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Yves-Thibault de Silguy, European Commissioner for Economic and Financial Affairs

Regular readers of *Inf€uro* will know that the euro involves a great deal more for Europe than a simple change from 11 currencies to 1. It is fundamentally changing the way many companies do business and it is making markets more competitive. In some places, for some products it is already bringing lower prices to consumers. It also requires more discipline from governments, particularly in managing public finances.

In this edition of *Inf€uro*, the Commission has tried to give a broad and comprehensive explanation of how the euro has changed and is changing Europe. We talk to Air France which is already using the euro, we point out how individuals can use it before the arrival of euro notes and coins on 1 January 2002 and we give an easy-to-understand description of how EMU is managed by the EU and its institutions.

Not everything you want to know about the euro is here — it would be impossible to satisfy everybody's curiosity in one edition of this newsletter. But after reading it, I hope you will have found a lot of what you need to know about our new money and its place in your life and the world.

When you read these lines, the Commission presided by Mr. Santer, of which I had the honour to be a member, will have finished its term of duty.

This means that it is time for me to say goodbye and to thank you for having joined your efforts to those of the Commission to create the best possible conditions for introducing the euro.

My friend, Mr. Pedro Solbes Mira, has had a very important role in preparing the European Economic and Monetary Union – he was at the head of the Ecofin Council during the second half of 1995 and to a large extent his perseverance and strength of conviction were what made it possible to adopt the final scenario for the transfer to the euro in Madrid in December 1995. His experience will be a major asset for the success of the EMU and I wish him a very successful new assignment.

2002, is just around the corner. My hope is that the largest possible number of citizens will look to the transfer to the euro with confidence, serenity and enthusiasm.

Graham Bishop - Salomon Smith Barney, Adviser European Financial Affairs

The euro's impact: stronger and earlier than expected

Inf€ ***The euro is expected to force through fundamental changes in Europe's financial markets. Are we beginning to see any of this yet?***

Yes – we are seeing some major changes. The wave of mergers is perhaps the most obvious sign, especially in the banking industry. This is a process of consolidation in anticipation of an expected surge in cross-border competition in which banks will try to use their own domestic deposit base to on-lend. Domestic deposits will always be a cheaper source of funds than borrowing in the other country's wholesale markets.

What was not so easily foreseen is the surge in bond issuance – up 33% from the first quarter of 1998. This has involved a quadrupling of bonds issued by corporations and is very significant. It suggests that European investors are beginning to organise themselves to analyse the credit risk of such bonds. In the past, they might have just taken the easy way out and bought government bonds but the low level of yields is forcing investors to look for better opportunities. This process is also forcing the banks to respond when their best customers are borrowing directly from the financial markets.

Inf€ ***Some people are expressing disappointment at the euro's fall against the dollar, saying this is hardly the performance of a hard currency. Did you expect better than this?***

The euro's fall against a strong dollar has surprised and disappointed most analysts because they were not expecting the US economy to grow so robustly! There are specifically European factors at work. With fiscal policy relatively stable, the European Central Bank (ECB) will probably keep rates low for longer than markets discount. I think the recent slippage of the euro and the rise of oil prices will encourage the authorities to keep rates where they are after the recent 50 basis point cut. Improved prospects for structural reform in countries such as Germany provide a more favourable long-term setting for the euro, although an early euro rebound remains doubtful as interest rate differentials continue to shift in favour of the dollar.

Inf€ ***As someone who is very close to the changeover in the financial markets, has it really been as smooth as claimed? If so, who deserves the credit?***

To the best of my knowledge, the changeover really was smooth – at least in the bond and equity markets. There were some initial problems in the payments systems because some banks had not appreciated the fundamental regime change that had taken place. The old "correspondent banking" model of turning to a bank in the country which issues the money that you are moving really became out-dated on the 1st January and not all banks wanted to recognise that reality. However, these were brief problems and customers should not have noticed any difference.

Credit for this smoothness should be spread widely. The European Commission began examining the detailed practicalities of the changeover in 1994 even when there were widespread doubts about whether EMU would happen at all, let alone cover 11 countries and nearly 300 million people.

After publication of the Commission's Green Paper on practical aspects of the changeover in May 1995, market participants began to take the possibility seriously and suddenly a sizeable number of practical people came forward to give their views on extremely detailed technical issues which had to be solved if the changeover was to work.

