Is the Euro, as a Common Currency, a Tool for Integration?

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Is the euro, as a common currency, a tool for integration? *

Maria Lorca*

So much of barbarism, however, still remains in the transactions of most civilized nations, that almost all independent countries choose to assert their nationality by having, to their own inconvenience and that of their neighbors, a peculiar currency of their own.1

Introduction

The European Union (EU) has become an icon of successful regional integration. Despite this success, the on-going integration process has two different speeds; while economic integration has been fast, steady, and assertive, political integration has been slow and demoralizing at times. This is justified by the complicated idiosyncrasy of the EU structure. However, this complacency with integration difficulties is becoming dangerous as the EU is at a critical moment with respect to both economic and political integration. In fact, many voices are claiming that the EU integration process has come to an abrupt end due to the latest difficulties in encouraging important structural reforms, implementing sound economic requirements, and struggling to agree on the Reform Treaty. Gros and Micossi have stated that:

“the EU’s inability to meet the challenges of integration is due to rigid economic structures and inadequate human capital—weaknesses that according to conventional wisdom can only be tackled by national policies, with little role for the Union and common policies. On the contrary, substantial policy spillovers across the EU justify strengthened policy coordination for labor-market, immigration and welfare reform”.2

However, this criticism is opportunistic because it does not take into account all that has been achieved in such a short period of time given the number of different countries involved, especially after the introduction of the EMU and the adoption of the euro as a common currency.

Currently, there is an academic debate on whether economic integration precedes political integration or vice versa: this debate mainly focuses on explaining whether regional integration is caused by political or economic factors. Some assert that political decisions have been motivated by economic reasoning3, and explain that historical evidence proves that “descriptions of

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fluctuations of international economic integration identify clear economic dynamics behind political decisions. "4 Others believe that political decisions are the propellers of regional integration and, as Balassa states, “political motives may prompt the first step in economic integration.”5

Regardless of this debate, this paper will explain how the introduction of the euro has facilitated the EU’s regional integration process, which encompasses both economic and political integration, and has allowed Europe to blossom “into a continent that is widely admired as prosperous, diverse and caring.”6

Regional Integration in the EU

The scientific community has not yet agreed on a sound definition of regionalism and regional integration, two terms that are often used synonymously. Regional integration—which is triggered by a momentum of consolidation, the determination to agree on terms, and the pooling of common interests—requires a commitment of governments to a political and economic objective. Regional integration has an effect on nation-states not only in terms of economy, but also in terms of institutional structures. Hence, regional integration forces states to become part of a larger political structure that is a counterpart to the economic system.

As governments foster regional integration, not only do political national borders disappear, making it harder to distinguish regional from national decisions, but also, particular economic national interests dilute in the process. Sometimes states highly oppose this evolutionary process and block regional political developments, which simultaneously affect the economic course of action. This is called a crisis, and the EU has so far overcome a few.

Economic integration is defined as “the continuous abolishing of discrimination between national economies”7, and political integration is identified “with rational actors seeking to pursue their interests within political institutions.”8 However, each type of integration has its stages oriented towards obtaining a full union, which can only be achieved with the complete unification of the economies involved and a unified policy on common issues.

Economic Integration: A Quick Overview

According to Balassa,9 there are different levels of economic integration, beginning with a basic preferential treatment and culminating in a monetary union—the last step to achieve political union.

Economic integration theory explains that preferential treatment is the most basic type of integration. It is one in which some non-EU members enjoy lowered import duties for a particular established set of goods. One example is the one formed by the EU and the African, Caribbean, and Pacific countries (ACP countries). This preferential treatment evolves to create the free trade

