



## PARLIAMENTARY DIMENSION



### **Background Note**

#### **Session 3**

#### **Twentieth anniversary of the Euro: achievements and future of the Euro**

With the participation of Ms Christine Lagarde,  
President of the European Central Bank

#### **COSAC Chairpersons' Meeting**

Paris, 14 January 2022



## Session 3

# Twentieth anniversary of the Euro: achievements and future of the Euro

### *I. The resilience and successes of the euro*

The Euro entered into force on 1 January 1999 and was put into circulation on 1 January 2002. Today it is the official currency of nineteen of the twenty-seven Member States of the European Union (Germany, Austria, Belgium, Spain, Finland, France, Greece, Ireland, Italy, Luxembourg, Netherlands and Portugal (1999); Slovenia (2007); Cyprus and Malta (2008); Slovakia (2009); Estonia (2011); Latvia (2014); Lithuania (2015)). The euro corresponds to the third phase in the achievement of Economic and Monetary Union (EMU).

In practice, the structural balance of the EMU is based on two distinct pillars:

- Firstly, a single monetary policy, entrusted to the European System of Central Banks (ESCB), made up of the European Central Bank (ECB) and the central banks of the Member States concerned. Its primary objective is to guarantee price stability. Without prejudice to this objective, the ESCB provides support for general economic policies in the European Union, with a view to contributing to the achievement of the objectives of the European Union. The independence of the ECB is explicitly provided for in the Treaty on the Functioning of the European Union (TFEU),<sup>1</sup> as is the ban on the ECB granting overdrafts or any other credit.<sup>2</sup>
- Secondly, within the euro area, fiscal and economic policies remain national and are the responsibility of the Member States, subject to the procedures for coordinating said policies provided for by the Treaties (see below).

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<sup>1</sup> Article 130 of TFEU.

<sup>2</sup> Article 123 of TFEU.

In order to ensure minimum convergence after the creation of the euro, two tools have been put in place:

- the Eurogroup, a multilateral exchange and supervisory body bringing together the finance ministers of the Member States of the euro area, whose existence is distinct from that of the ECOFIN, a specialised formation of the Council bringing together the ministers of all the Member States;
- the Stability and Growth Pact (SGP), which includes:
  - a preventive arm, whereby each Member State must present its medium-term fiscal objectives in a stability programme updated each year;
  - and a corrective arm, which provides for the triggering of an excessive deficit procedure (EDP) when a State exceeds the public deficit criterion set at 3% of GDP, except in exceptional circumstances (there is also an excessive public deficit when debt exceeds 60% of GDP). The ECOFIN then issues a recommendation to the State concerned, so that it corrects this situation and, if it does not correct its deficit within the allotted time, the Council can take sanctions against it (financial deposit with the ECB which can be transformed into a fine, ranging from 0.2% to 0.5% of its GDP).

In 2008, the euro area suffered the consequences of the “subprime crisis” imported from the United States. Member States were forced to support their weakened banks and were in some cases unable to finance themselves due to the lack of a lender of last resort. The crisis therefore became a sovereign debt crisis and the euro area as a whole was threatened with dissolution.

However, the euro area paradoxically emerged from this crisis stronger with:

- **enhanced coordination of the economic policies of the Member States**, in particular with the European Semester and the entry into force of the Treaty on Stability, Coordination and Governance (TSCG), also known as the “Fiscal Compact”, on 1 January 2013, which requires Member States to comply with a “fiscal golden rule”, according to which the fiscal position of general government must be balanced or in surplus;

- **the establishment in 2012 of a permanent body for financial assistance to countries in difficulty in the euro area, the European Stability Mechanism (ESM)**, with an initial lending capacity of €500 billion out of a capital of €700 billion, making it possible to release funds quickly to come to the aid of a Member State in order to avoid its default and spread of the latter throughout the euro area;
- **the gradual establishment, from 2014, of the Banking Union**, based on three pillars: a single supervisory mechanism, a single resolution mechanism and, in principle, a harmonised deposit guarantee system, which, however, still remains under discussion today.

Thus, whereas several economists and politicians had repeatedly announced the "death of the euro" or the division of the euro area, **the single currency and the euro area have "shown remarkable resilience" in overcoming this crisis, the most serious in Europe since the end of World War II.**

**For twenty years**, the euro has been the single currency of an **economic zone which today represents 85%** of the European Union's GDP and is the **world's largest trading zone**. In practice, the euro is used daily by more than 300 million citizens. An entire generation of young citizens of its Member States has never known any other currency. As the euro has generally been synonymous with lower transaction costs, stability and increased trade, a large majority of European citizens consider the euro "a good thing" for the European Union (80%) and for their country (70%).<sup>3</sup>

For companies, the adoption of the euro, by removing the costs associated with foreign exchange transactions in the euro area,<sup>4</sup> has offered greater security to their activities and more outlets, while facilitating their search for financing and their investments.

**The euro has also become an international benchmark currency.** Even outside the euro area, the single currency is used for transactions, as a store of value and a benchmark currency. Several examples:

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<sup>3</sup> Flash survey Eurobarometer 488 on "the euro area" (Spring 2021), survey carried out by telephone interviews with 17,723 people.

<sup>4</sup> « The Euro: How a Common Currency Threatens the Future of Europe », Joseph Stiglitz, 2016.

