The enlargement of the euro area

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Member of the Executive Board of the European Central Bank

Cyprus, 30 November 2006
Benefits of adopting the euro

a) **For the individual country**
   - Stable exchange rates in relation to most important trading partners
   - Credible framework for monetary policy and price stability = low risk premia and low long-term interest rates
   - Reduced transaction and information costs
   - Stronger protection against financial disturbances

b) **For the euro area**
   - Completion of the internal market, providing price and cost transparency
   - Economies of scale and more efficient allocation of production factors
Risks related to premature adoption of the euro

a) **For the individual country**
   - Differences in business cycles may lead to suboptimal interest rates in the national context and the emergence of local “bubbles”/ “crises”.
   - Unless convergence is sustainable, a country can run into competitiveness problems, with no resort to exchange rate changes.
   - Without sufficient flexibility to adjust to changes in competitiveness, there is a risks of protracted economic losses.

b) **For the euro area**
   - A lack of convergence and flexibility could affect the credibility of EMU.
The road to the euro

(As stipulated in the Treaty)

- Optional: Pre-ERM II phase
- ERM II membership
- ERM II membership - Technical preparations
- Adoption of the euro

Steps:
- Accession to the EU
- Entry into ERM II
- Assessment of convergence, formal decision on entry and conversion rate
ERM II membership

• Estonia, Lithuania and Slovenia joined in June 2004.
• Cyprus, Latvia and Malta joined in May 2005.
• Slovakia joined in November 2005.

<table>
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<tr>
<th>Country</th>
<th>Participation in ERM II with effect from</th>
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<tr>
<td>Czech Republic</td>
<td>-</td>
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<tr>
<td>Estonia</td>
<td>28 June 2004</td>
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<td>Cyprus</td>
<td>2 May 2005</td>
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<td>Latvia</td>
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<td>Lithuania</td>
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<td>Hungary</td>
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<td>Poland</td>
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<td>Slovenia</td>
<td>28 June 2004</td>
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<td>Slovakia</td>
<td>25 November 2005</td>
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<td>Sweden</td>
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<td>Denmark</td>
<td>1 January 1999</td>
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EUROPEAN CENTRAL BANK
Technical preparations

• The ECB and the national central bank together monitor all technical preparations for the cash changeover that fall in the areas of competence of the Eurosystem.

• The ECB and the national central bank carry out a public information campaign explaining the following aspects of the changeover to the euro:

  1. The visual appearance of the euro banknotes and coins
  2. Their security features
  3. The modalities of the cash changeover
Communication tools used in Slovenia

Exhibition

Leaflet to all Slovenian households

Euro web pages

Our money € CONFERENCE SLOVENIA
15 January 2007
Formal enlargement process – role of the ECB

• Every second year, or at the request of a country, the ECB and the European Commission report on the state of convergence in their Convergence Reports.

• Case-by-case examination based on the convergence criteria and the principle of equal treatment.

• Based on these examinations and a proposal by the Commission, the (ECOFIN) Council decides which countries fulfil the conditions for adopting the euro.

• The Council also decides the conversion rate at which the national currency will be replaced by the euro.
Policy challenges in the run-up to euro adoption

- Achieve **sustainable convergence**. Price stability and fiscal prudence are at present key concerns.

- Complete all transition and EU harmonisation-related reforms (e.g. price liberalisation, administered prices and indirect tax harmonisation).

- Contain over-heating tendencies, as indicated by:
  - Strong domestic demand, fuelled by low interest rates, credit and house price growth;
  - large current account deficits, which raise questions of sustainability.

- Focus on structural reforms which will make the economy more flexible and resilient to shocks.
End of presentation