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4 Ari Nieminen, “Towards a European Society? Integration and regulation of Capitalism,” paper presented, with the permission of the faculty of Social Sciences of the University of Helsinki, for public discussion in the Auditorium of the Helsinki University Museum, Snellmaninkat 3, on 19th March 2005, 91.
5 Bela Balassa, The Theory of Economic Integration. Homewood, Ill.: R. D. Irwin, 1961, 129
7 Ari Nieminen, “Towards a European Society? Integration and regulation of Capitalism,” paper presented, with the permission of the faculty of Social Sciences of the University of Helsinki, for public discussion in the Auditorium of the Helsinki University Museum, Snellmaninkat 3, on 19th March 2005, 89.
8 Ari Nieminen, “Towards a European Society? Integration and regulation of Capitalism,” paper presented, with the permission of the faculty of Social Sciences of the University of Helsinki, for public discussion in the Auditorium of the Helsinki University Museum, Snellmaninkat 3, on 19th March 2005, 78.
area which sees that all kind of trade impediments, such as import duties and quota restrictions, are not applicable among partner members. One notable example was the European Free Trade Area Association\textsuperscript{10} (EFTA) established by the EFTA Convention in 1960 which included Iceland, Liechtenstein, Norway and Switzerland. More recently, in the Barcelona Declaration (1995), the Euro-Mediterranean Partners\textsuperscript{11} agreed on the establishment of a Euro-Mediterranean Free Trade Area (EMFTA) by the target date of 2010. Further, the custom union follows the free trade area. The custom union is then characterized by a free trade area among member states and a common external tariff towards third countries. The most relevant example is the custom union between the EU and Turkey signed in 1995, which allows goods to travel between both the EU and Turkey without customs restrictions. When custom unions lead to a common external regulation and a fully free internal market of goods, services, labor and capital, member states are enjoying what is called a common market. When a group of countries with a common market achieve a high degree of coordination of sound economic policy, those countries form an economic union. This is transformed into a monetary union when the currencies of the member states are linked by a fixed exchange rate to a common currency. In this case, we should talk about an economic and monetary union (EMU).

### A Common Currency as an Integrating Tool

A common currency is a currency shared by a number of countries, which have agreed on ceasing their national currencies and adopting a common (or single) one. By agreeing to share a single currency, they create a monetary union. The most successful of all the monetary unions that have existed so far, and there have been many, is the Eurozone\textsuperscript{12}. The Eurozone is the only de facto common currency area that exists today, which has become a reality due to effective coordination between both political and economic integration.

Solana points out that the introduction of the euro in 1999 has fostered integration in the economies of the EU member states because it has brought not only macroeconomic and financial stability, but it has also reduced transaction costs and helped allow greater competition.\textsuperscript{13} Thus, although the introduction and adoption of the euro has meant economic and monetary sacrifices, at this point, the euro has proven to be not only economically but also politically beneficial.

The introduction of the euro is helping the implementation of the four fundamental freedoms of a common market—goods, services, people, and capital, which require the coordination of the functions at the legislative, executive, and judiciary branches of governments. Only a proper coordination of these functions guarantees the real movement across borders of the four freedoms, which, in turn, are helping not only the economic, but also the political and social integration. They are causing a “spill-over” effect since, as Noyer\textsuperscript{14} believes, in order to effectively guarantee these freedoms, “it has … been deemed necessary to grant power to the EU in fields such as immigration and human rights.”\textsuperscript{15} However, Noyer also concludes in his report that while “the integration of goods markets is relatively advanced, major shortcomings exist with

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\textsuperscript{10} European Free Area Association. [http://www.efta.int/](http://www.efta.int/)

\textsuperscript{11} The Euro-Mediterranean Partnership is formed by the 27 EU Member States and 10 Mediterranean Partners, which includes Algeria, Egypt, Israel, Jordan, Lebanon, Morocco, Palestinian Authority, Syria, Tunisia and Turkey. Libya has observer status since 1999

\textsuperscript{12} Austria, Belgium, Netherlands, Finland, France, Germany, Ireland, Italy, Luxembourg, Portugal, Spain, Greece and Slovenia, and since January 2008 Cyprus and Malta. New EU members Slovakia, Estonia, Latvia and Lithuania have joined the exchange rate mechanism; others with farther to go before adopting the euro are: Bulgaria, Hungary, the Czech Republic, Poland and Romania.


\textsuperscript{14} Christian Noyer is Vice-President of the European Central Bank

regard to the full integration of service industries”\textsuperscript{16} which is due to different national regulations. Further, people mobility is where integration is the weakest mainly because, as Bertola posits, “labor market integration is hindered by subsidiary and non-harmonised policies.”\textsuperscript{17} Trichet has denounced that as long as:

\begin{quote}
we have 27 different sets of consumer protection, data protection and contract laws, we will not be able to devise products that can be sold across the European Union without costly modification. Similarly, tax laws and (…) social security laws prevent us from reaping the benefits of integration”,\textsuperscript{18}
\end{quote}

This is a reminder that although much has been accomplished, there are major barriers still preventing integration.

