INSTITUTE FOR

WORLD ECONOMICS

HUNGARIAN ACADEMY OF SCIENCES

Working Papers

No. 112 September 2000

Margit Rácz

RISK FACTORS IN THE ESTABLISHMENT AND RUNNING OF EMU

1014 Budapest, Orszagház u. 30.
Tel.: (36-1) 224-6760 • Fax: (36-1) 224-6761 • E-mail: vki@vki.hu

SUMMARY

Taking a historic view of the preparations for monetary union remains important even after the birth of EMU, because reform of the political outlook of monetary integration created risk factors over the preparatory period that would necessarily persist into the early years of its operation. These risk factors are of two kinds. (i) Reunified Germany will have to find its place and interests within EMU, since it has not actually had time to consolidate its national economy after integrating economically and financially with the five East German provinces. Indeed the coincidence with the process of preparing for and introducing EMU may have impeded the reunification process. (ii) The Community has no clear concept of the further integration and harmonization tasks that the introduction of monetary union requires in the rest of economic policy and politics as a whole. Monetary union can be seen as a last stage in creating a uniform single market. However, it can also be seen not as the end-product, but as a commencement from the macroeconomic point of view. Raising monetary policy to a supranational level cannot leave intact fiscal policy or the whole political sphere in general.

The initial statement to make about national economic policies in the EU in the 1990s is that the challenges of preparing for EMU and the world economic constraints pointed in the same direction. World economic globalization can be said to have helped the introduction of EMU along, since the group of countries preparing for EMU began to address the requirements of globalization in the 1990s. Inflation in all member-countries was radically reduced, budget deficit was kept small, and high-taxation countries began to devise their first plans for cutting tax rates. All these moves were of cardinal significance for the introduction of EMU. It is only a slight exaggeration to say that without globalization, the economic conditions for introducing EMU would never have been met at all.

Although financial equilibrium is an achievement, it is not sufficient alone to win the approval of the international money markets. Foreign-exchange markets see as conditions for a country's economic success rigorous financial policy together with growth and favourable labour-market trends. In these respects, the majority of EU member-countries did not project a favourable picture in the 1990s. Several countries found their employment and GDP growth indicators did not improve with their finances.

Thus, apart from the emergence of a rigorous financial policy as a success factor, the period of preparation for EMU cannot be regarded as fruitful, either for GDP growth or employment. This is self-evident, but the problem appears graver when EU or EMU indicators are compared with American ones. It seems likely from the data that such problems with the economic policies of member-countries have been prolonged, that may be considered as risk factors from the viewpoint of EMU's international success.

The dollar rate of the euro has not been determined by the euro's internal value. The lesson has been that economic performance as a whole is decisive to the trend in the euro's external value. As long as the US economy produces better results in nearly all indicators than the EU 15 or the EMU 11, the euro will not strengthen against the dollar. Two questions can be raised about the external value of the euro in the coming two or three years. Will the longest period of boom in the American trade cycle since the Second World War come to an end in the near future? Will the EU start to catch up with its modernization in the period after 2000?

The interdependence of macroeconomic goals and political stability give issues of unemployment abiding immediacy. It is another question, whether increasing the proportion of part-time jobs outside the social-insurance system can be rendered a stable arrangement by expanding private pension arrangements. If most EU citizens find the transition from a centralized social-insurance system to a private, self-funded system unacceptable, there may be a crisis affecting the whole model of the monetary union. Of course, the change can be seen also as a beneficial alternative. The most positive change in the EU in 1999 was that the development of the capital markets began to speed up. It is almost inevitable in the medium term that new pension-endowment and stock market-linked savings instruments will gain ground at the expense of traditional savings accounts with banks. Here the question is whether the change will be uniformly welcomed in the coming decade in all EMU member-states.

Economic and economic-policy differences may cause various disturbances during EMU's first decade of operation. There is no experience of similar, previous integration formations to go on, so that forecasts are necessarily uncertain about the supranational and harmonization requirements and constraints. The possible harmonization constraints referred to are ones that may derive from tax harmonization or labour-market regulations. This means the task is not simply to maintain equilibrium, but to handle harmonization requirements that involve the detailed income and expenditure sides of the budget. This is not covered by the Maastricht Treaty, but it is raised in practice, so that it has an *ex post* character.

The harmonization tasks concerning the budget have also emerged in a different context. One condition for a successful financial policy is to have cooperation among otherwise separate monetary and fiscal policies, for instance, in attaining the proclaimed inflation targets.

It is very likely that with the passage of time, the stake and role of inflation targeting in ECB monetary policy will radically increase. However, this will become possible only if the mutual information and consultation claims of those responsible for fiscal and monetary policies can be met institutionally without hindrance. EMU today involves eleven separate ministers and ministries of finance. The presidency of ECOFIN rotates every half-year, in line with the EU presidency. In addition, EU monetary policy is shaped by a system consisting of the member-countries' central banks and the common bank of issue. This means in practice that it has to cooperate with eleven banks of issue, and the number will increase with the EMU membership. So the degree to which national fiscal policies can be harmonized with supranational monetary policy, to allow successful inflation targeting, is an institutional question that remains quite open.

An assessment of the tasks mentioned suggests that the monetary union is still not 'ready' institutionally. These problems must be solved, at the latest by the time before the euro takes over money functions in 2002, if EMU is to function properly. The number of unresolved institutional questions must be reduced to a minimum, so that the monetary union can be treated as one of the final achievements of European integration after its three-year operation. Otherwise it will not create the impression of the irreversibility of EMU in the minds of the international financial community. So long as there is thought to be a possibility of returning from EMU to national currencies, international trust in the euro will not improve.

1. INTRODUCTORY REMARKS

The idea of establishing a monetary union featured for a long time in the post-war history of European integration. It emerged at a time when world economic developments were bringing to an end the system of fixed exchange rates pegged to the gold standard and the US dollar. Member-countries of the European Community (EC) set out to fix the exchange rates between their currencies, at a time when fixed rates seemed impossible to maintain in the world economy. This proved impossible in practice in the 1970s, because the oil-price explosion had increased the danger of inflation and imposed varying degrees of inflationary strain on EC members.

Theoretically, it has never been established whether fixing exchange rates within the European integration process is possible, and if it is, under what conditions it is viable, if individual national economies and economic policies continue to exist. Nonetheless, the idea of fixing exchange rates appears at the beginning of the 1970s among the goals of integration, sometimes directly and sometimes indirectly.