(➢ 11)

Jean-Cyril Spinetta, Chairman of Air France

Flexibility, transparency, and productivity:

Air France's three essential factors for maximising the effects of the euro on its commercial strategy

Inf€ ***How has your company gone about making the transition to the euro? Has the transition been completed? What, if any, are your plans for future steps?***

The world's fourth largest international passenger airline, the world's third largest air cargo company, and the world's third largest provider of aeronautic maintenance: faced with the euro challenge, Air France was quick to adopt the voluntary measures of a company with a vision for the future. In 1997, a Euro Project steering committee was formed including all concerned Assistant General Managers under the authority of the General Manager. The Euro Project aims to identify and implement the measures needed to adequately prepare the company for the European currency. For each of our three activities (passenger transport, cargo transport, and aircraft maintenance), we defined a strategy for the transition to the euro. That strategy was then further defined for the different support functions (outstation operations, processing of commercial revenues, purchasing, cash management, accounting, auditing, human resources, legal services, and IT).

Three main plans of action were identified:

- offering clients, partners, and suppliers maximum flexibility beginning 1999 by allowing them to deal with us in euros or in the local currency until 2002;
- adopting the evolutionary dynamics which are best suited to each activity;
- preparing our personnel by providing them with all the information they need, as well as pertinent training. In this manner, 7 000 directly concerned employees were prepared for the euro by 31 December 1998.

The detailed plans of action were implemented with the energy that the deadline necessitated: sales and client-accounting systems and procedures were adapted based on 1998 accounting, and on 31 December, the moment that official conversion rates were announced, they were introduced into the computer systems.

We reached our objective: since 4 January, 1999, we have offered our clients the option of being invoiced and making payments in euros. This service is offered to passengers in all our agencies and at airport desks throughout France and in the ten other countries of the euro zone. Since 4 January, our suppliers too, have had the opportunity to deal in euros if they choose.

As for future steps, all internal management (statistical, budgetary and accounting information, etc.) will make the transition to the single currency as of 1 April, 2001. When coins and bills arrive on 1 January 2002, Air France will be "all euro".

Globally, over 4 years (from accounting year 1998/1999 to accounting year 2001/2002), the company will have spent some 190 million French francs (29 million euros) on preparations, i.e. 0.3% of its annual turnover.

Inf€ ***For an airline such as Air France, the world's fourth largest international passenger airline, to what extent is the introduction of the euro a commercial argument? What strategy have you adopted to maximise the effects?***

Air France makes most of its turnover in euro zone countries. The euro is just one more opportunity to satisfy, even anticipate, our clients' expectations. It was my hope that Air France would make use of all possible means to ensure a successful transition to the euro, guaranteeing the best quality service for our clients while minimising costs. In the commercial sphere, three essential factors gave guided our euro measures: flexibility, transparency, and productivity. *(➢ 11)*

Pause in growth is "temporary" says de Silguy

Although the slowdown in the European Union's economy over the last few months has been sharper than expected, it will be temporary and limited, Yves Thibault de Silguy, the Commissioner for economic, financial and monetary affairs, has told the European Parliament.

He was presenting the Commission's spring economic forecasts, which revise downwards the growth expectations it published last October. The Commissioner acknowledged at a hearing of the Parliament's economics committee at the end of March that a weakening in global demand and a fall in investment in equipment were having a negative effect in the early part of 1999. But these factors would be partially compensated by:

- a 3.5% rise in investment in construction this year, compared to 1.8% in 1998;
- a strong 2.6% rise in private consumption, sustained by low inflation and low interest rates;
- a speed up in public sector consumption, which will grow by 1.7% this year compared to 1.3% in 1998;
- stabilisation and gradual recovery in the world economy.

The key elements in the Commission's forecasts are:

Economic growth: will rise by an average of 2.1% in the EU15 in 1999 (down from the 2.4% forecast in the autumn) and by 2.7% in 2000. Average growth in the 11-country euro area will be 2.2% (2.6% forecast last autumn).

Unemployment: will fall from 10% in 1998 to 9.6% this year and 9.2% in 2000. The number of those in work grew by 1.1% in 1998, the equivalent of 1.7 million new jobs and the highest rate of increase since 1990. A further 2.5 million new jobs are expected to be created this year and next.

Inflation: will fall to 1.3% in 1999, from 1.5% last year. This will be the lowest inflation rate recorded since the end of the second world war. A slight pick-up to 1.6% is forecast for 2000. Nominal wage increases are expected to stay at around 3% this year and next.

