

The ECB. The EMU. Advantages and Disadvantages of the Euro.

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- 1 The European System of Central Bank (The ESCB)
- 2 The European Monetary Union (EMU)
- 3 Advantages and Disadvantages of the Euro

Statute and Main Goals of the ESCB

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Main Goal of any bank within the ESCB: Maintain medium-term price stability (2% CPI). How:

- deposit and lending facilities
- repo agreements (1-Week and 3-Months)
- reserve ratio (2%)

Article 108 of the Treaty establishing the European Community:

“When exercising the powers and carrying out the tasks and duties conferred upon them by this Treaty and the Statute of the ESCB [Eurosystem],...



...neither the **ECB**,

nor a **national central bank**,



nor any **member of their decision-making bodies**



shall seek or take instructions from Community institutions or bodies, from any government of a Member State or from any other body.”

THE EUROPEAN SYSTEM OF CENTRAL BANKS (ESCB)



ORGANISATION



THE EUROSISTEM



ORGANISATION

- € European Central Bank
- 1 Nationale Bank van België / Banque Nationale de Belgique
- 2 Deutsche Bundesbank
- 3 Central Bank and Financial Services Authority of Ireland
- 4 Bank of Greece
- 5 Banco de España
- 6 Banque de France
- 7 Banca d'Italia
- 8 Central Bank of Cyprus
- 9 Banque centrale du Luxembourg
- 10 Bank Ċentrali ta' Malta/ Central Bank of Malta
- 11 De Nederlandsche Bank
- 12 Oesterreichische Nationalbank
- 13 Banco de Portugal
- 14 Banka Slovenije
- 15 Suomen Pankki – Finlands Bank



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The Euro

ESCB

ESCB: A system involving the central banks of the EU members + the ECB

Eurosystem

Eurosystem: ECB + the central banks of the *countries using the €* as their official currency

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Who are these countries?



Parallels between the FED and the Eurosystem

The Fed

- 1 Who governs: BoG (7 members)
- 2 Who makes policy: the FOMC (7 + 5)
- 3 Who are the members: the Federal Reserve banks
- 4 BoG members serve 14 years

The Eurozone

- 1 Who governs: Executive board (6 members)
- 2 Who makes policy: the Governing council (6 + 15)
- 3 Who are the members: the national central banks
- 4 EB members serve 8 years

The European Monetary Union (EMU)

How does a country become a member of the Eurosystem?

The Maastricht criteria:

- 1 **Price stability:** at most 1.5% higher CPI than the average for the 3 best countries in inflation
- 2 **Exchange rate stability:**
 - $\pm 15\%$ around the parity vs. the € for 2 years
 - no devaluation of the currency 2 years before joining
- 3 **Interest rate convergence:** main interest rates not higher than 2% more than the 3 best countries in inflation
- 4 **Fiscal stability:**
 - Government deficit $\leq 3\%$ of GDP
 - Gross government debt $\leq 60\%$ of GDP

Advantages and Disadvantages of Joining the EMU

Advantages

- ↓ in transaction costs: incentives to go international for the local firms
- reduces currency risk
- overall stability of the economic environment

Disadvantages

- loss of independence of monetary policy
- monetary policy no longer tailored according to local needs, inflexible
- risk of asymmetric economic shocks