

THE COSTS AND BENEFITS OF ROMANIA'S ADERATION TO THE EURO ZONE AND ADOPTION OF THE UNIQUE CURRENCY

Apetri Anișoara Niculina

“Ștefan cel Mare” University

Faculty of Economic Sciences and Public Administration

Universitatii Street, No. 13, e-mail: anisoarad@seap.usv.ro, Phone: 0742624676

Hlaciuc Ana Maria

“Ștefan cel Mare” University

Faculty of Economic Sciences and Public Administration

Universitatii Street, No. 13, e-mail: hlaciuc_anamaria@yahoo.com, Phone: 0230522978

The accession to the Economic and Monetary Union, though not a criterion of accessing the European Union, involves the compliance with the convergence criteria of Maastricht: stability of the exchange rate, of interest rates, of the inflation, of the external debt and budgetary deficit. Even if the joining of the EMU represents therefore no conditioning of accessing the EU as a full rights member and, maybe, no priority of the candidate countries, the consequences of this option must be seriously put into balance, taking into account the most the fragile macro-economical stability of the pretending countries, such as Romania. A major regime change, as the monetary unification, is clearly made when there are strong motivations given by benefits, but such a change involves costs, risks and difficulties. The adoption of the unique currency in an unsuitable time can have more bad consequences than positive ones.

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Giving up the national currencies and adopting an unique currency rose serious and numerous controversies in the target countries, where there are supporters and critics of this idea. The introduction of the euro certainly involves a series of indubitable advantages, but also a series of costs both at the micro and macro-economical level. The literature analyzing the costs and benefits of the monetary union is rather diverse, and there we may find certain divergences referring to costs or benefits. Lutowski (1997) identifies that the main benefits of the EMU joining are the following: *eliminating uncertainty* deriving from exchange rate fluctuations, *suppressing the inflationist phenomenon*, *adopting active competitiveness increasing measurements* to correct the deficit of the commercial and payment balances as alternative to the devaluation, and as final effect of these positive evolution having the long-term macro-economical stability¹⁹⁵. The same author considers that, for the countries showing to have a commercial deficit to the European Union and a high inflation, the joining of the Economic and Monetary Union's exigencies is not recommendable in the first years of the EU joining.

1. Benefits of the Monetary Union

Though the benefits are identified and felt first of all at the macro-economical level, there also exist a series of benefits that come from the *macro-economical stability*, and also due to a better

¹⁹⁵ Golban, R., Silași, S., *Eurosistemul o tensiune arhitecturală a convergenței*, Ed., Economică, București, 2009.

international position¹⁹⁶. *Macro-economical level benefits. First of all, the use of the same currency by more countries reduces transaction costs.* As for the benefic influence of the unique currency by the price mechanism, the explanation lies in the fact that the existence of more currencies reduces price transparency, which may determine or support, on the unique market, the price discrimination between the national currency areas. As for the enterprises, an important benefit of the EMU joining is to be given exactly by *transaction cost reduction*, dissolving the element of currency-to-currency conversion afferent cost. Second of all, *the monetary unification eliminates the exchange rate volatility and its costs.* In this context, the diminution or even the elimination of uncertainties relating to the exchange rate stimulates commerce between the monetary union's members. Another economical benefit of joining the EMU is *the improved attractiveness for foreign capital*, encouraged by the macro-economical stability and of the exchange rate. *Third of all, the influences on the local preference are monitored.* It is said that this element is strong in Europe (as it is in the US and Canada), even if custom controls disappeared.

The macro-economical benefits reside from price stability, access to a wider and more transparent market that improves the external financing possibilities and, nonetheless, the elimination of production flows that may come from various economical policies. Benefits coming from the international role of the new currency. First of all, seniorage income is obtained, because an emission of currency is made as debt of the target country, not carrying interest. The currency is used outside the emitting economy and represents profit. If the US frequently imports more than they export, the international liquidity is improved, but in the same time makes profit from surplus. The Governing Council of the Federal Reserve System estimate seniorage profit of the US to be from 11 to 15 billion \$/ year. *Second of all, as the international role of the currency rises, the loans, investments, goods and services acquisition (national or international) will be more and more settled by the financial institutions of the emitting entity.* Therefore, the profits of the financial sector are to rise. *Third of all, the use of own currency in the exterior commerce makes the emitting economy to be less vulnerable to its exchange rate modification than of other economies.*

In the opinion of the authors Turluc Vasile and Cocriș Vasile, the main **direct economical advantages** of the euro are: **the elimination** of the currency risk in case of commercial exchanges between the euro zone countries; *the reduction of currency costs*, by eliminating the exchanges between the communitarian currencies; *price transparency* and, among the **indirect economical advantages** of the unique European currency we have¹⁹⁷:

- *interest rate reduction.* The inflation's reduction as consequence of the Central European Bank's monetary policy, that concerns first of all the countries previously recording weak results in facing it (Italy, Portugal), leading to the obvious decrease of interest rates in the euro zone;
- *the stimulation (of the continuation) of the structural reforms.* If, in order to pass onto the unique currency, the current member countries of the EMU had to adjust their economies, complying with the convergence criteria, The stability and increase Pact imposes the same austerity and rigorousness in the financial and monetary plans, also after joining the unique currency;

¹⁹⁶ Golban, R., Silași, S., *Eurosistemul o tensiune arhitecturală a convergenței*, Ed., Economică, București, 2009

¹⁹⁷ Turluc, V., Cocriș, V., Stoica, O., Roman, A., Dornescu, V., Chirleşan, D., *Monedă și credit*, Ed. Universității „Alexandru Ioan Cuza” Iași, 2009

- *encouraging the economical growth.* The lower costs of transactions, the reduced currency risk (or even eliminated), price transparency are only a few factors capable to push the development of the euro zone economies;
- *gaining the international currency status.* The euro shortly became, as estimated, a currency in which the international reserves are widely placed, a credible alternative to the American dollar, having a more important role than any of the extinct currencies.

The advantages and disadvantages of entering the euro zone must be taken into consideration and analyzed for each country, what for a certain country may be an advantage at a certain moment, for another country may be a disadvantage. For example, if for a strong economy, price transparency may be an advantage, for a less developed economy, the direct confrontation of the national products with the foreign ones may be a disadvantage (not as much for the consumers, as it is for the producers).

2. Costs of the monetary union

The main problem of the monetary unions refers to the costs of this process. The costs may appear due to the fact that, when participating to a monetary union, the countries loose important instruments of the economical policy, more specific- the ones specific to the monetary policy, that is maneuvering the interest and exchange rates. These costs are felt in the case of the asymmetrical shocks. There are two main costs at macro-economical level. A component is represented by the operational costs, necessary to adapt the systems to the new currency: accounting, contracts, devices etc, expenses that *are made only once*, which is very important. The second component is represented by strategic challenges, that is- redefining competition and the apparition of specific risks. The member states of a monetary union cedes the prerogatives of the monetary policy to a central authority, which makes the national authorities unable to make adjustments in case of asymmetrical shocks, by the use of monetary instruments. Moreover, varying with the institutional architecture, the member states are to have a more or less important influence in the decisional process, situation that may be perceived as negative fir the low-influence states. What must be known is the nature and probability of asymmetrical shocks and the alternative instruments that may be used when there is no exchange or interest rate. The properties or criteria of the optimal monetary zones are conditions that the states wanting to participate to a benefic monetary union must comply with. The existence of such conditions makes less probable the presence of asymmetrical shocks, or in case of such shocks assures efficient adjustment instruments.

In order to resume the problem, the costs increase when offer or demand shocks appear, variously affecting the economies participating to the monetary union, when there are different preferences for unemployment or inflation, legislative differences, or differences between the growth rates or the adjustment mechanisms do not work.

3. Opinions against the unique currency introduction

The euro-skeptics often invoked critics referring to the introduction of the unique currency, one of them referring to the cost of the euro introduction, made by the printing or minting the new currency and the withdrawal of the national currencies of the member countries, and costs of the informing campaigns on the euro, of the consumers, replacing the banking and ATM software's costs being huge. Others consider that the functioning of the Monetary Union without a budgetary union is to lead to malfunctioning. Another fear regarding the introduction of the unique currency refers to the price increase, consequence of the

adjustment effect speculated by traders, in spite of the consumers. The main critics formulated by the euro-skeptics, concerning the unique currency, can be summarized¹⁹⁸:

- *the regulations regarding the EMU and the unique currency adopted at Maastricht are unreal*, being the result of an economic and financial-currency conjuncture favorable even since the beginning of the 9th decade. This aspect was confirmed by the difficulties encountered by the European states developed after the year 2002 in order to maintain the budgetary deficit under 3%GDP. On another hand, it was often seen that these convergence criteria were made at a time when the extension of the EU was not anticipated, and the average development level of the member states was a lot over the ones joining the union in 2004 or 2007.
- *the convergence criteria of the Maastricht Treaty* assure the premises of a low inflation, but determine also a low economical growth, the critic referring first of all to the restriction on the maximum budgetary deficit level;
- *the loss of monetary and currency autonomy*;
- *price increase*. There were fears, that partially also became true, that the euro introduction is to lead to price increase, but the impact of the euro introduction is even more relevant comparing the value of a 500 Euro bill with the value of the greatest banknote previously circulating;
- *the existence of a monetary union without a budgetary union*. It is appreciated that the existence of a budgetary union (that does not exist now) would have been capable to compensate for the impact of negative influences on the national economy, which are hard to combat in the absence of the monetary policy autonomy.