Public finances: slower growth and relatively modest efforts by governments to adjust their public deficits means that the average EU deficit is likely to remain as it was last year, 1.5% of gross domestic product (GDP). In the euro area, the average deficit is expected to fall from 2.1% last year to 1.9% of GDP in 1999. On the basis of present policies, the deficit is likely to fall to 1.3% in 2000 in the EU as a whole and to 1.7% in the euro area. The main impetus is coming from falling expenditure, which has been declining as a proportion of GDP since 1993. Government debt as a proportion of GDP, which peaked at 72.8% in 1996, is forecast to fall to 67% in 2000. By 1998, seven member States had debt ratios below the 60% reference point set in the Treaty on European Union.

Growth: annual % change in GDP at constant prices

	1997	1998 (estimates)	1999 Forecasts	2000 (Unchanged Policies)
B	3.0	2.9	1.9	2.5
DK	3.3	2.7	1.7	2.0
D	2.2	2.8	1.7	2.4
EL	3.2	3.7	3.4	3.6
E	3.5	3.8	3.3	3.5
F	2.3	3.2	2.3	2.7
IRL	10.6	11.9	9.3	8.6
I	1.5	1.4	1.6	2.3
L	3.7	5.7	3.2	4.1
NL	3.6	3.7	2.3	2.7
A	2.5	3.2	2.3	2.7
P	3.1	4.0	3.2	3.3
FIN	5.6	5.3	3.7	3.9
S	1.8	2.9	2.2	2.7
UK	3.5	2.3	1.1	2.3
EU15	2.7	2.9	2.1	2.7
EU11	2.5	3.0	2.2	2.7
US	4.0	3.9	2.7	2.2
JAPAN	0.8	-2.9	-1.3	0.5

An adjustment to economic realities

Prompted by regular headlines about its value falling against the US dollar, "is the euro strong or weak?" has become one of the most frequently asked questions about Europe's new single currency over the last few weeks. At its launch, the euro was worth $1.18 and by early May it had gently subsided by around 10%.

This was not a huge variation against the dollar compared to some of the Deutsche Mark's movements against the American currency in recent years. Nor was it a sign of unprecedented weakness – the euro/dollar exchange rate at the end of March was very close to where it would have been in May of last year when the countries participating in the euro zone were announced.

Currency exchange rates go up and down for many reasons – from political upheaval to economic disaster. Although the conflict in the Balkans did not help the euro, the currency had not been subjected to either of these during its downward trajectory in the first months of 1999. Instead, analysts have identified two factors at work: one relates to what is called "economic fundamentals" and the other to expectations among those who buy and sell currencies about the future movements of interest rates on the two sides of the Atlantic.

Economic fundamentals count

"Economic fundamentals" really refer to the condition of the muscles and sinews of an economy at any one time. The most important is its capacity to grow and generate wealth. Since the launch of the euro in January, it has become apparent that the growth expectations of the US and EU economies have changed. Last autumn and winter, it was thought likely that growth in the EU could match or even outrun the US' performance in 1999. Instead, the outlook for the EU has become less promising and that for the US better than expected.

"It appears, therefore, that the recent developments of the euro exchange rate primarily reflect the previously unexpected strength of the US economy," said Wim Duisenberg, the President of the European Central Bank, in March. He added that he did not believe that the euro's current exchange rate hinted at a misalignment with the dollar or at a structural weakness of the single currency.

According to the Commission's forecasts, the US economy will grow by 2.7% this year (the comparable figure for the EU is 2.2%) and 2.2% in 2000 (EU 2.7%). It is this difference in growth prospects for 1999 which makes the dollar and the US economy more attractive for investors.

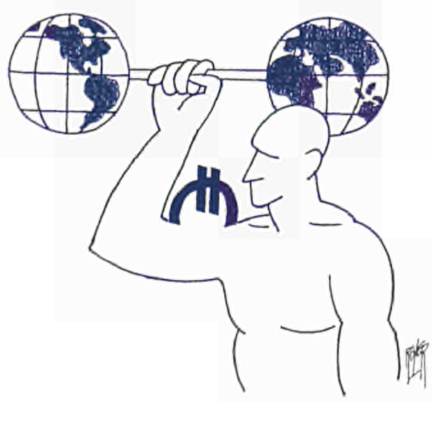
Some analysts think that the euro is weaker than it deserves to be against the dollar because investors and those who advise them have been focusing too much on the recent slowdown in the German economy, the largest in the euro zone, and are not really seeing the picture as a whole. Output in Germany contracted by 0.4 per cent in the last quarter of 1998 and prospects for the year as a whole are an unexciting 1.7% – significantly lower than the outlook for the euro zone as a whole.