**Why is the Eurozone a successful example of integration?**

The Eurozone has become a model to imitate because of the role played by the euro. The euro has been an incentive attractive enough to change economic, political, and social behaviors. The history of Europe reveals many efforts towards integration, but only the EU has passed the test (see table Annex 1).

There is an important difference between the unsuccessful monetary unions and the EMU represented by the Eurozone. While the pioneering monetary unions rested on the value of gold and silver, what is called (bi)-metallism, the Eurozone rests on the euro, chartalism, as fiat money. Metallism or bimetallism is a monetary system in which the value of the currency unit is expressed in amounts of gold or silver, and where the “exchange rate” is fixed by law. The problem is that this system is very unstable mainly because gold and silver are scarce resources: governments can only print as much money as could be backed up by the stock of gold or silver stored. Fiat money is issued by a central national bank, and its value and stability depends on the good credit of the issuing authority. This good credit, in turn, is based on the political and economic stability of the country.

In the EU, economic stability has been mainly achieved with the introduction of the following two economic pillars:\textsuperscript{19} the economic union and the monetary union. The economic union has the Stability and Growth Pact (SGP) as a major instrument, which is based on the implementation of specific fiscal and monetary requirements among EMU member states with the goal of maintaining fiscal and monetary stability. The monetary union is based on the existence of the euro as a common currency, and the implementation of a common monetary policy supervised by a Central Bank- the European Central Bank (ECB). The introduction of a common interest rate by the ECB, and the requirements of the SGP have encouraged integration because they have fostered the synchronization and harmonization of the economic behaviour. This leads Rose to think that “business cycles are systematically more highly correlated between members of currency unions than between countries with sovereign currencies.”\textsuperscript{20}


Political Integration and the Euro

The Reform Treaty (Lisbon, Dec. 1, 2007) is the latest tool of political integration that has been implemented after the French and Dutch rejected the proposed EU constitution in mid-2005. This rejection not only stalled the designs for deeper political integration but also dramatized public disaffection with a constitutional project that appeared remote and bureaucratic. With this impasse in political integration, efforts towards further economic integration were ‘delayed’ as well. Therefore, the main objective of the Treaty is to re-launch, after two years of introspection, the political integration of Europe which, in turn, will strengthen economic integration.

However, the Reform Treaty has many detractors trying to delay political integration. Roy explains that this delay is often caused by a "healthy resistance to a potential loss of national identity."21 For instance, the position held by Great Britain and France has resulted in the Treaty resisting the importance of four major symbols of EU political integration: the Charter of Fundamental Rights, the flag, the anthem, and the EU Foreign Minister. For others, as Janowski explains, these symbols “are part of the European ‘policy building’ that fosters socio-cultural integration in Europe.”

According to Calleja22, although this treaty is a tool for political integration, it has also been designed with two economic objectives in mind: One is to help face hard competition coming from economic giants such as China, India, and Brazil. The second is to prevent the European economic decline caused by the currently global geopolitical instability that might affect the economic performance of the EU. Javier Solana23 was asked during an interview for the People’s Daily24 if the Reform Treaty has really brought new hopes for the political integration of the EU. He answered that “not merely hopes but reality. The treaty (...) indicates that 27 member nations will work to implement the aspiration of joint economical and political plans, so as to better cope with new challenges brought to us by economic globalization.”

It is important to explain that while the EU is understood as a single political bloc, from an economic perspective, the EU is a fragmented bloc. On one hand, the EU is composed of fifteen European countries that have the euro as common currency—Eurozone member states25. On the other hand, there are a number of countries that are part of the EU but do not have the euro as common currency (non-Eurozone countries).26 Hence, the economic conduct of the Eurozone as a bloc directly influences the economic performance of the EU as a whole.

