

Integrative Case 3

The Eurosystem, the Euro, and the U.S. Dollar

You have been hired as a financial analyst in the Bank of Canada. As an initial project, you have been assigned to investigate recent developments pertaining to the introduction of the euro and its implications for the United States and international financial markets. There are concerns that the introduction of the euro has led to currency diversification in international banking and that the increasing use of the euro in world trade will reduce the international use of the U.S. dollar and potentially affect the exchange rate between the Canadian dollar and the U.S. dollar.

You are familiar with the Eurosystem, which consists of the Frankfurt-based European Central Bank (which came into being on January 1, 1999, in succession to the European Monetary Institute) and the national central banks of the 12 euro-area countries—Austria, Belgium, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, the Netherlands, Portugal, and Spain. The Eurosystem excludes the central banks of the European Union countries that have not yet adopted the euro—Denmark, Sweden, and the United Kingdom. These three countries continue to pursue national monetary policies and have no input into the decisions related to the single monetary policy for the euro area.

To expand your knowledge and prepare for your talk, as a first step you want to identify a number of issues that you would like to address. You begin by visiting the Internet site of the European Central Bank (ECB) at www.ecb.int, and the site of the European Commission at www.europa.eu.int/euro to access the Commissions newsletter *InfEuro*. You also visit the Internet site of the Federal Reserve Bank of St. Louis at www.stls.frb.org. Click *Publications* and then *Review (Bimonthly)* to access the Bank's *Review*. In the September/October 2001 issue, you find an interesting article written by Patricia S. Pollard (a research officer and economist at the Federal Reserve Bank of St. Louis) entitled "The Creation of the Euro and the Role of the Dollar in International Markets."

Based on these readings, you decide to answer the following questions.

1. How is the Eurosystem governed?
2. What is the primary objective of the European Central Bank?
3. Who is responsible for the implementation of monetary policy in Europe?
4. What are the gains in the euro-area from the introduction of the euro?
5. What is the relative size of the U.S. and euro-zone economies?
6. What is the share of the U.S. and euro-zone economies in international trade?
7. What changes (if any) have occurred since the euro was introduced on January 1, 1999?
8. Has the dominance of the U.S. dollar in international money and capital markets declined since the introduction of the euro?
9. In 2000, how many IMF member countries had their currencies pegged to the euro? To the U.S. dollar?
10. Do you know of any countries that adopted a currency board with the euro?