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Course Title

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Should the UK Join the Euro

The Economic and Monetary Union (EMU) in which some members of the European Union (EU) have joined, proposes great benefits and challenges for the European countries. Most of discussions have focused on the immediate issues, such as prospects for the euro and the possibility of expanding the euro-zone. Discussion of the prospects for European monetary union has often focused on whether the European Union is an optimal currency area for Britain and, if not, how long it might take to become one and whether there might be unacceptable costs to some part of the territory along the way.

Euro is defined as a single European accounting currency and an official currency of the European Union. "The role of the euro as an international investment currency, anchor currency and reserve currency is inseparably associated with its internal stability" (Artis et al p. 10). Today, this is an official currency 15 Euro states and Eurozone. Euro was introduced in 1999, but practically launched only in 2002. Critics admit that: "the euro has a good chance of becoming a lastingly stable currency, respected by the markets and the population alike. Domestic stability is at the same time the best contribution the euro can make to a sound, viable and stable global financial system in which the financial market players can act in a spirit of responsibility" (Artis et al p. 10). The advent of a single European currency, alongside enlargement and the growing international role of the EU, as codified in the SEA,

TEU and Amsterdam Treaty, gives rise to questions regarding the type of actor the EU constitutes for external partners at the start of the twenty-first century. In this respect, debates over the EU's future parallel some of those which preoccupy Japan in the postCold War world (Armstrong and Bulmer 32).

Britain is one of the European countries which does not join Euro and uses its national currency, the pound. The main disadvantage of this currency is financial instability and inflation. Many countries do not invest in Britain because of its monetary policies and the unstable exchange rates of the pound. Because of its current policies, Britain lost its influence in Europe and around the world. The search for a new way of conceptualizing power and international responsibility continues in Europe, within the framework of an international discourse that is already familiar to both (Barnard and Scott 88). This contemporary discourse is one in which previous questions of 'high' versus 'low' politics have to some extent been replaced by a debate over the types of issues that have to be confronted in this new international environment. Critics admit that joining the Euro will help the country to increase standards of living and maintain financial stability. For Britain, Europe is the largest market it deals with. Without a single stable currency, many companies cannot operate effectively in Europe. Economists admit that since 1999, Britain is in worst position because of different currencies and unstable exchange rates. If Britain does not join the Euro, it will suffer from economic crisis and decreasing standards of living (Barnard and Scott 98). The EU's attitude towards this kind of security debate leads to the promotion of international cooperation through preventive diplomacy, confidence-building measures, peacekeeping and the management of regional crises, which are all characteristic themes of civilian power discourse. However, despite the presence of 'neutral' states in Europe, the role of the military is seen to be fundamental to securing stability, and to actions that are consistent with political, economic and humanitarian aspects of European crisis management. If Britain joins the Euro,

it will overcome economic crisis and improves its economic and political position in Europe and around the world (Balanyá 43).

The main threat of joining Euro is possible economic crisis affected Europe. Europe economy is unstable influenced by political and social changes. In the case of the Euro, however, the change is not going to be a simple decimal shift, but a change that will involve five significant places, a truly barbarous fraction, in moving from Euro to national currency, or back again (Minford n.d.). When it happens, it will be deeply unpopular. It is a master stroke, to leave this shift in national currencies into Euro notes and coins for several years, until the operation of Euro wholesale markets and the central monetary and macro institutions for the ESCB had already fully bedded down. The Euro, in effect, would be a *fait accompli*, before the implications of the change would seriously affect the ordinary person in the street. Indeed, the whole EMU process is both fascinating and unique; never before in history have a number of separate national, sovereign countries agreed to pool their sovereign control over money within the adoption of a single federal monetary system. There are only two allowed methods for paying off debt. The first is by raising net tax revenues, relative to expenditures; the second is through a form of inflation tax. Consequently, under this theory, if there is no political will to raise the primary surplus, then the inevitable way in which the existing debt is effectively reduced must be through an inflation tax. Even when the money stock is tightly controlled, equilibrium can only be achieved by reducing the level of debt, to that which people are prepared to hold, through some measure of inflation. So, inflation has to be the equilibrium outcome (Layar et al n.d.).

The Five Economic Tests were developed by the Chancellor of the Exchequer. The first tests measures 'convergence' of the UK economy and political situation with the rest of the EU (Minford n.d.). The second tests measures economic flexibility of the UK; the third

tests measures the level of inward investment; and the fourth test assess investment in the City of London. The fifth test analyzes impact of the economic integration on the UK. These tests allow economists to analyze and evaluate the Euro's long-run effect on employment (Minford n.d.). However, European Monetary Union (EMU) is likely to have the largest negative, or smallest positive, effect on employment. They show that, between the euro-zone and the US dollar, nominal exchange rate trends are increasingly in line with the required real exchange rate adjustments. In the more recent past, exchange rate flexibility has outperformed the Bretton Woods system in this respect (Balanyá 22).

The UK should join the Euro because it will have one common central bank, the ECB. It will eventually issue the only circulating money in Euroland. The previous central banks of the members of EMU will diminish in power and importance according to the Maastricht Treaty. They will most likely resemble the regional reserve banks of the Federal Reserve System of the US. This analogy suggests that they will not formulate a common European monetary policy. Monetary policy will be centralized on a pan-European level under the ECB. Furthermore, membership in EMU and the adoption of the Euro are regarded as permanent. There are no escape clauses (Minford n.d.).

The key assumption, however, is to rule out any possibility of another way of dealing with excessive debt, which is direct default. Given the lack of will in certain cases to raise the primary surplus, the decision whether to default, or to allow a massive inflationary tax, would not necessarily go in favor of the latter. Moreover, markets, faced with the prospect of either being defrauded by inflation or by direct default, would raise interest rates in advance of either event so rapidly and so fiercely that governments would rapidly be faced with the impossibility of raising more debt on such markets, and should monetary growth still be controlled, (as it would be by the ECB in EMU), would then be forced into default (Minford

n.d.). The market process would seem much more likely to drive excessive deficit countries within the Eurozone into default than into hyperinflation, given the inability to control monetary growth for such a debt-raising government body. It is against this background that the limitations on the ability of member countries within the Eurozone to increase their debt without limit by raising deficits above 3 per cent of GDP should be seen.

Exchange rate policy for the euro has been a matter of debate. “It is true that differences in inflation are now small but that has been so now for at least a decade and a half; this has not stopped very large swings in the exchange rate due to these other reasons which affect the ‘real exchange rate’ (that is, the exchange rate adjusted for relative inflation.)” (Minford n.d.). The experience of German, French and Japanese ministers is an example of monetary policy. German, French and Japanese ministers of finance have called for exchange rate targets between the euro, the U.S. dollar and the Japanese yen, while the President and the Vice-President of the European Central Bank, the Chairman of the Federal Reserve Board and a US Secretary of the Treasury have opposed the idea. (Central bankers tend to dislike exchange rate fixing because it constrains their room of maneuver, and, shortly before elections, incumbent politicians may need their support.) They have stressed the well-known instability of adjustable peg systems. But the theory of optimum currency areas is also relevant (Barnard and Scott 99). If Britain joined EMU, regulatory competition would suffer as well. Financial regulation of the City of London is known to be liberal - more liberal than regulation on the continent. Up to now, the regulation of banks has remained in the hands of the national institutions. But the President of the ECB has called for the centralization of banking regulation in the hands of the ECB. If Britain joined EMU, reserve requirements could easily become more stringent.

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