

The International Role of the Euro

Is international currency status desirable?

Upside

- Central bank seigniorage revenues
- Lower yields for sovereign issuer (safety & liquidity premium)
- Spread between aggregate return on foreign assets & cost of foreign liabilities
- Lower transaction costs for companies and citizens
- Competitive advantage for domestic banks issuing foreign currency
- Less dependence on US-driven global financial cycle (Hélène Rey)
- Geopolitical influence

Downside

- Currency appreciation during times of global stress
- Role as international lender of last resort, constraint on domestic policy
- Current account deficit & Triffin dilemma (downside for some, not all in society)

Historical dominance

Druegel

- Natural monopolies are rare (Eichengreen *et al*, 2018)
- Pre-WWI (1890-1914): multipolar system dominated by the British pound sterling, the German mark and the French franc.
- WWI to WWII (1919-39): duopoly of the British pound sterling and the US dollar
- Post-WWII Bretton Woods (1945-1973): US dollar monopoly
- Post-Bretton Woods (1973-today): USD dominance, lesser international role of the euro (previously mark) & Japanese yen.

International role of the euro – ECB summary index

Source: ECB. Notes: 'Arithmetic average of the shares of the euro at constant (current) exchange rates in stocks of international bonds, loans by banks outside the euro area to borrowers outside the euro area, deposits with banks outside the euro area from creditors outside the euro area, foreign exchange settlements, global foreign exchange reserves and share of the euro in exchange rate regimes globally. Data at constant exchange rates were not available for foreign exchange settlements. Data for 2016 are used for 2017 and 2018 observations for the share of the euro in exchange rate regimes globally. The latest observations are for the fourth quarter of 2018.'

What makes an international currency?

1. Large economy, both in GDP and trade terms, economic dynamism
2. Free movement of capital
3. Willingness of authorities to play an international role
4. Stability (monetary, financial, fiscal, institutional, judicial, etc.)
5. Large and elastic supply of safe assets
6. Developed – liquid and deep – financial markets
7. Geopolitical or military power, strong state

Supply of safe assets from the euro area

Source: Bruegel using data from Bloomberg for bonds issued by EFSF, EU, ESM and EIB, S&P for credit ratings and Eurostat for government debt securities. Notes: Includes bonds issued by 19 EA countries, European Financial Stability Facility, European Union, European Stability Mechanism and European Investment Bank.

How to enhance the international role of the euro?

- Ambitious strategic recovery & growth plan -

What is an international currency?

International functions of the euro – FX reserves & international debt securities

Source: ECB. Notes: Current exchange rates, end of period.

International functions of the euro - international trade

Source: ECB. Notes: Use of the euro as a settlement/invoicing currency in extra-euro area exports and imports of goods and services