Monetary integration historically belongs to an aspect of the European integration process concerned with integrating economic policies, due to the consequences of the market unification. The big objective between 1985 and 1992 was to arrive at a single internal market, which meant in practice establishing the 'four freedoms': allowing microeconomic players free flows of labour, capital, services, and products across national boundaries. A necessary continuation of this is the gradual integration of the macroeconomic system of terms. Because of the microeconomic implications, fixing rates of exchange and establishing a common currency on that basis play a prominent role in the process. The birth of the new currency gives further impetus to market integration, which commences and accelerates with the free flow of capital. Thus monetary union can be seen as the crowning achievement of the single market, since no single market can be fully integrated without it.

As the Economic and Monetary Union (EMU) was being prepared in the 1990s, systematic arguments were put forward, especially in Anglo-Saxon literature, casting doubt on whether a single market necessarily precluded the possibility of national currencies continuing to function. According to this logic, market integration can be deepened just as easily if national currencies are allowed to survive, so that monetary union is superfluous in practice.

Theoretically, neither this statement nor its opposite can be proved conclusively. The European integration process is a historical formation, geographically and historically unique, and as such, it cannot be judged by considerations of efficiency, since there is nothing with which to compare it. The logic of the monetary integration, outlined above, has certainly gained during its development from facts that allowed new interpretations of monetary integration as a whole. The emergence of EMU should be explained rather by the existing set of historical circumstances than inherently, by the logic of the single market.

These historical circumstances can be apprehended in the European processes of the late 1980 and early 1990s. This was the period when post-war power relations in Europe were breaking up and giving way to a new geopolitical constellation. The first and perhaps most relevant element in this for the European integration process was German reunification, from which the concept of monetary union could not be divorced at the beginning of the 1990s. On this historical inherence rests a further assumption: the creation of a monetary union was decided for political motives. To be more precise, it was designed to accomplish the ultimate integration of a reunified Germany into Europe, in a way that became law at the beginning of the 1990s, based on the principles laid down in the Treaty of Rome.

Taking a historic view of the preparations for monetary union remains important even after the birth of EMU, because reform of the political outlook of monetary integration created risk factors over the preparatory period that would necessarily persist into the early years of its operation. These risk factors are of two kinds. (i) Reunified Germany will have to find its place and interests within EMU, since it has not actually had time to consolidate its national economy after integrating economically and financially with the five East German provinces. Indeed the coincidence with the process of preparing for and introducing EMU may have impeded the reunification process. (ii) The Community has no clear concept of the further integration and harmonization tasks that the introduction of monetary union requires in the rest of economic policy and politics as a whole. Monetary union can be seen as a last stage in creating a uniform single market. However, it can also be seen not as the end-product, but as a commencement from the macroeconomic point of view. Raising monetary policy to a supranational level cannot leave intact fiscal policy or the whole political sphere in general.

The first year and a half of EMU have passed without essential problems, which means that the accounts of a successful introduction of the euro can taken as true. From another standpoint, the two risk factors mentioned mean that macroeconomic problems are likely to arise later, during the operation of EMU, in the form of various disturbances. Thus the first year and a half can be seen as a special period of grace, before the deadlocks in decision-making due to lack of economic-policy harmonization emerge and the market players lose confidence. Certainly one cannot extrapolate from the experiences of one-and-a-half years. The weakness of the euro against the dollar may indicate that the monetary union is not wholly incorporated into EU economic policy, so that market confidence in the dollar is matched by suspicion of the euro. This will change only with further moves towards supranational integration in the EU.

Starting from the idea that monetary union forms the last element of the single market, it is apparent first of all that EMU includes only eleven of the 15 EU member-countries (twelve from January 1, 2001). Slightly sarcastically, it might be said that the single market has integrated the EU countries while EMU has merely regionalized them. Of course that only applies for as long as three developed EU members choose to stay outside EMU.

The first short period of EMU operation has not yet provided adequate experience from which to outline future development. However, it may be possible to do so after three phases (including the preparatory phase) have elapsed at the end of 2002.

2. THE EU'S ECONOMIC DILEMMAS IN THE 1990S

The 1990s can be seen as a period in the history of the EU and monetary-policy when priority went to combating inflation. The main aim of monetary policy was stability, and by the end of the decade, this applied to fiscal policy as well. When analysing the system of policy targets, there is no ignoring the fact that this was a decade of accelerating globalization. This coincidence alone might justify seeking a connection between globalization and the emergence of tight monetary policies. To go beyond the logical approach, such policies could also be justified in the EU simply because they were being practised by the overwhelming majority of OECD countries.

The initial statement to make about national economic policies in the EU in the 1990s is that the challenges of preparing for EMU and the world economic constraints pointed in the same direction. World economic globalization can be said to have helped the introduction of EMU along.

The 1990s began for the EC with economic and political changes or developments that had unexpectedly strong impacts. (i) There was the sequence of changes in

Europe, mentioned in the introductory remarks: dissolution of the Soviet power system and directly consequent German reunification. (ii) There was an economic recession that swept through the Community in 1991–3. This was the first such period burdened with grave and lasting economic problems deriving from 'imported' causes. It broke the run of success in establishing the single market. The recession stoked inflation and unemployment, and curbed GDP growth, the trends being manifest to different degrees in all the member-countries. The different degrees of crisis in each country initiated speculation against one currency or another. The semi-fixed exchange-rate mechanism arrived at a point when Italy and Britain withdrew their currencies from the EMS and the ECOFIN widened the intervention exchange-rate band to 15 per cent for the remaining currencies. This was designed to reduce the need to act in defence of currencies under attack from speculation.

The liberalized capital movements and expanded information network led to a situation in which movements of speculative funds became an objective classifier of national economic policies to a degree not seen before. This triggered an unexpected, quite important change within the Community. The 15 per cent intervention band amounted to an admission that the exchange rates of the member-country currencies could not be fixed permanently against each other. This would not have caused trouble if the member-countries had not been preparing to introduce EMU in the 1990s, since monetary union could not be introduced until the exchange rates have been fixed.

A major international assault on first one and then another national currency began in 1995. However, the increased attention of foreign-exchange markets in the Italian and Spanish currencies had political, not underlying economic reasons. The runs began with accusations of corruption were being made and proved against politicians—members and former members of government alike. This demonstrated that international currency markets speculate against events that shake stability, irrespective of whether it is economic or political. The shaking of stability may be interpreted as inherent to the economy, but it may also be construed as loss of confidence in the government in power. Between 1991 and 1995, the challenges that the exchange-rate mechanism faced raised the question whether all the conditions for fixing exchange rates in the course of the decade were present. Their presence, under conditions of free capital movements, could have been proved by an absence of speculation. This seems such a rigid, external and objective test that finance ministers and central bank presidents at ECOFIN meetings decided to retain the 15 per cent exchange-rate band until December 1, 1998.