Next move for US interest rates may be up

Nevertheless, investors have been impressed by the gap in transatlantic growth rates and have consequently favoured the US currency. They have also been encouraged to do so by other factors. The relative strength of the US economy after an uninterrupted 8-year growth cycle has heightened expectations that inflationary pressures may shortly emerge and encouraged speculation that the next move in American short term interest rates would be upwards. At the same time, signs of unexpected weakness in the EU economy fed a growing expectation throughout the first quarter of the year that euro zone interest rates would be cut – as they eventually were in early April. In normal circumstances, higher rates tend to boost a currency while expectations of lower rates may well weaken it.

Reuters news agency conducts frequent polls of economists on their expectations for the euro. Surveys in March and April showed a consistent majority believing that the euro would recover against the dollar during the course of the year. Their median forecast in early April was that the euro would stand at $1.0700 in one month's time, $1.1000 in three months, $1.1250 in six months and $1.1600 in 12 months. This recovery would be due in part to a pick-up in growth in the euro zone and in part to the belief that the dollar could not maintain its value with the US trade deficit deteriorating so sharply.

The US and European economies are unlikely ever to march together strictly in step. What we have seen in the early part of this year is a fairly normal adjustment of exchange rates to the economic realities. This is desirable so long as it is not accompanied by disruptive and extreme swings. We should get used to seeing the euro move upwards and downwards. There are times when it is not only necessary but helpful to the European economy.



Commission's economic policy guidelines seek sound public finances and reform of markets

The first set of Broad Economic Policy Guidelines for adoption by the European Council since the launch of the euro were recommended by the European Commission at the end of March.

The guidelines are an important part of the economic policy co-ordination and surveillance that has been strengthened on the introduction of the euro. As well as setting the basic strategy for the European Union to achieve its growth and employment objectives, the guidelines also contain specific policy recommendations for each Member State.

Asserting that the first aim of economic policy is to achieve a high level of employment, the Commission proposes a three part strategy:

1. sound macro-economic policies based on well-managed public finances, low inflation and appropriate wage trends;
2. reforms to improve the operation of markets for goods, capital and services;
3. active policies to modernise labour markets, for example by improved training, and measures to boost entrepreneurship and adaptability.

The Commission's recommendations apply to all countries, but some Member States are more particularly affected by certain recommendations than others. The main recommendations are:

Sound macro-economic policy:

- Member States should ensure that they meet the annual budgetary targets contained in their national stability and convergence programmes. This message is addressed at four countries in particular (Italy, France, Germany and the Netherlands). Countries with modest budgetary targets should aspire to be more ambitious and update their stability programmes accordingly (Germany, Italy, Austria, the Netherlands and Portugal in particular);
- Improvements in budgetary positions should be achieved through expenditure restraint rather than tax increases;
- Member States with high levels of public debt as a proportion of gross domestic product need to maintain a high primary surplus, supported by appropriate privatisation policies (Belgium, Italy and Greece in particular);
- Countries should review pension and health care systems to ensure that their public finances can bear the burden of an ageing population (in particular Spain, Italy, Luxembourg, Portugal, Finland);
- Efforts should be made to reverse the decline in government investment (Greece, Spain, Italy) and to ensure that the necessary resources are available for investment in human capital and other active policies to improve the operation of the labour market (Spain, Austria) as well as Research and Development expenditure (Greece, Spain, Ireland, UK);
- Further progress should be made with tax reform (Denmark, Germany, Greece, Austria) and co-ordination to improve incentives for employment and to eliminate distortions in the single market;
- Wage increases should avoid creating inflationary pressures and thus be constrained by productivity gains, taking account of differentials in terms of qualifications, sectors or regions (Belgium, Spain, Italy, UK). Success in this area depends on effective social dialogue at all levels.

Economic reform

- Single market and competition legislation should be strictly applied and monitored in all Member States. Further progress is needed with opening up public procurement (Denmark, Greece, Italy, Austria, Portugal, Finland), liberalisation in the public utilities, telecommunications (France, Ireland, Luxembourg, Austria, Portugal) and transport sectors (Belgium, Denmark, Ireland, Italy, Luxembourg, Netherlands, Austria, Portugal, UK) and strict control of state aids (Germany, Spain, France, Italy, Luxembourg, Portugal);
- The legal and regulatory framework for business should be improved (e.g. relaxing restrictions on retailers in Germany, Denmark, the Netherlands, Austria, Portugal and Sweden or price regulation in Luxembourg). In particular, Member States should set specific targets for reducing barriers and delays to starting up new businesses (e.g. Germany, Spain, Greece, France, Italy, Netherlands, Austria);
- Determined efforts should be made to promote the development of deep and integrated capital markets (Greece, Ireland, Austria, Portugal).

