Economic and monetary union EMU: external aspects

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OBJECTIVE: to provide an initial analysis of the external aspects of the introduction of the euro. SUBSTANCE: given the economic importance of the euro area - whatever its initial size - the introduction of the single currency will also have a significant impact on Member States outside this area as well as on third countries. The Commission's discussion paper presents an initial economic analysis of the likely impact of the euro on developments in the international economy and, more specifically, in the international monetary system. While the analysis outlined the main issues, it was not the intention to reach firm conclusions at this stage but rather to stimulate the debate. According to the European Commission, the introduction of the euro would have several consequences at international level: (1) the euro area: an economic entity comparable to the United States: the euro area (supposing all 15 Member States join) would have an economic and commercial clout similar to that of the US and greater than that of Japan. In 1996, the Union's share of the GDP in the OECD amounted to 38.3%, as against 32.5% for the US and 20.5% for Japan. If intra-Community trade was excluded, the European Union would account for 20.9% of world trade, as compared with 19.6% for the United States and 10.5% for Japan. As a result of monetary union, Europe would possess its own internal market of great economic and commercial importance. The euro bond market should, in fact, become one of the largest financial markets in the world; (2) less sensitivity to international exchange-rate fluctuations: European economies are very vulnerable to fluctuations in the international exchange markets because a great deal of European economic activity is based on international trade (exports account for around 30% of European GDP, against 8% for the US and 9% for Japan). After the introduction of the euro, the corresponding figure for the EU would be about 10%. European companies will therefore be less affected by exchange-rate fluctuations on the world markets; (3) a gradual fall in the international domination of the dollar: the dollar's dominant position has been gradually eroded since the early 1980s, and the introduction of the euro should accelerate this process on three levels: (a) commercial transactions: the euro will represent an attractive alternative to the dollar for trade, especially with the countries of Central and Eastern Europe, the Mediterranean Basin and Africa; (b) central bank reserves: the euro should become a particularly attractive reserve currency; (c) composition of portfolios: between 1981 and 1995, European currencies' share of the world private portfolio had increased from 13% to 37%, while the dollar's share fell from 68% to approximately 40%. This trend should continue with the introduction of the euro; (4) no harsh effects on exchange rates: the document, after considering the impact of the introduction of the euro on the markets, concluded that there would be no excessive or untimely fluctuations in exchange rates. If based on sound economic principles and on an anti-inflationary, institutional framework, the euro would strengthen the stability of the international monetary system; (5) an opportunity to strengthen international macroeconomic cooperation: the introduction of the euro would present an opportunity to enhance international surveillance and coordination of economic and monetary issues with a view to ensuring more stable exchange rates. The document considered the institutional framework on which the euro's exchange rate policies would be based. It discussed, in particular, the responsibilities of the Council, the European Central Bank and the Commission in terms of the various possible forms for exchange relations between the euro and third countries' currencies. The document concluded that the current managed floating system would be maintained. It underlined, however, that certain issues had still to be resolved, particularly the way in which the euro's exchange-rate policy would be defined. The consequences of the introduction of the euro for international bodies, such as the IMF and G7, would also be looked at in detail.