There is no need for better evidence of the impact of globalization. In fact, globalization expectations may even be considered as constraints that have to be observed, because otherwise, speculation becomes inevitable and impervious to traditional economic-policy tools. The acceleration of globalization has brought an acceleration in international capital movements. To the money markets, each country appears as a place of business or set of places of business. Places of business come in two kinds: advantageous or disadvantageous. In advantageous places of business, economic policy is predictable, inflation low and taxation not relatively high, so that continual stability is characteristic in a financial sense. The group of countries preparing for EMU began to address these requirements in the 1990s. Inflation in all member-countries was radically reduced, budget deficit was kept small, and high-taxation countries began to devise their first plans for cutting tax rates. All these moves were of cardinal significance for the introduction of EMU. It is only a slight exaggeration to say that without globalization, the economic conditions for introducing EMU would never have been met at all.

The wave of speculation in the first half of the 1990s did not return. It was therefore possible to introduce monetary union on January 1, 1999 without thinking through the possible disadvantages of ir-

revocably abandoning national exchange-rate policies. Theoretically at least, there are two or more issues worth considering. (i) The two waves of speculation showed that trust in the leading political forces plays a role in the value stability of a currency and the durability of international confidence in it. Problems such as this may arise in any EMU member-country. (Nor need it necessarily be a small member-country. There were examples in the decade of German and French politicians being implicated in corruption.) This problem leads far from purely economic matters, but it has to be mentioned because no step in the integration process that affects national economic policy leaves the political infrastructure unaffected. (ii) Are the member-countries of EMU economically integrated to an extent that renders national monetary policy superfluous? Are there differences of economic development, or between degrees of reform concerning the role of the state, that still call for active national exchange-rate policies? The question may seem theoretical, since national exchange-rate policy has ended with the introduction of EMU, but it is worth raising for at least two reasons. On the one hand, Britain, Denmark and Sweden show no serious intention of joining EMU in a short term. On the other, assuming that Eastern enlargement ensues in the early 2000s, the question of independent national exchange-rate policy for these new members arises.

A marked change in national exchange-rate policies took place in the 1990s, as the rate of exchange increasingly became exclusively a tool of monetary policy and ceased to play an active part in influencing foreign trade. From the viewpoint of monetary policy, the existence of lastingly low inflation created the chance to renounce active exchange-rate policies. With the EU member-countries, which have operated the single market for several years, no sweeping changes can be expected in their internal commercial relations, so that the balance of trade is not exposed to the danger of radical alteration. However, it is less certain whether inflationary trends can be permanently avoided under EMU. One serious problem with inflation these days is the trend in international oil prices. It is interesting to consider whether EMU member-states will all be affected in a similar way by high oil prices. There are several other economic factors of importance to inflation, for instance, the danger of rapid wage growth. Pay claims may vary from country to country. If Ireland experienced a period when its wages rise much faster than the EU, that would not produce a substantial impact on EMU overall, or on the external exchange rate of the euro, since the Irish economy is small. Should the same happen in Italy or France, reinforced with strikes, it could exert serious pressure on the euro. These problems, which endanger supranational monetary policy without being able to influence it, have never been theoretically clarified. Some practical solution will have to be found for cases of emergency, but this leaves EMU susceptible to 'imported' instability.

During the preparatory period for EMU in the 1990s, the issue that led to the sharpest political debates among member-countries was the interpretation of the budget deficit and its probable developments. With hindsight, it can be said that the impact of globalization has left none of the governments of EMU or potential EMU member-countries with the option of treating its budgetary deficit relatively freely. The preparations for EMU were governed by the Maastricht Treaty, which defined four criteria of monetary and fiscal convergence with the dedicated purpose of establishing a system of requirements in which preparing countries could be classed. The statement can be risked that in a number of EU member-countries, the fiscal conditions necessary for EMU membership could hardly have been effective enough in themselves to enforce fiscal-policy discipline, which is sensitive to political pressures. The fact that member-countries finally managed to pursue a rigorous fiscal policy in an internationally authentic way can be attributed much more to globalization than to Maastricht. Again as a globalization constraint, the role of the state in the economy of the EU member-countries has been shrinking,

slowly but surely. This change manifests itself ultimately in a steady fall in the budget deficit. Although the shrinkage of the role of the state is an impact of globalization, this was not obvious in the 1990s to EU governments, and there was consequently serious debate on questions of fiscal discipline, mainly between Germany and the other member-countries. This 'decimal' debate, as it was known, evolved from the Maastricht convergence criterion setting a budget deficit ceiling of 3.0 per cent of GDP. At the same time, signatories had opened a back door in the document by authorizing the European Council to interpret the fulfilment of fiscal criteria. If the current deficit exceeded 3.0 per cent in a country, it might still fulfil the criterion if the Council took into account previous development.

This interpretation allows the conclusion that the financial leaderships of the member-countries did not hold out much hope for the emergence of rigorous fiscal policies and their success. At that time such a picture of future was likely in which soft fiscal policy would take shape and become a lasting feature in certain member-countries. Over the whole period ministers of finance worked hard on designing some regulation that would have impeded the mounting of budgetary deficit with punitive sanctions *ex post*. Developments soundly contradicted expectations. Rigorous fiscal policies emerged even in countries where exactly the opposite feature was traditionally characteristic to fiscal policy. This phenomenon must be considered a serious globalization impact.

In September 1994, a short paper by Wolfgang Schäuble, of a leading politician in the ruling CDU in Germany, gained renown for advocating an 'elite club' within the EU, among other reasons, because of the economic-policy tasks of preparing for EMU. Schäuble called the position of the EU critical and advised a rethinking of the Franco-German relationship along with integration at different speeds. The Schäuble paper provoked heated international disputes because it omitted Italy from the list of putative EMU founder-members. It was evident that the concept was prompted mainly by the disorders in Italian fiscal policy. Of course the Italian government itself did not construe the Schäuble-paper rightly, simply regarding it as a political insult. It became apparent in the debate that several EU member-countries considered entry to EMU a political issue. It could be concluded directly from this that the attitude of member-countries would make the common currency a weak one.

The preparations for EMU were a pressing political problem for Germany. The stability of the Deutschmark was one of the 'mental' pillars of the Federal Republic. An integration measure that replaced it with a dubious currency was publicly unacceptable. Nonetheless, the disputes which broke out between member-countries over the introduction of EMU foreshadowed a weak euro.