Employment

- In line with the employment guidelines and in the context of the 1999 national plans, employment policies should concentrate on both demand and supply of labour, including more efficient training and education (Ireland, Italy, Portugal), reducing taxes and other charges on low paid workers (Denmark, Germany, France, Italy, Netherlands, Austria, Finland, Sweden, UK) and reviewing the duration and eligibility conditions for benefits (Belgium, France, Italy, Portugal, Sweden);
- Links between unemployment benefit and other benefits should be reviewed to ensure an appropriate balance between work incentives and social inclusion (Denmark, Germany, Italy, Netherlands, Austria, Finland);
- The social partners should be encouraged to take forward discussions on flexible working patterns including part-time working and possible reductions in average annual working time without eroding the international competitiveness of the labour force (Greece, Spain, France, Ireland, Austria, Portugal).

Use and learn is the best strategy

Whether you live in or outside the euro zone, you will have increasing opportunities as a consumer to use Europe's single currency well before it is available in notes and coins from 1 January 2002.

Until then, it will remain a "scriptural" currency – sometimes known as "written money" or "book money". This idea is familiar to most people – the millions of credit card users in the European Union, for example, or the many travellers who use travellers cheques in Europe every year. Each time they use a non-cash method of payment – other methods are cheques, bank transfers and electronic purses – they are using scriptural money.

Since the euro was launched on 1 January 1999, increasing numbers of people have been transacting in the new currency, sometimes without them necessarily being aware of it. One motorway operator in France, for example, has been billing drivers in euro every time they use a credit card to pay the toll. This does not cause any problems for the credit card companies, they as are ready to convert the euro amounts into the currency of the customer's account as they are for any other currency transaction.

This means that it is totally convenient for a tourist travelling in the euro zone to make payments in euro whenever the supplier offers this facility. Hotel, restaurant and other charges are immediately comparable once they are expressed in euro, rather than in the different currencies of each country. So management of the holiday budget becomes very much easier without having to make complicated conversions from one currency to another.

There is also another very practical advantage: the more you use the euro, the more quickly you learn its value and what it will buy. At the moment everybody's frame of reference for prices and values is their own national currency.

This frame of reference will fade away once euro notes and coins are put into circulation on 1 January 2002. Shops and supermarkets will still be showing prices in both euro and national currencies for a short time. Nevertheless, learning through use is the best strategy for everyone who wants the final changeover to be as easy for them as possible.

When can I use the euro?

On all occasions when the shop, hotel, bank or any other service provider is prepared to accept the euro, although they are not obliged to do so before 1 January 2002. During the so-called "transition period" (1 January 1999 to 1 January 2002), use of the euro is governed by the principle of "no compulsion, no prohibition". Generally speaking this means that no one can be forced to use or accept the euro, but nor can they be barred from doing so if two parties to a transaction agree.

Using the euro: a checklist

How can I use the euro?

- **Travellers cheques:** increasingly, issuers are making these available in euro. They can be used for paying for goods and services and for exchanging into the national local currency units of the euro.
- **Credit cards and payment cards:** these can be used to make payments denominated in euro. The credit card company will convert them into the currency in which the card holder usually makes his or her repayments.
- **Bank cheques:** not everyone will want to use cheques because it may be difficult to find a bank ready to handle a normal cheque if the account is in another country, even if written in euro. Cheques written on a euro account at a bank in a euro zone country should be acceptable within that country. But there are exceptions and some operators are not planning to handle cheques in euro before 1 January 2002.
- **Electronic purses:** before long it will be possible in many countries to load an electronic purse with euro at a bank and to replenish it electronically at automatic teller machines.

How does Economic and Monetary Union work?

EMU's objectives: stable prices, sound public finances, growth and employment
Economic and Monetary Union is organised and managed according to the conviction that stable prices and sound public finance are much the best basis for creating economic growth and job creation. These principles underpin the institutions, laws and practices that operate EMU.