- at the end of December 2020, at least €167 billion were in circulation in banknotes outside the euro area;<sup>5</sup>
- at the end of 2019, 20.6% of global foreign exchange reserves were held in euros (for a value of \$11,076 billion). However, the dollar's share in these foreign exchange reserves (around 60%) has remained unchanged;
- several states outside the euro area have pegged their national currencies to the European currency. Others have even adopted the euro as their official currency (Andorra; Monaco; San Marino; Vatican; Montenegro).

## **II. The remaining challenges**

**In the short term**, the priority for the euro area is to emerge from the crisis caused by the Covid-19 pandemic, while the situation is not under control. In the spring of 2020, the pandemic indeed imposed an unprecedented halt to economic activities and strict movement restrictions for several months, which caused the worst recession ever experienced by the euro area (-6.8% in 2020), before a real but fragile recovery of the economies.

Drawing lessons from previous crises, **the European Union's fiscal authorities provided a rapid, effective and coordinated response** to this growth shock: activation on 20 March 2020 of the general exemption clause of the Stability and Growth Pact intended to allow governments to temporarily deviate from the objectives of the Pact (until the end of 2022) and adoption of a **Recovery Plan for Europe** at the European Council from July 17 to 21, 2021. This plan provides for an investment of €750 billion (comprising €390 billion in loans and €360 billion in grants) by the end of 2026.

This recovery plan, as the creation of the European Instrument for temporary Support to mitigate Unemployment Risks in an Emergency (SURE) and the possibility of benefiting at advantageous conditions from ESM credit lines, constitute major advances in European solidarity.

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<sup>5</sup> Source : Eurosystem.

For its part, **the ECB vigorously intervened to support the economy of the euro area from the start of the crisis and the stance of its monetary policy has since remained very accommodating**, because, as stated by Christine Lagarde, president of the ECB, “*extraordinary times require extraordinary action. There are no limits to our commitment to the euro*”.

In practice, the ECB has allocated an additional €1,970 billion to the overall envelope of its asset purchase programme (i.e., 17% of euro area GDP in 2019), including €1,850 billion for the Pandemic Emergency Purchasing Programme (PEPP). It has also authorized new targeted refinancing operations and kept its key interest rates at a historically low level.

The ECB is pursuing this policy while containing a surge in inflation which appeared with the economic recovery, due to external factors (increase in the prices of energy and food products).

At the same time, the euro, like the dollar, is being challenged by the technological advance of China, which is developing a digital yuan capable of giving this currency international influence. The ECB indicated in November 2021 that it would launch a prototype digital euro in 2023 after a two-year exploratory phase, in order to respond to the growing dematerialization of payments and the proliferation of cryptocurrencies.

In addition, European companies have been subject to sanctions of a considerable amount by the American authorities since the beginning of the 2010s for transactions they had carried out in dollars. The strengthening of the international role of the euro could constitute an element of response to this extraterritoriality of sanctions which hinders the development of European companies.

**In the longer term, the priority is to reduce economic divergences between euro area Member States, which, over the course of the crises, have not only persisted but have even been deepened.** In a September 2021 study, the OECD emphasises these differences in economic trajectories, public debt and the functioning of labour markets, and therefore considers it

"crucial to increase fiscal integration to reduce the divergence of economic cycles and strengthen the stability of the euro area in the event of a shock".<sup>6</sup>

### **The euro area therefore remains a work in progress today**

Although they agree on this assessment, Member States remain divided on the most pertinent solutions to remedy it. The main suggested avenues are as follows:

- **a simplification of the current European fiscal rules**, sometimes "considered complex and unreliable";<sup>7</sup>
- **the establishing of a euro area budget**,<sup>8</sup> with some States considering it a simple instrument to support investments and reform projects, others wishing to make it a permanent fiscal stabilization mechanism,<sup>9</sup> which would take the form of the **creation of a European unemployment reinsurance scheme** in the form of repayable loans, vis-à-vis national systems, in the event of a large-scale shock;
- **the consolidation of the Banking Union**, on the one hand, by setting up, via the modification - in progress - of the treaty establishing the ESM, of a "backstop" to supplement the Single Resolution Fund if necessary, and, on the other hand, by setting up a European Deposit Guarantee Scheme (EDGS), which remains to be established.

These developments would imply a strengthening of the economic governance of the euro area and increased democratic control of the latter by parliamentary means, for example through the establishment of a euro area parliament, comprising members of parliament from the national parliaments concerned.

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<sup>6</sup> OECD Economic Surveys of the European Union and Eurozone, September 2021

<sup>7</sup> Report "Reconciling risk sharing with market discipline: A constructive approach to euro area reform", joint press release of fourteen Franco-German economists, January 17, 2018

<sup>8</sup> Proposal of the Meseberg declaration of 19 June 2018.

<sup>9</sup> For example: Report "Towards a Genuine Economic and Monetary Union", a.k.a "Four Presidents' Report" (Van Rompuy ; Barroso ; Juncker ; Draghi), European Commission, 5 December 2012 ; Report « Completing Europe's Economic and Monetary Union », a.k.a "Five Presidents' Report"(Juncker ; Tusk ; Dijsselbloem ; Draghi ; Schulz), European Commission, 22 June 2015.



### **Questions for discussion:**

- Twenty years after its creation, what is your assessment of the euro for your country - whether it is a member of the euro area or not -, for the euro area and for the European Union?
- How do you view the action of the ECB, including the use of "unconventional measures"?
- In your opinion, should the euro area move today towards greater coordination of the economic policies of its members? If so, according to what mechanisms?
- How to simultaneously improve parliamentary control of the functioning of the euro area?
- How to strengthen the international role of the euro?