Efforts to reach stability goals were manifest in two directions. (i) The number of founding members could have been reduced for stability's sake, but this solution might not be accepted by Germany for political reasons. (ii) There were efforts to create a further document following the expiry of the Maastricht Treaty, to impede increases in the budget deficit with punitive sanctions. This so-called Growth and Stability Pact was accepted after long debates in June 1997, at the EU summit in Amsterdam. There was also a German initiative, put forward for the first time at the beginning of the 1990s, to declare that EMU necessitated the formation of a political union. According to the original proposal, the political union would have been established before the monetary union.

A few trends are abundantly clear from the data in *Table 1*. The budget deficit in the United States was less than in the EU in every year between 1991 and 1995. In some EU countries, the deficit was chronically high, while in others, the deficit steadily declined after the recession. Looking at the twelve countries, there seems to be plenty of foundation for the German fear that the entry of some countries as founder-members of EMU might have inflationary

Table 1
The balance on the budget in EU member-countries and the United States
(% of GDP)

	1981–90	1990	1991	1992	1993	1994	1995
Belgium	-8.8	-5.4	-6.5	-6.7	-6.6	-5.5	-4.7
Denmark	-2.5	-1.5	-2.1	-2.5	-4.4	-4.3	-3.0
France	-2.3	-1.6	-2.2	-3.9	-5.8	-5.6	-4.9
Germany	-2.0*	-2.1*	-3.3	-2.9	-3.3	-2.9	-2.4
Greece	-10.3	-14.0	-13.0	-11.7	-13.3	-14.1	-13.3
Ireland	-8.5	-2.2	-2.1	-2.2	-2.5	-2.4	-2.0
Italy	-11.2	-10.9	-10.2	-9.5	-9.5	-9.6	-8.6
Luxembourg	–	–	2.3	0.3	1.1	1.3	1.6
Netherlands	-5.4	-5.1	-2.9	-3.9	-3.3	-3.8	-3.5
Portugal	-7.9	-5.5	-6.6	-3.3	-7.2	-6.2	-5.8
Spain	-4.6	-3.9	-4.9	-4.2	-7.5	-7.0	-6.0
United Kingdom	-2.3	-1.5	-2.6	-6.1	-7.7	-6.3	-4.6
EU-12	–	–	-4.6	-5.1	-6.0	-5.6	-4.7
United States	-2.7	-2.5	-3.5	-4.5	-3.5	-2.3	-2.0

Source: *Europäische Wirtschaft Jahrewirtschaftsbericht.* 1995.
* West Germany.

effects in the early years. The data would seem to justify leaving out Greece and Italy. It is remarkable how successful the rigorous Irish fiscal policy was compared with the previous decade. On the other hand, the deficit in France showed an increase and then stabilized at a high level. This also deserves attention because the deficit in most countries started to decline then and the trend continued in the following two years.

Based on these data, that positive trend, which consolidated in the last third of the decade, could not have been forecast yet. It is therefore worth considering the factor to which can be attributed a change that led to budget surpluses in several EU countries by 1999. Again, the suspect is the impact of globalization, which was asserted ever more strongly in the second half of the decade. *Table 2* sheds light on the magnitude of the change.

Table 2
The aggregate budget deficit in the 11 EMU member-countries
(% of GDP)

Year	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999
Deficit	4.2	4.5	4.7	5.7	5.5	2.2	4.4	2.6	2.0	1.4

Source: *Deutsche Bank Research Aktuelle Themen 2000.* 03. 03.

The table shows that the budget deficits of the 1990s can be divided into three phases. The first covers the years before the recession and the first year of the recession. The second lasted from 1992 to 1995. The third began in 1996 and persists to this day. Between 1996 and 1997, the deficit as a proportion of GDP almost halved, not fortuitously, since the European Council had decided to elect the 1998 founder members of EMU on the basis of their 1997 economic results. By 1997, all the EU member-countries aspiring to be founders of EMU were busily meeting the convergence criterion for budget deficit, with the help of some cosmetics. The cosmetics meant that lasting success could hardly been expected, although reality has contradicted the gloomy expectations. The situation improved in 1998 and showed a radical change for the better in 1999.

The gradual diminishing of budget deficit in all member-countries was an unforeseen positive turn for the monetary union. Two conclusions present themselves. (i) The main internal financial conditions for launching EMU became favourable. This might allow the conclusion that the start was undisturbed. (ii) Theorists at the time expected a restrictive monetary policy and a soft fiscal policy, but in the event, it was the other way round. It must be emphasized that the equilibrium-seeking fiscal policy of the 1990s conforms with a trend emerging all over the developed world, most probably because globalization was advancing in the world economy.

Although financial equilibrium is an achievement, it is not sufficient alone to win the approval of the international money markets. Foreign-exchange markets see as conditions for a country's economic success rigorous financial policy together with growth and favourable labour-market

trends. In these respects, the majority of EU member-countries did not project a favourable picture in the 1990s. Several countries found their employment and GDP growth indicators did not improve with their finances. These macro indicators are worth surveying. The whole decade of the 1990s will be examined in terms of growth and employment, for reasons of expediency. It is worth observing the trend over a decade, because growth and employment started to improve gradually after the recession of 1991–3.

Table 3

GDP growth in the EU 15 and the USA

	1992	1993	1994	1995	1996	1997	1998	1999
Austria	2.0	0.4	3.0	1.8	1.0	1.2	2.9	2.3
Belgium	1.7	-1.4	2.3	1.9	1.4	3.5	2.7	2.3
Denmark	0.2	1.5	4.4	2.8	2.1	3.1	2.7	1.4
Finland	-3.6	-1.2	4.4	4.2	2.3	6.3	5.0	3.5
France	1.2	-1.3	2.8	2.2	1.1	2.0	3.2	2.8
Germany	2.2	-1.1	2.9	1.9	1.4	1.5	2.2	1.5
Greece	0.4	-1.0	1.5	2.0	2.4	3.4	3.7	3.5
Ireland	4.6	3.7	7.3	10.3	7.8	10.7	8.9	8.3
Italy	0.6	-1.2	2.1	3.0	0.8	1.8	1.5	1.4
Luxembourg	1.9	0.0	3.3	3.4	2.3	7.3	5.0	5.0
Netherlands	2.0	0.8	3.4	2.1	2.5	3.8	3.7	3.5
Portugal	1.1	-1.2	0.8	2.3	2.5	3.5	3.5	2.9
Spain	0.7	-1.2	2.1	2.8	2.1	3.8	4.0	3.7
Sweden	-1.4	-2.2	2.6	3.0	1.7	2.0	3.0	3.8
United Kingdom	-0.5	2.2	3.8	2.4	2.3	3.5	2.2	2.0
EU 12	0.9	-0.5	2.8	2.7	1.6	2.3	2.7	2.3
United States	2.5	3.4	4.1	2.0	2.4	4.5	4.3	4.1

Source: *European Economy Supplement A*. April 1998 and April 2000.

