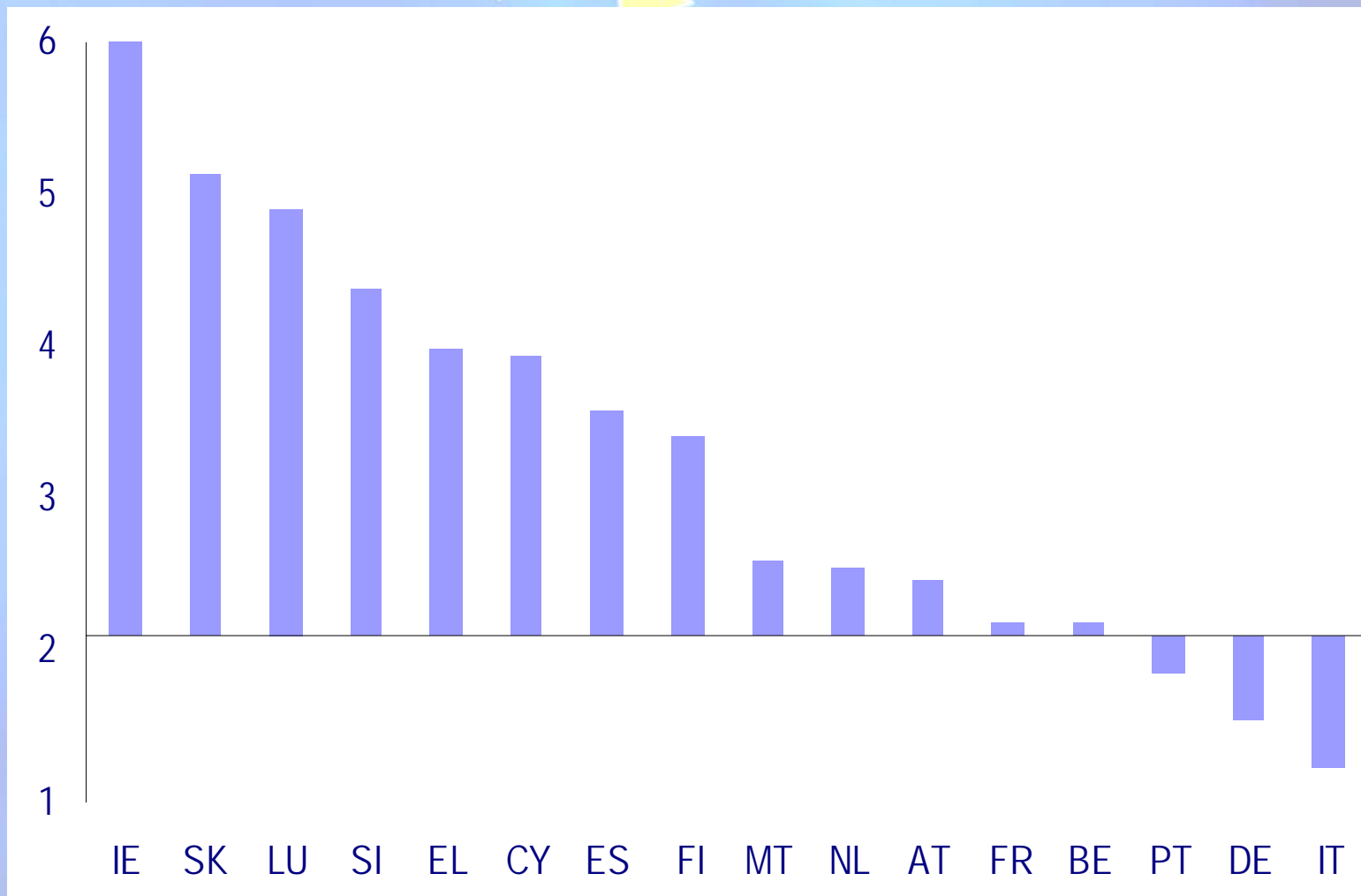
A benign first decade

- ❖ **Macroeconomic stability helped by the ‘great moderation’**
- ❖ **Favourable supply conditions (new technologies, globalisation)**
- ❖ **Supportive financial conditions, accommodative monetary policies, financial innovation**
- ❖ **Fiscal windfalls associated with booms in real estate and other asset markets**