Stable prices are assured by the balance between the monetary policy of the European Central Bank (ECB) and the budgetary policies of the Member States. Price stability was set as the ECB's primary objective by the Treaty on European Union. The ECB decided last December that price stability is being achieved if price rises move in the range of 0-2%. Its operation of monetary policy aims to secure price stability through the raising or lowering of short-term interest rates. The ECB's policies are also designed to support the EU's broader economic objectives such as higher rates of economic growth and job creation provided that price stability is not put in jeopardy.

Sound public finances are required by the Treaty and the procedures for achieving them are set by the Stability and Growth Pact. Low budget deficits help to keep short-term interest rates low and also favour the lowest possible long-term rates that are good for investment. Budget discipline reduces the burden of public debt and frees government money for long-term policies supporting growth and employment.

Securing the objectives: detailed surveillance and co-ordination; preventative action; dissuasion. Surveillance and co-ordination is required to ensure that Member States' economic policies support the common price and budget discipline objectives and also address other issues that might threaten the smooth functioning of EMU.

The procedure begins each year with:

- **The Annual Broad Economic Policy Guidelines** adopted every summer by ECOFIN after their endorsement by the European Council of heads of state or government. These recommend the priorities for Member States' macroeconomic policies including budget policies and policies affecting markets for labour, products and services. The Commission closely monitors Member States' policies and economic performances to make sure they are in line with the guidelines.
- **Preventive action** is needed to ensure that the economies of Member States continue to converge through policies directed at growth and stability objectives.
- **Stability programmes** are submitted by members of the euro zone towards the end of the year – pre-in countries send in "convergence programmes" which are very similar. Member States are required to table plans for achieving balanced budgets or budget surpluses in the medium-term so that they have room for manoeuvre in an economic downturn without breaching the 3% of gross domestic product ceiling on deficits set by the Stability and Growth Pact. The Commission gives an opinion on each plan which forms the basis for ECOFIN's judgement and policy recommendations to the Member States.

Dissuasion is part of the procedure designed to ensure that Member States do not breach the 3% of GDP ceiling on budget deficits. If it is apparent that significant slippage from targets is taking place, the Commission reports to the Council which can then issue a recommendation to the Member State concerned to take the necessary adjustment measures. A Member State may face sanctions if, after ten months, it is still failing to fulfil its commitments on budgetary discipline. The sanctions, initially taking the form of a non-interest-bearing deposit, may be avoided in exceptional circumstances, such as a severe economic downturn or a natural disaster.

The 1998-99 Timetable

May 1998	Commission proposes Broad Economic Policy Guidelines
June 1998	ECOFIN submits Guidelines for political endorsement by European Council
June 1998	European Council endorses the Guidelines
July 1998	ECOFIN formally adopts the Guidelines
1 January 1999	EMU is launched
November 1998-January 1999	Member States submit their Stability and Convergence Programmes
December-February 1999	Commission issues its opinion on the programmes
January-March 1999	ECOFIN examines the Programmes and issues recommendations
March 1999	Commission issues draft Economic Policy Guidelines for 1999-2000

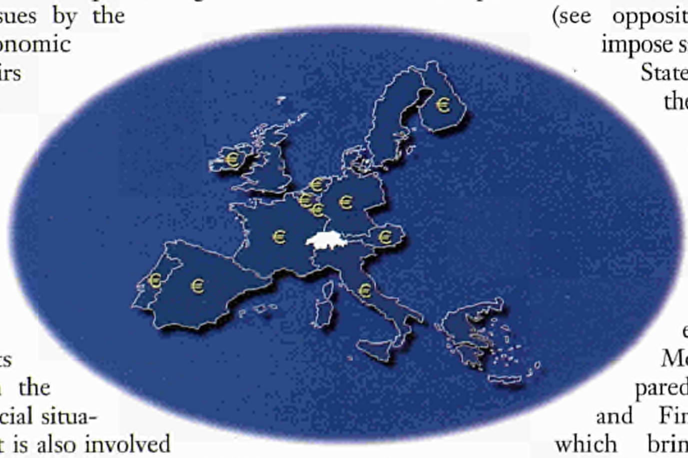
Who does what in EMU? The role of the European institutions

To run smoothly, the European Monetary Union (EMU) needs good and efficient co-operation between the EU's various institutions. Each has a special part to play in a process designed to deliver better prospects for economic growth, job creation and stable prices than there were in the era of national currencies.

The European Parliament – ensuring accountability

The European Parliament has the key responsibility within the EMU decision-making process for the democratic scrutiny of the European Central Bank (ECB), whose independence is guaranteed by the Treaty. The Parliament is consulted on appointments to the Bank's Presidency and Executive Board.