Comparing the United States and EU averages for the whole period, it is apparent that only with one out of the eight data, growth in 1995, does the EU outstrip the United States. (*Table 3*) The conclusion has to be that the 1990s were a period of economic success for the United States, compared with the EU. Furthermore, while financial stability was gradually improving in all EU member-countries, the decade was one of low GDP growth.

Matters are complicated by the fact that the 15 countries cannot be regarded as having similar histories of GDP growth. There were characteristic country differences also during the period of recession, and by the second half of the decade, development prospects were differentiating. Germany, France and Italy had relatively low growth rates between 1995 and 1999, while Ireland and Finland, joined by Spain and Portugal in the last third of the decade, had relatively high annual GDP growth rates in the main. By the end of the decade, there was a fast-developing periphery round a core grappling with growth difficulties. It was as if the constraint of financial equilibrium had placed a bigger burden on Germany or France than on Ireland or Spain. In other words, EU countries with relatively undeveloped welfare systems were better prepared for the challenges of globalization than those with developed welfare systems, which were also those classed as most highly developed in per capita GDP terms.

It is also worth surveying the movements of another macro indicator from the point of view of economic success. The EU 15 averages in 1992–9 seem to show that with some fluctuation, unemployment stabilized at a high level. This is especially obvious by comparison with the same indicators of the United States. These showed a lower level in each year than those of the EU and a lower than the one in the previous year. Thus the rapid rate of GDP growth in the United States was accompanied by improving financial balances and by a rapidly improving employment situation. (*Table 4*)

As with GDP growth rates, EU member-countries evolved differences in their unemployment data. However, when these are analysed, no clear connection can be found with the role of the state or with adaptation to globalization. There are probably traditional, country-specific differences in labour policy behind them. Some countries had characteristically low unemployment rates throughout the decade (for instance Austria and Luxembourg). There were others where unemployment climbed in the first half of the decade and fell rapidly in the second half (such as Denmark, the Nether-

Table 4
Unemployment in the EU 15 and the USA

	1992	1993	1994	1995	1996	1997	1998	1999
Austria	3.6	4.1	3.8	3.8	4.1	4.4	4.7	4.4
Belgium	7.3	8.9	10.0	9.9	9.9	9.4	9.3	9.0
Denmark	9.2	10.1	8.2	7.1	6.2	5.6	5.1	4.5
Finland	13.1	17.9	18.4	17.2	16.0	12.7	11.4	10.2
France	10.4	11.7	12.3	11.5	12.3	12.3	11.7	11.0
Germany	6.6	7.9	8.4	8.2	9.0	9.9	9.4	9.1
Greece	7.9	8.6	8.9	9.1	9.9	9.8	10.7	10.4
Ireland	15.4	15.6	14.3	12.4	12.5	9.8	7.7	6.5
Italy	9.0	10.3	11.4	11.9	12.1	11.7	11.9	11.3
Luxembourg	2.1	2.7	3.2	2.9	3.1	2.8	2.8	2.7
Netherlands	5.6	6.6	7.2	7.3	6.8	5.2	4.0	3.1
Portugal	4.2	5.7	7.0	7.3	7.3	6.8	5.1	4.5
Spain	18.5	22.8	24.1	22.9	22.0	20.8	18.7	15.8
Sweden	5.8	9.5	9.8	9.2	9.8	9.9	8.3	7.0
United Kingdom	10.1	10.4	9.6	8.8	8.3	7.0	6.3	6.1
EU 12	9.4	10.9	11.3	10.9	10.9	10.6	9.9	9.2
United States	7.4	6.8	6.1	5.6	5.4	4.9	4.5	4.2

Source: *European Economy, Supplement A*. April 1998 and April 2000.

lands, Britain and Ireland). The countries that are most problematic in terms of employment policy showed rising unemployment rates throughout the decade and especially in its second half. Most of these are highly developed, such as Germany, France, Belgium and Italy, but they are joined by relatively undeveloped Greece

The data draw attention to the fact that the problems of unemployment in most EU member-countries increased in the 1990s. No really effective remedy for solving EU-level unemployment problems has been found. On a national level, mention is often made of the 'Dutch model', since the 1995 unemployment rate in the Netherlands, which was the highest in the decade, shrank to less than half by 1999, which was a spectacular success in a comparatively short time, and left this small country with the lowest unemployment rate in the EU. The main element of success in Dutch employment policy has been with raising substantially the proportion of part-time employment and home-working. This form of employment is generally coupled with a significant cost advantage for the companies involved, since they avoid paying social-insurance contributions on employees.

The 'Dutch model' did not become a pattern for the rest of the EU member-countries in the 1990s, but other member-states will presumably try to apply some elements of it, adapted to their traditions. It is especially important for the three biggest EMU countries (Germany, France, and Italy) to start steadily reducing their unemployment. This would substantially improve the international rating of the EU economy. High unemployment is seen as a serious risk factor in the medium term, with latent effects on financial stability and social peace.

Thus, apart from the emergence of a rigorous financial policy as a success factor, the period of preparation for EMU cannot be regarded as fruitful, either for GDP growth or employment. This is self-evident, but the problem appears graver when EU or EMU indicators are compared with American ones. It seems likely from the data that such problems with the economic policies of member-countries have been prolonged, that may be considered as risk factors from the viewpoint of EMU's international success.

Throughout the 1990s, warnings were heard from independent researchers in EU countries that there had been insufficient preparation for EMU and its introduction should therefore be postponed. That did not happen. On January 1, 1999, the common currency was introduced, the European Central Bank in charge had already been operating for six months, and prices in all EMU countries began to appear euros alongside the national currency. With that, the monetary union became a practical question, even in the uncomfortable sense that from that day onwards, all unanswered questions would spoil the ability of the monetary union to operate and damage the international reputation of the euro. The eleven EMU members embarked on a course that confronted them with successive further requirements to move towards a supranational system. If these requirements were

neglected any more, there would be a danger of significant losses in the medium term.