There are two economic indicators that demonstrate the economic importance of the Eurozone and its impact on the EU as a political and economic bloc: First of all, the size of total real Gross Domestic Product (GDP) is the economic indicator that best explains the economic supremacy of the Eurozone over the other non-Eurozone countries. Basically, this indicator measures “the size of a country’s economy.”27 The latest “OECD Factbook”28 reports the

“Para afrontar la competencia de los nuevos gigantes económicos, China, India, Brasil, y evitar el declive económico de Europa, también porque dada la inestabilidad geopolítica mundial cada vez es más evidente la urgencia de que la Unión Europea hable con una sola voz en la escena diplomática mundial.”
23 High Representative of the EU for Foreign Affairs
24 People’s Daily Online, “EU Heading for Vital Reform.”
25 Countries that have the euro as a common currency.
26 U.K., Denmark, Sweden, Estonia, Latvia, Lithuania, Poland, C. Republic, Slovenia, Hungary, Romania, Bulgaria.
27 OECD Factbook, “Macroeconomics Trends: Gross Domestic Product (GDP).”
28 OECD Factbook, “Macroeconomics Trends: Gross Domestic Product (GDP).”
following size of Gross Domestic Product (GDP) in 2005 for the Eurozone-15 and certain non-Eurozone countries.

<table>
<thead>
<tr>
<th>Countries</th>
<th>Size of RGDP (in Bill US$, current prices and PPPs)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Eurozone</td>
<td>$11.818,60</td>
</tr>
<tr>
<td>OECD Total</td>
<td>$33.301,80</td>
</tr>
<tr>
<td><strong>Some Non-Eurozone countries</strong></td>
<td></td>
</tr>
<tr>
<td>U.K</td>
<td>$1.978,80</td>
</tr>
<tr>
<td>Denmark</td>
<td>$185,00</td>
</tr>
<tr>
<td>Sweden</td>
<td>$290,00</td>
</tr>
<tr>
<td>C. Republic</td>
<td>$188,60</td>
</tr>
<tr>
<td>Poland</td>
<td>$530,00</td>
</tr>
<tr>
<td>Hungary</td>
<td>$179,00</td>
</tr>
</tbody>
</table>

The second economic indicator is the country’s performance in terms of exports, the Eurozone has the U.S., the U.K., and China as its biggest competitors, but still when compared with these major competitors, “the euro area accounts for the largest share of world exports and has experienced a relatively smaller decline in export market share since the early 1990s.”

The Eurozone will be able to maintain this privileged position vis-à-vis these economic giants as long as the Eurozone remains market-competitive. Many have criticized Sarkozy’s success in removing from the Reform Treaty the reference to market competition as an objective. For Sarkozy “competition is no longer an objective in itself. It is a means in the service of the internal market.” While EU member states do not fiercely compete among themselves any more in a zero-sum game, but companies still do. Moreover, for the sake of the countries’ living standards, competition is necessary to raise productivity and competitiveness among companies in order to attract both national and foreign capital investment. Ekinci, Kalemli-Ozcan, and Sorensen point out that there is a “positive relation between capital flow and various determinants of productivity, such as property rights, low cost of physical capital, and low risk of default.” They have concluded that ‘social capital’, when proxied with confidence and trust, demonstrate capital flows to those regions where there is confidence in the courts, the parliament, and other institutions. They explain that in the US ‘ownership of physical capital among the 50 U.S. states is almost perfectly diversified across the entire United States,’ demonstrating a high level of integration. However, the level of integration in the EU tells a different story.

The expected result, C. Noyer explains, is that “the euro, together with healthy competition among differing policy designs of national authorities, will act as a catalyst for


35 Vice-President of the European Central Bank
further reform and integration.\textsuperscript{34} In fact, Giuseppe Bertola claims that enhancing market competition will, in turn, foster production efficiency and “make it more difficult for National governments (…) to conduct independent macroeconomic policies”\textsuperscript{35} which could easily delay economic and political integration. Hence, Michael Deppler explains, “integration and competition are the answer, not the problem.”\textsuperscript{36} However, the debate is raised when certain sectors of society blame the euro, most specifically the recent euro appreciation against the US dollar, for the loss of competitiveness. However, the high euro is impacting some areas more than others because “it causes more problems for those who have not done the work they should have done on competitiveness in recent years.”\textsuperscript{37}

Consequently, the Euro, which since its inception has become an international currency, is helping strengthen the image of the Eurozone and the EU as an influential political bloc, is not in vain to be considered an international currency of paramount political importance. The “Survey on the use of euro cash outside the EU”\textsuperscript{38} explains that the exchangeability of euro cash abroad seems to have generally improved, with wider acceptance and availability of the currency at banks and exchange offices. This improvement in the general demand for the euro on an international level fostered the image of the Eurozone as a strong political actor.

