

# The euro

by Richard Corbett MEP

Almost all of the other Member States of the EU now have a common currency – the euro - or have committed to joining as soon as they are ready. Why did they conclude that a single market needs a single currency?

## Arguments in favour

### Eliminating hedging costs

Selling to a client using a different currency involves contracts that are vulnerable to changes in exchange rates. It's like working with metres that could change in length or kilos that could change in weight from one week to the next.

Companies therefore have to 'hedge' (insure) against exchange rate fluctuations. This costs firms billions of pounds a year and is growing every year as more and more trade is conducted across internal European Union borders. A single currency eliminates such costs within our principal market.

### Eliminating conversion costs

Simply converting from one currency to another involves a cost of anything up to 5% every time you change. Again, this is a burden on companies, especially small and medium-sized businesses, who pay about £3bn a year. But it is also an expense for individual citizens as tourists.

### Stability

Over the years we have suffered from currency fluctuations. Exchange markets tend to 'overshoot' when adjustments are made, causing currencies to be overvalued or undervalued. Having the same currency within the European market eliminates that problem within that area, and since the majority of all EU countries' trade is within the EU, this is a significant improvement.

### Transparency of competition

Using the same currency throughout the single market will allow consumers to compare prices more easily (and everyone to compare benefits, wages, pensions etc.).

### Releasing money tied up in currency reserves

The EU states maintained currency reserves to defend their own currencies, partly against each other. With a single currency, they need just one common set of reserves, to defend the currency with respect to the rest of the world. Since smaller amounts are needed, assets are released to more productive purposes.

### A share of the world's main currency

As Europe's share of world trade is greater than America's, the euro will in due course replace the dollar as the main denomination for world trade. At present, many of our production costs rise and fall with the value of the dollar, as commodity prices are fixed in world markets in dollars. Our costs therefore fluctuate according to events in the American economy that have nothing to do with our suppliers nor with our own economy. This advantage that the Americans currently enjoy, of having world commodity prices fixed in their own currency, will be transferred to Europe.

### **Less scope for speculators**

A single market with free circulation of capital, but with fifteen different currencies changing in value, is a speculator's paradise. They cause changes in exchange rates to 'overshoot', creating instability. The attempt by governments to counter them through the halfway house of the Exchange Rate Mechanism proved costly and ineffective. The problem disappears with a single currency.

## **Where does this leave Britain?**

To these seven main reasons for giving the single European market a single currency, we can add the reasons which now arise for the UK as a result of being outside the single currency now that it has been set up by our partners. Staying out means losing out - not just in respect of the above but also...

### **In terms of sovereignty**

Outside, we have no influence over major economic decisions which are in any case going to impact on us. Inside, we have a powerful voice.

### **In terms of our competitive position**

As UK companies are alone within the EU in having to bear hedging and conversion costs, Dutch, Irish, French, German etc. companies now have a competitive edge over our exporters within the Euro area. Nearly 60% of our exports go to the EU and over 3 million jobs depend on them.

### **Fluctuations**

Caught between the dollar and the euro, the pound is particularly vulnerable to international exchange markets. Joining the currency used by our largest market would give us absolute stability vis a vis that market. The recent high level of the exchange rate of the pound against the euro, which has contributed to the loss of over 200 000 manufacturing jobs since 1977, would disappear.

### **Lower interest rates**

If we joined, UK interest rates would at last be able to fall to the European average, stimulating investment and providing cheaper mortgages.

### **Inward investment**

There has already been a dramatic fall in the level of inward investment coming to Britain. There is also a risk of already established companies moving to a euro-zone country (see recent statements by Mathmos, Vauxhall, Toyota, Mitsubishi, Peugeot, Renault, Ford and others).

## **Arguments against**

There are, of course, arguments against joining the single currency. But many of them don't stand up to scrutiny.

### **"We would lose our traditional currency"**

The pounds and new pence of the 1990s bear no resemblance to our traditional pounds, shillings and pence which we dumped in the early 1970s. There is nothing "traditional" about our currency, other than the name 'pound'.

One side of euro coins is left for national symbols, such as the Queen's head. But even the Queen's head on our notes is a recent addition, dating from the early 1960s, and not used in Scotland.

### **“A single currency implies a political union and a common identity “**

The UK and Ireland shared a single currency until the late 1970s, but this didn't mean that they were a single country, and there was certainly no political union. Belgium and Luxembourg did the same, as do many other groupings around the world. Sharing a currency does not mean you lose your national identity.

### **“We will no longer control our economy”**

Jointly deciding on monetary policy gives us a greater chance of resisting international pressures. And other instruments of economic policy making, remain in the hands of national governments: notably fiscal policy and public investment.

### **“We lose control of our currency to Germany”**

In fact, the opposite is true! When the Deutsch Mark was the strongest currency in Europe, we all had to adapt to decisions taken by the German Bundesbank in the German interest. With a single currency, all member states have a say in decisions about a jointly-owned currency.

### **“The single currency will be run by bankers”**

Just like the Bank of England, the European Central Bank is a publicly owned bank, not a private one. Its Governors and Board are appointed by elected governments and must report back to them and to the European Parliament.

It is an independent bank in the same sense that judges are independent of politicians in their day to day decisions, but must nevertheless apply the decisions in light of the legislation and economic policy laid down. It is, in other words, the same system as the one we already have in Britain with the Bank of England.

### **“A one-size-fits-all interest rate is not suitable for diverse economies”**

We already have this problem within the UK, where interest rates often reflect the interests of the South East and the City of London rather than the needs of the manufacturing North.

The problem would be no worse at EU level - it might even be better, with interest rate decisions less bound to the interests of a single financial centre. In any case, the convergence of economic cycles and of inflation rates achieved within the Euro area have considerably lessened this problem. The Chancellor's five economic tests include an assessment as to whether the UK and euro economies have converged sufficiently to avoid this being a problem. We will only join when it isn't.

### **“Joining means we would have to cut public spending”**

There is nothing whatsoever in the Treaty provisions on monetary union that impose any limits on public expenditure. Member states are free to choose their own levels of public spending. Indeed, most have far higher levels (and often better public services) than Britain.

What the treaty does limit is public deficits (ie financing expenditure by borrowing instead of taxing), where governments should not run “excessive deficits”. What is excessive? The treaty provides for an evaluation of the situation in any country where the deficit is more than 3% of GDP – well above the current level in the UK.

Even then, allowance must be made where it is for investment or is deliberate counter-cyclical spending. This flexibility is more than adequate, bearing in mind that excessive deficits over a long period are not a good idea: look at what happened in Belgium where the government now has to spend some 20% of its tax revenues on paying back debt and interest instead of on public services!

### **“Joining means we would have to harmonise tax rates”**

It is not true that the single currency requires harmonised taxation.

There may be a case for that anyway, even outside the euro, as regards indirect taxation in a single market: look at the thousands of jobs and millions of pounds lost to the British brewing industry, for example, with the van run to Calais to take advantage of French excise duty on beer, wine and tobacco undercutting ours.

But the Treaty provisions on monetary union made no change to the existing system: taxation can be harmonised only with the agreement of each and every member state (and even then, not direct taxation like income tax).