3. ONE-AND-A-HALF YEARS OF THE EURO AND THE THIRD PHASE OF EMU

The third phase of EMU is running its course between 1999 and 2002. In this phase, the euro is simply a currency on account and all EMU member-states retain their national currencies. However, the rates of exchange between the euro and the national currencies were fixed on December 31, 1998 and cannot be changed in the period before they are ultimately abolished in 2002. Only the euro has an external exchange rate. Although its functions are limited internally, the euro has been the sole currency for the eleven EMU members' external financial transactions since January 1, 1999. In this respect, there has been no interim period for the operation of the euro. The third phase involves a gradual extension of the euro's role only in its internal functions, while its external functions have operated fully from the outset.

The statement can even be risked that the EU, by introducing EMU, became open towards the rest of the world from a financial point of view. Its fortress character disappeared and it became more vulnerable in this respect.

This vulnerability has been apparent in the dollar-euro exchange-rate movements. The euro exchange rate deteriorated until March 2000, with some fluctuations. Before its introduction in 1999, people in the EU had thought the euro would be a strong, even too strong for some exporters. In the event, it has been just the opposite.

Even in the short time that has passed since the introduction of the euro, two views – which largely contributed to the formation of radical standpoints – aired in the debates on monetary union have been disproved. (i) As mentioned earlier, the greatest danger to the stability of the new currency was seen in the fact that fiscal policy had remained a national prerogative. This would pose a big inflationary danger, since national fiscal policies could hardly be controlled. In the event, the national governments of EMU countries have pursued rigorous fiscal policies since 1997, as a relatively positive effect of unexpected globalization impacts. (ii) It was repeatedly stated that the euro would be a strong currency from the moment of its launch. In the event, although the rise in consumer prices remained below 2 per cent in the EU in 1999, the euro fell steadily against the dollar.

The dollar rate of the euro has not been determined by the euro's internal value. The lesson has been that economic performance as a whole is decisive to the trend in the euro's external value. As long as the US economy produces better results in nearly all indicators than the EU 15 or the EMU 11, the euro will not strengthen against the dollar. Two questions can be raised about the external value of the euro in the coming two or three years. Will the longest period of boom in the American trade cycle since the Second World War come to an end in the near future? Will the EU start to catch up with its modernization in the period after 2000?

The exchange rate of a currency changes according to expectations and trends in the short run and the medium term. In 1999, EU economic performance fell far behind that of the United States, especially in GDP growth and employment terms. The question for EMU is whether the growth prospects will improve and an efficient system for mitigating unemployment evolve after 2000.

The forecasts of several monitoring institutes suggest that the EU and US growth indicators will be similar, while with other overall economic indicators, the gap may narrow too. These may include, for instance, the rate of inflation or perhaps the budget deficit. With the current account, EMU is likely to be more successful, but forecasts suggest that the US will do better in com-

bating unemployment. It is worth surveying a few forecast data for the EU and the United States in 2000 and after. (*Table 5* and *6*)

Table 5
Some macroeconomic indicators for the EMU countries

	1997	1998	1999	Forecasts	
				2000	2001
GDP growth	2.3	2.7	2.3	3.4	3.1
Investment in equipment	4.8	8.9	6.6	8.1	7.6
Unemployment rate	11.5	10.8	10.0	9.2	8.5
Inflation	1.6	1.1	1.2	1.8	1.8
Government deficit (% GDP)	-2.6	-2.0	-1.2	-0.9	-0.8
Government debt (% GDP)	74.5	73.1	72.3	70.5	68.2
Current-account balance (% GDP)	1.6	1.2	0.5	0.4	0.6

Source: *European Economy Supplement A, Economic Trends.* April 2000.

Table 6
Some macroeconomic indicators for the United States

	1997	1998	1999	Forecasts	
				2000	2001
GDP growth	4.5	4.3	4.1	3.6	3.0
Investment in equipment	11.5	15.2	7.6	6.1	4.8
Unemployment rate	4.9	4.5	4.2	4.3	4.6
Inflation	2.3	1.6	2.3	2.6	2.4
Government deficit (% GDP)	-0.9	0.0	0.7	1.3	1.8
Current-account balance (% GDP)	-1.5	-2.3	-3.4	-4.1	-4.2

Source: *European Economy Supplement A, Economic Trends.* April 2000.

According to the forecasts, the main macro indicators for the year 2000 in EMU and the United States were converging, in a change from the ruling tendency throughout the 1990s. This closure of the gap is most spectacular in the forecast rate of GDP growth. In 2001, the value of EMU's growth indicator will surpass the American one for the first time, albeit to a small extent. It is worth noting that in 2000 and 200l, the annual growth rate of investment in equipment in EMU will increasingly surpass the US indicator. Based on these data, it seems that the expansion in the US will ease in the early 2000s, while in EMU, economic activity will pick up. It is also apparent from comparing *Tables 5* and *6* that while growth rates will converge, the inflation rate will remain below 2 per cent in EMU and above 2 per cent in the United States. Another forecast that favours EMU is that the decreasing surplus on the current account in 2000 and 2001 will not turn into a deficit. Meanwhile the deficit on the US current account will continue to increase year by year. However, the government budget began to show a growing surplus in 1998. With the 11 EMU countries, there is an accelerating decrease in the deficit, but the balance remains negative. Finally, the unemployment rate is declining year by year in the EU 11, but it will remain significantly higher than the US rate in 2001.

These partly forecast data are worth studying because, according to the current-account figures, the successful economic development of the US is based on mounting indebtedness. If the objectives accepted in the spring of 2000 at the extraordinary summit in Lisbon are to be realized, the current-account balance in EMU also may begin to deteriorate. There may even be growing asynchronism between US and EMU macro indicators, perhaps from 2001 onwards.

In 1999, the US economy proved to be more attractive to the foreign-exchange markets than the economies of the EU, because 1998 expectations of relatively high GDP growth rates in the latter had been belied. Instead, there were only outstandingly low growth rates, in the light of the performances in previous years, especially in some big EMU countries, with a decisive weight in the average. The optimistic expectations had been based on the idea that introducing EMU would lead to heightened competition, which in turn should have resulted in increased investment and faster GDP growth. There was no such impact, probably because the actions of a minister of finance in Germany drew up unfavourable and uncertain prospects for the business sphere concerning the goals of tax reform. After a personnel change in the summer of 1998, public consultation on tax reform was started much more widely.