Nonetheless, the introduction of the euro notes encountered some difficulties. For instance, the design of the euro opened a two-sided political debate because the euro was designed to display “symbolic bridges and other architectural emblems seemingly designed to avoid giving offense to anybody.”\textsuperscript{39} This design meant that most countries will lose a part of their history usually reproduced in national bank notes. Therefore, while some applauded this neutrality as a sign of respect for the new period opening up for Europe, others were reluctant to lose certain symbols representative of their identity and sovereignty. However, in 2009 the EU celebrates the 10-year anniversary of the land of the EMU, and the “EU has asked European citizens to vote and choose the design of a commemorative 2-euro coin …since the people of Europe are the ones who use it.”\textsuperscript{40}

Final Word

This paper has, in broad terms, analysed how the euro since its inception has fostered political and economic integration, mainly because it enhances transparency and competition in both the political and economic arena. A competitive country depends both on the “quality of a country’s economic and political institutions”\textsuperscript{41} and the maintenance of “high rates of growth and


\footnotesize{35} Giuseppe Bertola, “Economic Integration, Growth, Distribution: Does the euro make a difference?”, DG RCFIN Annual Research Conference in Brussels, October 2007.


\footnotesize{41} Eurointelligence, “Why the European Debate on Competitiveness is Going Nowhere,” May 12, 2006, \url{http://www.eurointelligence.com/article.581+M5a26e023014.0.html} (accessed January 27, 2008)
employment in the medium term.” 42 For instance, Almunia has recently explained that “en España es necesario el aumento del nivel de productividad por que el empleo sin una mejora productiva no será sólido ni sostenible.” 43 Therefore, growth and employment objectives are, in fact, the main theme of the Lisbon Agenda, which was designed to foster labor, services, goods, and capital mobility. Although the Lisbon Agenda has not been sanctioned as law, the continued necessity to work towards the achievements of these proposed goals are of great importance to help advance political, economical, and social integration among EU member states. In fact, Gonzalez, as Chair EU Advisory Committee, has expressed recently that Europe is “losing influence in the geopolitical sphere. We are losing influence in economic and technological terms, and as a result, we are also becoming less relevant to our citizens – by losing competitiveness and value.” 44

This paper has demonstrated that much has been accomplished and that the euro as a common currency is here to stay. However, the recent strengthening of the euro vis-á-vis the U.S. dollar is not going to last forever, and many are forecasting the impending end of this situation and return the ‘U.S. dollar-euro’ exchange rates to traditional levels. At this point, if the political and economic grounds of the EU are not firmly consolidated, outcomes are expected to be extremely dangerous for survival of the EU. Hence, it will be in this precise moment that the European Union will need more than ever united visionary leaders, as were its founding fathers, in order to save the situation.

## Table - Annex 1

<table>
<thead>
<tr>
<th>History of failing attempts to common currencies and monetary integrations</th>
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</thead>
<tbody>
<tr>
<td><strong>1. There were three stages</strong>(^{45}) <strong>to the economic and monetary union in Europe</strong></td>
</tr>
<tr>
<td>a. the 1969 Den Haag summit and Werner Report</td>
</tr>
<tr>
<td>b. the 1979 European Monetary System and the ECU</td>
</tr>
<tr>
<td>c. and the 1989 Single European Act and the &quot;Delors Report&quot;</td>
</tr>
<tr>
<td><strong>2. In terms of historical monetary union among European countries, there have also been several unsuccessful attempts. According to Bartel</strong>(^{46}), <strong>there were four major attempts:</strong></td>
</tr>
<tr>
<td>a. the Austro-German monetary union (1857-1866)</td>
</tr>
<tr>
<td>b. the Latin Monetary Union (1965-1878) among France, Belgium, Italy, and Switzerland</td>
</tr>
<tr>
<td>c. the Scandinavian monetary union (1875-1917) among Denmark, Norway and Sweden</td>
</tr>
<tr>
<td>d. finally, one between Belgium, Luxemburg in 1921</td>
</tr>
<tr>
<td><strong>3. Worldwide we must take into account:</strong></td>
</tr>
<tr>
<td>a. East African currency area</td>
</tr>
<tr>
<td>b. Gold Standard</td>
</tr>
<tr>
<td>c. French African Community Franc</td>
</tr>
<tr>
<td>d. Gulf Rupee</td>
</tr>
</tbody>
</table>

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