After the first nominations were announced by the European Council of heads of state or government in May 1998, Mr Wim Duisenberg, the ECB President, and his five colleagues on the Executive Board were subject to close questioning on a range of policy issues by the Parliament's Economic and Monetary Affairs Committee. The President gives testimony to the committee four times a year on the Bank's conduct of monetary policy.



In addition to its regular debates on the economic and financial situation, the Parliament is also involved in the passage of legislation related to EMU, and is consulted by the Council when it has to decide whether a Member State can qualify for membership of the euro area.

The Council

The Council acts as a sort of management board of EMU and in this function is normally made up of the Member States' Economic and Finance Ministers, which is why it is known as the "ECOFIN".

However, heads of state or government sit as a formal Council when they are deciding whether a Member State can adopt the euro. When they meet twice a year in the European Council they also give direction and impetus to economic policy in the EMU. Of particular importance are the conclusions the European Council draws every June, based on recommendations from the Commission, about the broad economic guidelines which Member States should follow. These provide a yardstick against which to judge whether their policies are pulling in the direction of commonly agreed objectives.

The Council is also responsible for more detailed aspects of economic policy. After receiving the Commission's opinion, ECOFIN has to decide whether Stability Programmes submitted every year by Member States in the euro area conform to the disciplines of the Stability and Growth Pact (see opposite). It would also impose sanctions if a Member State had failed to respect these disciplines.

The Council also keeps an eye on the euro's exchange rate and may fix the orientation or general approach to exchange rate policy. Most of its work is prepared by the Economic and Financial Committee which brings together two Commission representatives and officials from the European Central Bank and the Treasuries and central banks of the Member States.

The Euro 11

This is not a Council in any legal sense but an informal gathering of the Economic Affairs and Finance ministers of the 11 Member States participating in the euro area. The purpose is to debate, discuss and to exchange information so as to improve understanding and policy co-ordination between the participants. The Commission and the European Central Bank usually take part in these meetings which precede the regular monthly meetings of ECOFIN. However, ECOFIN remains the decision-making body.

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The European Central Bank

Formally constituted on 1 June 1998, the ECB is the European Union's newest body, wholly independent and a central pillar of Economic and Monetary Union.

Together with the 11 national central banks (NCBs) of the participating Member States, the ECB is part of the European System of Central Banks (ESCB) whose statutes set maintaining price stability as its primary objective. The ESCB's basic tasks include defining and implementing monetary policy for the euro area, conducting foreign exchange operations and holding and managing the official foreign reserves of the Member States. It has also to promote the smooth operation of payment systems and contribute to the work of the relevant national authorities in supervising credit institutions and the stability of the financial system.

The ESCB is governed by the decision-making bodies of the ECB :

- the Executive Board, comprising the ECB President, the Vice-President and four other members. The current President of the ECB is Wim Duisenberg, Christian Noyer is Vice-President and the other four Executive Board members are Eugenio Domingo Solans, Sirkka Hämäläinen, Otmar Issing and Tommaso Padoa-Schioppa;

- the Governing Council, which meets twice a month and comprises the members of the Executive Board and the governors of the NCBs of Member States participating in the euro area;

- the General Council, which meets less frequently than the Governing Council, is made up of the ECB President and Vice-President and the governors of all Member States' NCBs, including those not participating in EMU.

The European Commission

The Commission has a broad range of responsibilities for managing and safeguarding EMU, including its primary role as the initiator of legislative proposals and the guardian of the Treaties.

The Commission's main tasks are to:

- propose every year the broad guidelines of economic policies to be pursued by Member States and the European Union;

- support the close co-ordination of economic policies and multilateral surveillance by reporting to the Council on economic developments in each Member State and whether they are consistent with the broad guidelines. The Commission reports to Parliament on the results of multilateral surveillance;

- ensure respect for the rules of the Stability and Growth Pact. The Commission monitors Member States to make sure they are meeting their obligations on budget deficits and medium-term budgetary objectives. It reports to the Council when it thinks an excessive deficit is threatening or has occurred and makes recommendations for action by the European Council and ECOFIN;

- report to the Council on whether Member States qualify for the euro area and issue recommendations on whether or not they should be admitted.