The other EU country with a rather low growth rate was Italy. There GDP hardly grew by 1 per cent, due probably to a unique 'stop-go' mechanism, rather than frustrated expectations. Ever tightening fiscal policy caused the growth of the Italian economy to slow. The question remains as to whether the budget deficit will grow again if the growth trend turns round. The EU forecast for 2000 and 2001 suggest that the growth rate will almost double. Nevertheless, the budget deficit, equal to 2.7 per cent of GDP in 1997, will fall to 0.8 per cent by 2001, according to the forecast. The forecast figures show the cessation of the mechanism just mentioned. The constraints of globalization also affect Italy. Another question is what complexion of government will form after various government crises in Italy over the next one or two years. On the other hand it remains unclear whether dynamic growth can occur in conjunction with the structural features of the Italian economy if the rigorous fiscal policy remains unchanged. The Italian rate of GDP growth has indisputably been falling since 1997, the year whose figures decided Italy's admission as a founder-member of EMU. By the end of the 1990s, there was still no sign that the classic 'stop-go' cycle in the Italian economy had ceased.

Perhaps it can be assumed that the impacts of globalization have given budgetary discipline a priority unquestionable even if it triggers social unrest. Certainly restrictions on free capital movements seem unlikely in the EU countries in the medium term. By 2004 or 2005, therefore, a rigorous fiscal policy may become imbedded in Italy, bringing a firm 'stability culture'. The problem with this lies in Italian political history. There remains a possibility that the period of establishing a stability culture will pose the risk of a right-wing populist government taking over. Roughly speaking, this is the period after which solid conclusions are to be drawn about how successful the attempt to make a rigorous fiscal policy a lasting priority in EMU countries has been.

The interdependence of macroeconomic goals and political stability give issues of unemployment abiding immediacy. The question is whether increasing the proportion of part-time jobs outside the social-insurance system can be rendered a stable arrangement by expanding private pension arrangements. If most EU citizens find the transition from a centralized social-insurance system to a private, self-funded system unacceptable (due to lack of tradition or low incomes that make savings unfeasible), there may be a crisis affecting the whole model of the monetary union. Of course, the change can be seen also as a beneficial alternative. The most positive change in the EU in 1999 was that the development of the capital markets began to speed up. It is almost inevitable in the medium term that new pension-endowment and stock market-linked savings instruments will gain ground at the expense of traditional savings accounts with banks. The question is whether the change will be uniformly welcomed in the coming decade in all EMU member-states.

Economic and economic-policy differences may cause various disturbances during EMU's first decade of operation. There is no experience of similar, previous integration formations to go on, so that forecasts are necessarily uncertain about the supranational and harmonization requirements and constraints. Just as the persistent differences between Anglo-Saxon and continental writers on aspects of the single market and its requisite monetary policy will never be reconciled, so there is no defining *ex ante* the optimal harmonization needs in fiscal policies, economic policy and politics in the broad sense.

As mentioned earlier, the greatest theoretical challenge for experts during the preparations for EMU was the fact that fiscal policy would remain within national bounds. This was serious because fiscal subordination to national parliaments precluded preliminary disciplining by applying Community rules to curb a budget deficit. The problem seems to have been solved after all by the effects of globalization.

Nonetheless, the same question can be raised in another context. The possible harmonization constraints referred to are ones that may derive from tax harmonization or labour-market regulations. This means the task is not simply to maintain equilibrium, but to handle harmonization requirements that involve the detailed income and expenditure sides of the budget. This is not covered by the Maastricht Treaty, but it is raised in practice, so that it has an *ex post* character. The adjustment processes dependent on economic policy-makers have typically been reactions not initiatives. Adjustment in the business sphere, on the other hand, is frequently *ex ante* in character, or if it is subsequent, the reaction comes comparatively fast. The slow, *ex post* state responses in the EU are made slower still by the harmonization constraints, which require the standardization of the various forms of adjustment customary in each country. So, just as in the area of tax harmonization, further protracted debates can be expected.

The harmonization tasks concerning the budget have also emerged in a different context. One condition for a successful financial policy is to have cooperation among otherwise separate monetary and fiscal policies, for instance, in attaining the proclaimed inflation targets.

On a conceptual level, the monetary policy of the European Central Bank (ECB) is a mixture of money-supply targeting and inflation targeting. In practice, the ECB shapes the desirable level of the EU consumer-price index for a particular year, although it has only had money-supply targeting available to this so far. The big advantage of money-supply targeting at present is probably that the ECB carries it out independently of the institutions responsible for fiscal policy in each member-country. So clear-cut a division of decision-making responsibilities cannot be established in any other case.

It is still very likely that with the passage of time, the stake and role of inflation targeting in ECB monetary policy will radically increase. However, this will become possible only if the mutual information and consultation claims of those responsible for fiscal and monetary policies can be met institutionally without hindrance. EMU today involves eleven separate ministers and ministries of finance. The presidency of ECOFIN rotates every half-year, in line with the EU presidency. So the degree to which national fiscal policies can be harmonized with supranational monetary policy, to allow successful inflation targeting, is an institutional question that remains quite open.

On strategic and technical questions of operation, the example is usually set to the ECB by the German central bank, the Bundesbank, which provides the money-supply targeting. In hardly any of the last 15 years have the volume of money in circulation and Bundesbank’s target quota been similar in size. The size of the differences make it safe to conclude that the Bundesbank’s money-supply targeting has had little to do with the country’s prolonged period of low inflation. The crux must be something else entirely. There are two possible explanations: (i) the still unshaken prestige of Bundesbank and the international confidence in it, and (ii) the post-war economic policy of the Federal Republic, with its priority for price stability. German financial legislation provided that the current deficit should not increase to any great extent, irrespective of what coalition formed the government. This prevented really strong inflationary pressures emerging from the budgetary side. Even if these pressures had emerged, the Bundesbank would have been equipped to counter it with monetary measures.

These frames are basically different for the ECB. It has not track record yet, so that it is surrounded only by an inquisitive distrust. Price stability is challenged not by one, but by eleven national budgets, not all of them in countries with a culture of stability. Furthermore, money-supply targeting presents a technically much harder task to the ECB than to the central bank of a single country.

ECB monetary policy aimed at price stability is necessarily supplemented by the assumption of a widening international role.

The EU, standing behind the ECB, matches the United States in size and economic weight. That makes the Fed the natural partner of the ECB. The Americans have much more practice with cooperation on monetary and fiscal policy and its implementation is inherently a simpler task in the first place. The EU will therefore have to create clear, smoothly operating institutional relations between monetary and fiscal policies in the longer term.

An assessment of the tasks mentioned suggests that the monetary union is still not 'ready' institutionally. These problems must be solved, at the latest by the time before the euro takes over money functions in 2002, if EMU is to function properly. The number of unresolved institutional questions must be reduced to a minimum, so that the monetary union can be treated as one of the final achievements of European integration after its three-year operation. Otherwise it will not create the impression of the irreversibility of EMU in the minds of the international financial community. So long as there is thought to be a possibility of returning from EMU to national currencies, international trust in the euro will not improve.

