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The Euro

Introduction

The Euro is the currency used in the 19 member states of the EU that have signed up to full Economic and Monetary Union (EMU). People in all of these countries use the same coins and notes and business amongst companies in Eurozone states takes place in the single currency. For many people, the most noticeable benefit is that money does not have to be changed when travelling within the Eurozone. The Euro economy relies on all members cooperating with one another, and obeying the rules of the Stability and Growth Pact (SGP). There has been scepticism about the ability of the Euro to remain a stable currency serving the interests of all its members. Politicians and economists have expressed concern that the different structures of member states' economies might cause the monetary union to come apart at the seams.

History

The idea of having one currency for the European Community was first put forward in the 1970 Werner Report. The idea was then developed as the European Monetary System (EMS). In 1989, member states set the process of Economic and Monetary Union in motion. The Maastricht Treaty (1992) made EMU part of EU law and set out a plan for the single currency to be established by 1999. To be a part of EMU, countries had to meet certain rules. They agreed to keep their exchange rates within bands called the Exchange Rate Mechanism (ERM), and government borrowing and spending had to be kept under control, with low inflation and low interest rates. Finally, in 1998, 11 of the member states agreed to fix their exchange rates together and handed over the power to set interest rates to the European Central Bank (ECB). Three member states – Britain, Sweden and Denmark – stayed out of this final stage of EMU. The Euro notes and coins were launched on 1 January 2002. The Europa series of banknotes will be gradually phased in from November 2015.

All new EU member states have to join the Euro once they fulfil the necessary monetary and budgetary conditions, except Denmark and the UK, which have negotiated an 'opt-out' clause. Greece joined the Eurozone in 2001. Of the new member states that joined the EU in 2004, Slovenia adopted the Euro in 2007, Cyprus and Malta followed in 2008, Slovakia joined in 2009, Estonia in January 2011, Latvia in 2014 and Lithuania in 2015.

Since the Euro was set up, the markets have been cautious about the single currency, especially as many members have failed to stay within the SGP rules. The currency had performed well until a global economic downturn began in 2008. In general, countries worldwide suffered badly. In particular, Eurozone members with weaker economies (e.g. Portugal, Italy and Spain) struggled to repay their debts, which damaged confidence in the Euro. The situation in the Eurozone worsened in 2010 when Greece suffered a financial crisis. Despite initial reluctance, Eurozone countries gave €80 billion worth of loans to Greece. In return Greece had to cut its public spending and allow EU auditors to assess its finances. After concern that other weak Eurozone economies would face similar crises, a European Financial Stability Facility (EFSF) was created to provide loans to struggling Eurozone states. In March 2012 the size of the rescue fund was increased from €500 billion to €800 billion. Ireland will receive a €17.7 billion loan over 2011 and 2012 as part of its bailout package and Portugal will receive €26 billion, to be disbursed over 3 years. The EFSF will contribute a total of €109.1 billion to the second Greek bailout. In 2013 the EFSF was replaced by the European Stability Mechanism (ESM), a permanent crisis mechanism for the Eurozone. However, in 2015 a third Greek bailout was agreed, worth €85 billion, after Greece failed to meet the deadline for a crucial payment to the European Central Bank.

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How does the Euro work?

The idea behind the single currency is that getting rid of national currencies would make the operation of a single market easier. This requires the EU to become what economists call an 'optimal currency area', which effectively operates as one economy. It is the role of the ECB to manage this by attempting to control inflation through setting interest rates and printing money. In this sense, the EMU sees national governments lose monetary power to the ECB.

Euro notes look the same wherever you are in the Eurozone – they come in denominations of 5, 10, 20, 50, 100, 200 and 500 Euros. The coins have different national images on the reverse side. Coins and notes issued in one Eurozone country can be used in any other Eurozone country. The currency was supposed to be regulated by the SGP, but these rules have not been strictly enforced.

Facts and figures

- The Euro is also the official currency in Monaco, San Marino, the Vatican City, Guadeloupe, French Guyana, Martinique, Réunion and Madeira.
- Just over 21% of world foreign exchange reserves are held in Euros, the lowest share in 13 years.

Arguments

For

- The Euro makes trade and travel between Eurozone countries cheaper and easier.
- The Euro creates greater economic stability in the countries that use it because it takes control of monetary policy out of the hands of politicians and gives it to the ECB. This encourages confidence among investors.
- The Euro is a symbol of European identity and a vital part of the process of political integration.

Against

- The Eurozone is not an optimal currency area; the economies that make it up are too different to make the Euro work properly. This could result in more severe unemployment during recessions and more inflation during booms.
- EMU can't work because many members fail to meet the SGP rules. This will eventually create uncontrollable splits.
- A national currency is a symbol of identity: adopting the Euro means symbolically and practically giving up sovereignty.
- The Euro is primarily a political, not an economic, project.

Technical Terms

- ***Eurozone: the nickname commonly used to describe the 17 member states that use the Euro.***
- ***Exchange rates: the ratio in which one country's currency is valued against another.***
- ***European Financial Stability Facility (EFSF): fund set up in 2010 to defend the stability of the Euro area.***
- ***Opt-out: The ability to decline from signing an agreement.***
- ***Optimum Currency Area (OCA): when the benefits of adopting a single currency are greater than the costs of losing monetary and economic independence.***

Links

- http://ec.europa.eu/economy_finance/euro/index_en.htm

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