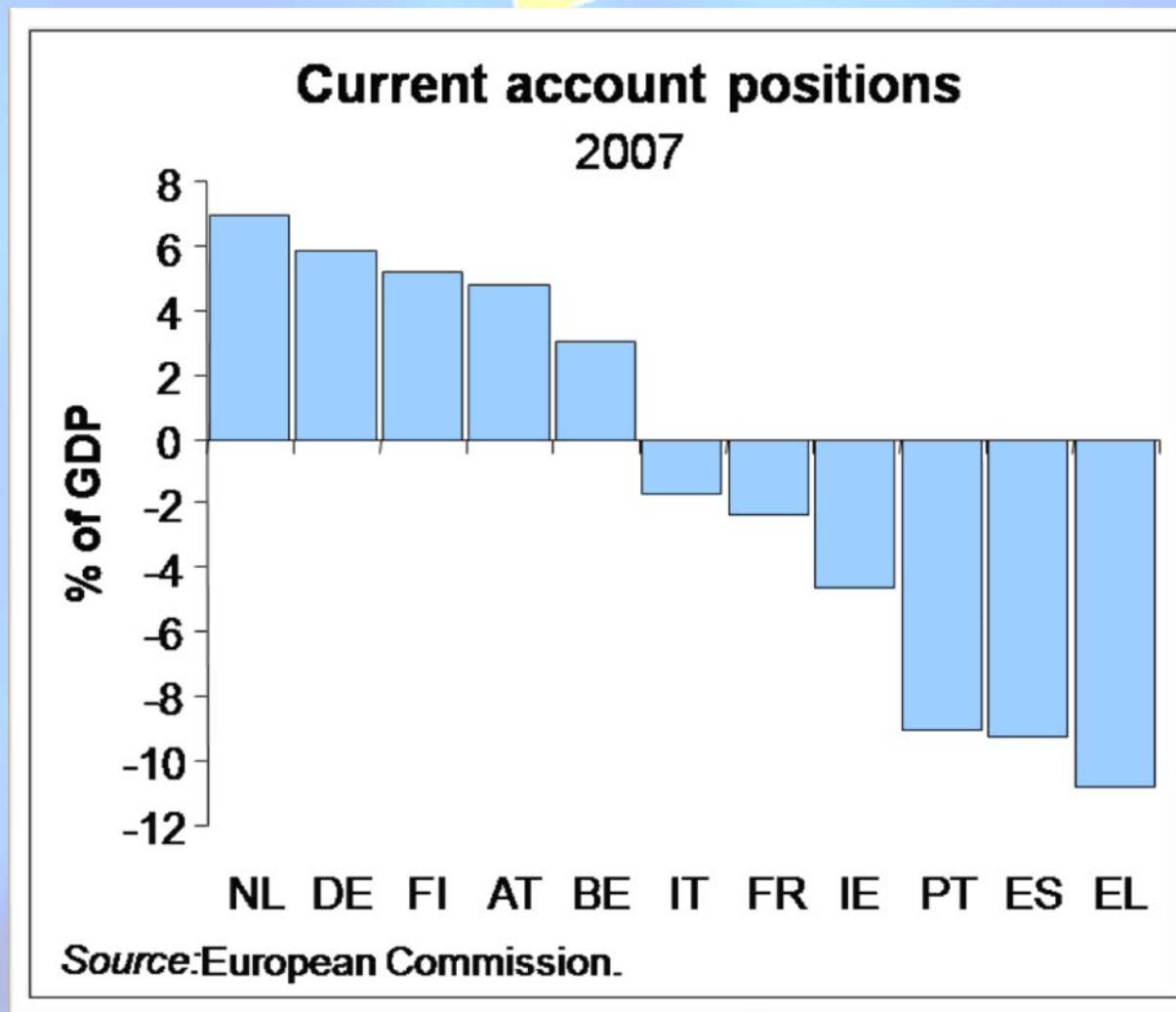
... came to a sudden end worldwide



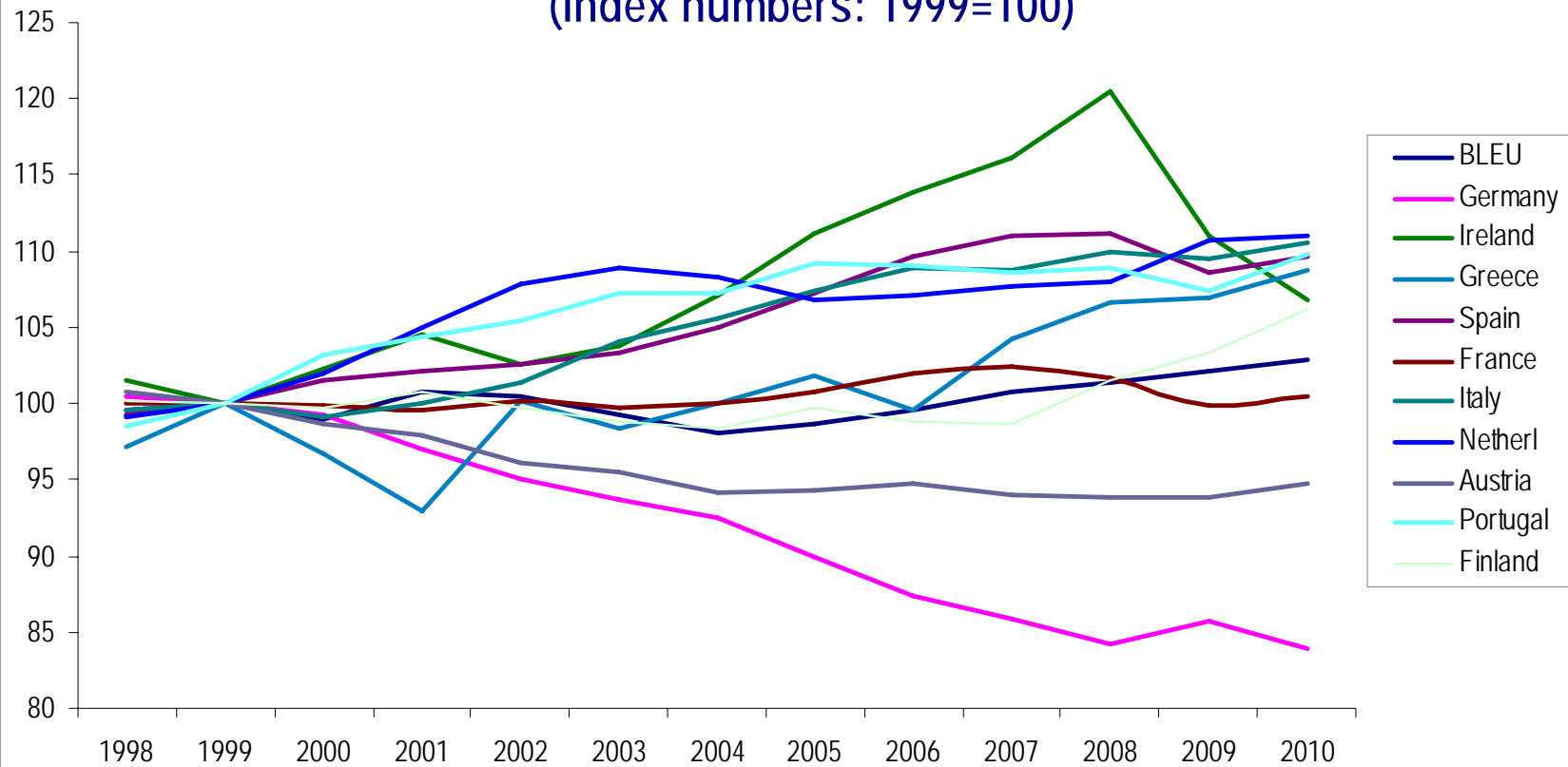
Average real GDP growth (relative to the euro-area average, in %, 1998-2008)



Large current account imbalances



Competitiveness: Real Effective Exchange Rate* vis-a-vis rest of euro area MS (index numbers: 1999=100)