Graham Bishop - Salomon Smith Barney, Adviser European Financial Affairs

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Inf€ ***Was agreement within the financial services industries on what needed to be done really as broad as it seemed?***
The Commission's Directorate-General II started the "Giovannini Committee" to act as a focal point for the professional associations and to see what legislation might be needed. The European Monetary Institute – the forerunner of the ECB – was then hard at work on its preparatory tasks and acquiring a reputation for professionalism which acted as a spur to the private sector.

At the heart of Europe's financial markets, the City of London played a leading role in providing detailed technical work under the leadership of the Bank of England. Many people were surprised by this role – given the UK's non-participation in EMU – but the City's vital commercial interests were at stake. Failure to handle the changeover would have been a commercial disaster.

No single body deserves all the credit for the smooth changeover. It was an incredible team effort that spanned Europe and may have been a bit disorganised at times – but there was no precedent at all and often it was not clear who (if anyone) had the legal right to "decide" on a course of action. The only solution was to create such a wide consensus that everyone agreed to the new "convention" whether it had legal force or not.

Inf€ ***What do we know about the use of the euro in financial markets? Is it living up to expectations?***
The financial markets changed over to the euro completely, at least as far as the wholesale markets are concerned. This was exactly as expected –– and intended – and there is virtually no trading in the old legacy currencies.

Inf€ ***Since the launch of the euro, has anybody had cause to revise their view about the impact on the City of the UK staying out of EMU?***
In the short run, the role of the City has probably been reinforced by the surge in bond issuance as perhaps 70 % of all (including dollars, etc.) bonds are issued from City-based trading desks. Prime Minister Blair made clear, when launching the UK's National Changeover Plan, that the basic intention is to join EMU and bond yields are consistent with UK participation around 2002. At present, there seems little need to start making serious contingency plans for a scenario in which the UK is permanently out.

Jean-Cyril Spinetta, Chairman of Air France

(≺3)

- **Flexibility :** each agent may, when requested to so by the client, express values in local currency or in euro. If they wish, clients may settle in euros by credit card (all of our payment terminals having been adapted by January 1999) or with a euro check.
- **Transparency:** we are looking to accompany our clients in developing a new monetary reference. For that reason, we have decided, for example, to print the exchange value in the other currency on the passenger receipt.
- **Productivity:** the tools adopted for the arrival of the euro have been adapted to allow our agents to work in two currencies in a single country, without increasing the time it takes for processing and thus without affecting the quality of the service to the client.

Inf€ ***To what extent do your trading partners, clients, and suppliers use the euro? Does that degree correspond with your expectations?***
Globally, the degree of use of the euro remains rather moderate, which, at this stage, is exactly what we were expecting. It is over the next 18 months that the euro's growth will have to be watched very closely.

Our hypotheses predict varying speeds of transition to the euro depending on the type of client and the market.

At present, individual travellers' use of the euro is declining somewhat, after being rather fashionable at the beginning of the year.

For cargo and aircraft maintenance, which are business-to-business activities, we expect quicker transition to the euro, however. Air France Cargo, for example, has already concluded a number of agreements with clients for invoicing in euros. In fact, all players in the air cargo sector are registering tremendous interest in the single currency and have decided to shift to the euro as quickly as possible, country by country. The 'France' market, in agreement with the French society of air cargo agents (SNAGFA), began quoting rates in euros at the beginning of the year, and the majority of transactions are made in the single currency. Other "in" countries should soon be following.

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The € charms

Early assessments suggest that the euro has proved to be a far more popular currency in the international capital markets than expected.

According to data provider Capital Data BondWare, by mid-April international bonds denominated in euro accounted for 44.39% of all issues since the start of the year, fractionally behind the US dollar's 44.71% share. The balance is made up by other global currencies, principally sterling, the Swiss franc and the yen.

Total issuance of euro-denominated bonds reached 227 billion € in the first quarter, up 33% from total volumes in the predecessor national currencies at the beginning of 1998. Total bonds issued by companies were four times higher than last year.

Analysts say that to some extent the euro-issuance has been benefiting from a generally strong demand for corporate bonds among investors. But they also say that European companies have been anxious to take advantage of low current interest rates which are giving them access to relatively cheap funds. This being so, the 0.5% cut in official interest rates by the European Central Bank in early April is likely to make the euro-denominated bond markets even more attractive to companies.

These developments confirm the Commission's own expectations of recent years that lower average interest rates, more liquid financial markets and opportunities for companies to finance themselves at lower costs in these markets would all prove to be strong benefits of Economic and Monetary Union.

Heads or tails

The Luxembourg national face of the euro coins

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