The more harmonized fiscal policy becomes and the clearer the way for cooperation between finance ministers and the ECB president, the better supranational monetary policy will operate and be susceptible to prognosis about possible outside effects on the euro. As the result, the ability of the euro to take over functions from the dollar and assume a growing international role will improve.

The ECB is unique among the common EU institutions in pursuing a Community policy independently from the Commission. This also means that supranational monetary policy bears a relationship to national fiscal policies in guarding the value stability of the common currency, while the common budget of the EU is essentially indifferent. Nevertheless, the question will emerge subsequently in a different way. Eventually significant mobilizable reserves will be needed to deal with shocks, and the source will have to be the common budget of the EU. The arrangement will work only if member-countries multiply their contributions to the common budget. It is hard to foresee whether the integration conditions for such funds will appear in the medium term.

The ideal ECB model for the relation of monetary and fiscal policies would be the national, state model, where the bank of issue is independent and there are adequate means of cooperation. The fiscal background from which the ECB is supposed to reach this ideal situation is more than disquieting. Will it be possible to develop an institutional structure that takes account of the state interests of sovereign nations, while allowing harmonized relations to emerge between monetary and fiscal policies?

The operation of the ECB is hindered from within because EU monetary policy is shaped by a system consisting of the member-countries' central banks and the common bank of issue. This means in practice that it has to cooperate with eleven banks of issue, and the number will increase with the EMU membership. It is alarming to imagine 21 or more national banks of issue having a say in the common monetary policy. Perhaps the best institutional conditions for making supranational monetary policy would be for the national central banks gradually to lose their strategic role, so that the ECB took over all the functions for monetary policy-making (such as the monitoring activity, for example). The less the extent to which the conditions of such a change emerge, the slower the ECB will be in its decision-making. Slow decision-making, moreover, increases the monetary-policy hazards faced by the EU.

The institutional problems mentioned in connection with the fiscal-policy background and the functions of national central banks may confine the euro to being a regional currency for the EU countries, with very little international role. This could be decided in the medium term for a long time to come, so that the EU has little time left to resolve its institutional problems. Throughout the history of the EU, national and su-

pranational institutional features have mingled in community policy-making. Development on a supranational level has not led to any reduction in the apparatuses controlling the commanding heights of national economies, either in agricultural policy or trade. The same seems to be happening with supranational monetary policy. All previous community policies were built on the close informal links between the Commission and the national economy management organizations.

Concerning the unsettled fiscal policy background, it seems that the Commission's controlling function over current budgetary balances prevails. The peculiarity of the situation rests with the fact that this controlling has no relevant effect on budgetary processes, only in certain special cases. (Such as in case of a debate on the accession of a country to EMU, which had been left out because of fiscal policy problems.) Thus, in the course of fiscal policy harmonization, there cannot be seen today yet such a strategy in the system of relations between Brussels and the nation sates which would increase the weight of the Commission in the harmonization tasks. (According to the Growth and Stability Pact the punishment may come into effect through such a subtle mechanism, that there is hardly anything to tell about the real role of the community institutions for want of practical experience.) From the present situation such a new type of harmonization may start that results in the strengthening of nation state cooperation outside from the Commission. Of course this is true to the context not the form. The form may even be the ECOFIN. However, the context may be such a direct nation state system of contacts that has no precedent. It would also mean that Brussels' role in the field of supra-nationalized financial policy remained limited. It has to be noted though if tax harmonization accelerates then in this field the traditional functions of the Committee may perform useful and important tasks.

In any case, on the grounds of the present situation the statement can be risked, that in the supra-nationalization process of financial policy nation state sensitivity and hesitation are much more prevalent than they were in case of previous common policies. Nonetheless, in order to play a determinative role in world economy, for EMU as an integration institution, and for the euro as a common currency, it is presumably necessary that on the one hand monetary policy should become institutionally supranational also, and on the other the cooperation of monetary and fiscal policies should become viable in practice on the institutional side. All this has not assumed a form even on the visionary level in the EU. There are considerable fears of the continuation of supranational development in the member-countries. Therefore, it is not possible to express an opinion about the kind of a unique mixture of national and supranational institutions and regulations that are to take shape finally for the sake of the successful financial policy of the monetary union.

In view of the future of EMU it is worth touching on a further question. And this is the chance of the medium term joining of three developed EU member-countries remaining outside of EMU in their own free will. It is Great Britain's entry to EMU that can be considered an essential question at the first place. On the one hand because the British joining would further the Swedish and Danish accession to EMU, on the other hand because in the EU the British set the example of the national monetary policy alternative as opposed to supranational monetary policy.

In Great Britain the joining of EMU is an issue, much rather political and emotional than economic. In the medium term, neither alternative can be considered more likely than the other with respect to British accession. Here two questions are worth raising. One of them is that with the joining of these countries the reduction of budget deficit in the EU may gain momentum. The other of them is that on the level of market relations the cooperation of the business sphere has resulted such an intricate network that, if EMU is successful, it will make the accession of the country to EMU neces-

sary after a certain time. It has to be remembered here above all, that the cooperation between the stock markets of London and Frankfurt is ever tightening. For the British, it will mean a certain type of exclusion, if fiscal policy coordination accelerates in the EU. It has already caused the practical problem that in the cooperation of the eleven central bank presidents the British cannot participate. The British staying outside in the long run will only be economically sensible, if EMU is disadvantageous for the economies of the countries participating. It would be worth avoiding.

The building up of the monetary union will probably not wholly be completed until 2002 due to the size and political sensitivity of the hardships it faces. However, the direction for solution will have to be pointed out. Without this such uncertainties persist in the EU that will not allow the confidence to evolve in the European Central Bank and the euro in the medium term.

* * * * *

REFERENCES

Europäische Wirtschaft Jahreswirtschaftsbericht. 1995.

European Economy, Supplement A. April 1998.

European Economy, Supplement A. Economic Trends. April 2000.

CDU/CSU-Fraktion des Deutschen Bundestages: Überlegungen zur europäischen Politik. September 1, 1994.

Europäische Zentralbank Jahresbericht. 1999.

Frankfurter Allgemeine Zeitung. Various issues.

Deutsche Bank Research Aktuelle Themen 2000. 03. 03, 04. 28, 06. 09 and 06. 23.

Deutsche Bank Research Wirtschaftstrends 2000. 06. 16.

Deutsche Bank Research EWU-Monitor 2000. 04. 27.