Source: European Commission, May 2009

* Deflated with united labour cost

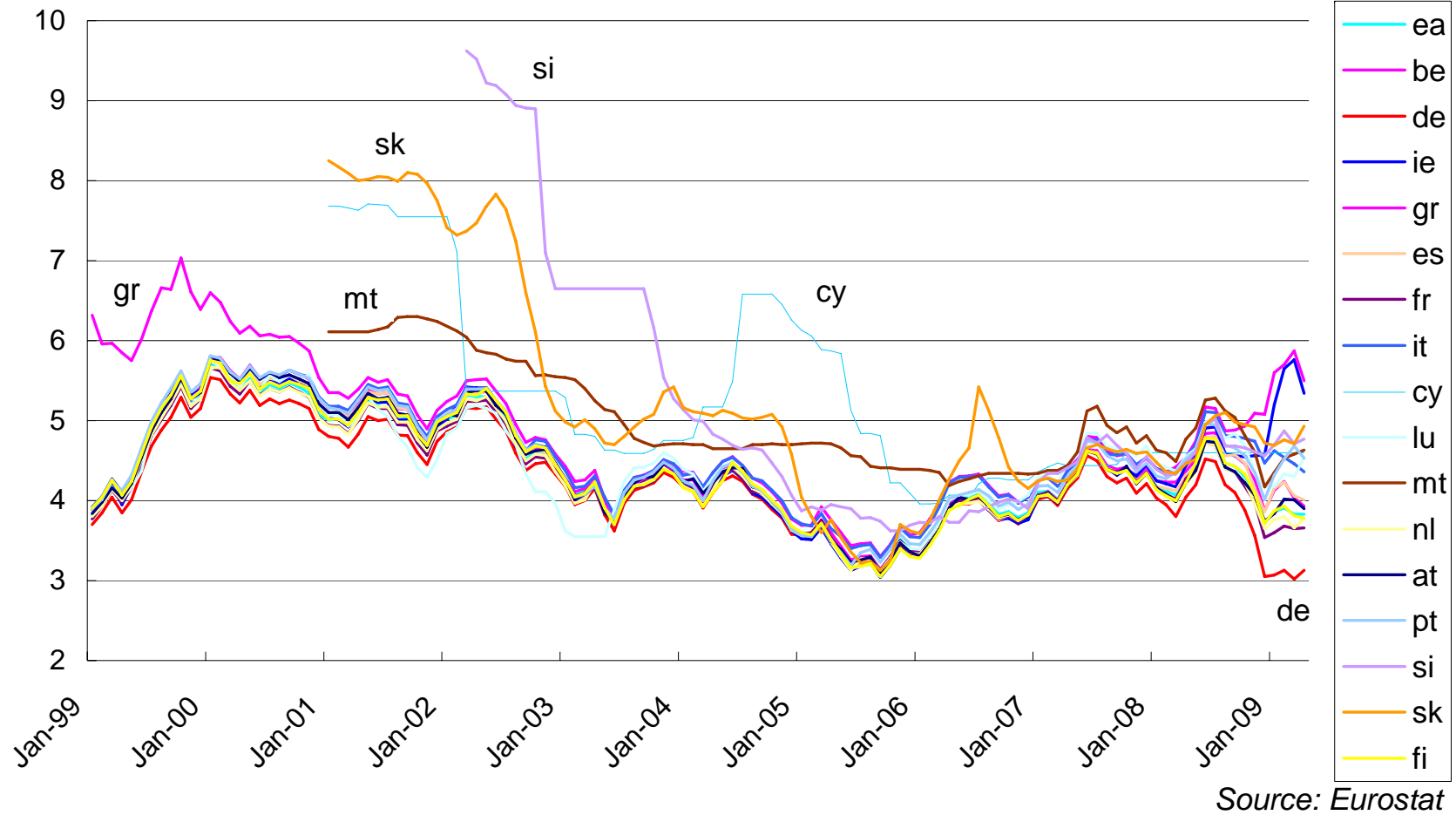
Public finances hit hard by downturn

Government balance (% of GDP)

	2007	2008	2009	2010
Belgium	-0.2	-1.2	-4.5	-6.1
Germany	-0.2	-0.1	-3.9	-5.9
Ireland	0.2	-7.1	-12.0	-15.6
Greece	-3.6	-5.0	-5.1	-5.7
Spain	2.2	-3.8	-8.6	-9.8
France	-2.7	-3.4	-6.6	-7.0
Italy	-1.5	-2.7	-4.5	-4.8
Netherlands	0.3	1.0	-3.4	-6.1
Austria	-0.5	-0.4	-4.2	-5.3
Portugal	-2.6	-2.6	-6.5	-6.7
Slovakia	-1.9	-2.2	-4.7	-5.4
Finland	5.2	4.2	-0.8	-2.9
Euro area	-0.6	-1.9	-5.3	-6.5

Source: European Commission, May 2009

Euro area: 10-year Government bond yields



10-year Government Bond Yields

	Average 2004-08	Average 2008	22 June 2009	Spread Vis-à-vis bunds
Greece	4.11	4.80	5.28	182
Ireland	3.99	4.50	5.68	223
Italy	4.20	4.66	4.58	112
Portugal	4.15	4.52	4.44	98
Spain	4.00	4.38	4.24	79

Source: Commercebank, European Commission

Preliminary Conclusions

- ❖ **First decade of EMU very successful**
- ❖ **But: EMU not a magic solution for all problems**
- ❖ **Accumulated imbalances need to be tackled
... that can be painful**
- ❖ **If necessary, euro partners would provide financial assistance**
- ❖ **Benefits of EMU far bigger than cost**
- ❖ **Enlargement and deeper integration more likely than break-up**

The background of the slide is a blue field with twelve yellow five-pointed stars arranged in a circle, characteristic of the European Union flag. The text "Lessons for Asia?" is centered in a bold, dark blue font with a slight drop shadow.

Lessons for Asia?

Big Differences between Asia and Europe

- ❖ **Economic situation**
- ❖ **Geography**
- ❖ **Culture, religion**
- ❖ **Political systems**

But ...

Objectives for integration are the same in Asia and Europe

- ❖ **Peace**
- ❖ **Growth and jobs**
- ❖ **Crisis management**
- ❖ **Shape globalisation**

Step-by-step approach also in Asia

- ❖ **Trade liberalisation**
- ❖ **Chiang Mai Initiative**
- ❖ **Multilateralised swap arrangements**

What Next?

- ❖ **Single Market in ASEAN by 2015**
- ❖ **Closer monetary cooperation?**
- ❖ **Stronger Institutions?**
- ❖ **Which countries will integrate most?**

Conclusions

Deeper regional integration requires

- ❖ **Political will**
- ❖ **Independent institutions**
- **Benefits of integration can be huge**
- **Integration speed will vary**
- **Easier to start with small group**