Nevertheless, Europe has its own currency, whose introduction generated the following effects¹⁹⁹:

- the creation of a large-size monetary market;
- the increase of monetary market liquidity, giving the banks liberty in movement both in what regards placing resource excess and the possibility to loan;
- the monetary policy gains more rigorousness and answers to the common exigencies, the CBE being the only responsible with the monetary policy;
- the unique momentary market that accelerates the integration process of the other markets in special of the financial market;
- the increase of investments' volume;
- competition accentuation on the financial markets;
- the increase of price transparency as consequence of currency exchange rate disappearance.

The balance of the first existence decade shows that the euro has not fulfilled even the extreme prophecies of the euro-skeptics, who warned that this is a “serious error” that is to irreconcilably deepen the differences between the economies of the states that are to adopt the unique currency, but has not opened any growth or economical convergence era without precedent in the Euro Zone, as hoped by the most enthusiastic promoters. The introduction of the euro currency is an “extraordinary success”, as said by the governor of the Bank of France Christian Noyer, a success “not due to the result of a magical wand movement, but of

¹⁹⁸ Turliuc, V., Cocriș, V., Stoica, O., Roman, A., Dornescu, V., Chirleşan, D., *Monedă și credit*, Ed. Universităţii „Alexandru Ioan Cuza” Iași, 2009

¹⁹⁹ Golban, R., Silași, S., *Eurosistemul o tensiune arhitecturală a convergenței*, Ed., Economică, București, 2009

the fact that this introduction was carefully thought and the bases of the EMU are extremely solid and effective”²⁰⁰.

It is important to mention that the adoption of the euro currency must not be treated by any “pretending” countries and, as consequence, nor by our country, as a purpose itself. The most important thing for Romania to make, now, resides in recovering the gaps in the real economy domain, in order to assure the success of the unique currency adoption. The Romanian National Bank’s policies are concentrated on fitting Romania on the euro adoption trajectory in 2014. On middle term, the retaking of inflation and price increase bringing as close as the European standards are not the only elements taken into consideration, but also is the imbalance minimization – especially, the gradual reduction of the external deficit, in order to give durability to the inflation reduction process²⁰¹. Regardless of the target date Romania sets, the advantages and disadvantages the euro adoption generates in a short-term and long-term period must be taken into calculation, and those are:

Long-term postponing of the euro adoption		Accelerating the euro adoption in a relative short term	
Advantages	Disadvantages	Advantages	Disadvantages
Longer period to make the structural adjustments that are still not made	Persistence of greater transaction cost associated to the currency risk, that may inhibit investments and economical growth	Earlier manifestation of the benefits of currency risk disappearance, leading to stimulating the sustainable economical growth	Loss of monetary policy and exchange rate autonomy, which would move the whole burden of structural adjustments to the level of economical activity and occupation degree, given the still limited flexibility of the Romanian economy
More accentuated progress in the real and nominal convergence plan	Possibility of postponing structural reforms and relaxing the macro-economical policies (especially the fiscal and salary ones) given the establishment of a far target period of the euro adoption	Minimizing the motivations of relaxing the structural reforms’ rhythm	Lack of synchronizing the business cycles of Romania and Euro Zone, which may improve the risk of generating asymmetrical risks, hard to face in the absence of independent monetary and exchange rate policies
Synchronization of the business cycle from Romania to the one of the Euro Zone (pre-condition of minimizing the risk of asymmetrical shock apparition)	The unclear message sent to the international capital markets, the postponing may be attributed to structural or economical policy weaknesses, less visible to the investors, than to the authorities’ decisions	Stimulating the time consequence of the macro-economical policies’ assembly	Difficulty in decelerating a representative central paring for the balance exchange rate leu/euro, leading to the substantial participating period to the ERM2
Longer-term keeping of the monetary and exchange rate policies			Probability of a stronger manifestation of the Balassa-Samuelson effect, in the first part of the economical adjustment process after joining the EU, with repercussions on disinflation

²⁰⁰ Christian Noyer, *Euro - O monedă stabilă în slujba unei economii dinamice*, București

²⁰¹ Isăescu, M., *Probleme ale convergenței reale în drumul spre euro*, www.bnr.ro

			limiting and/or on the national currency appreciation
			Limiting the period in which the efficacy of the inflation target, as monetary policy regime, can be finished

It is worthy to signal that, in order to join the euro zone, the convergence criteria taken into consideration are only the nominal ones: exchange rate stability, low inflation, interest rates close to the euro countries' ones, moderate budgetary deficit and public debt stock, but we still must be assured that at the date of complying with the nominal criteria, a significant progress in the real convergence will have been made²⁰².

The adoption of the unique currency by our country before having made a minimum real economical convergence would be risky and even counterproductive. It is essential that the main reforms (restructuring, privatization, salary policy, mobility of labor force, fiscal policy) to be approached *before*, and not entering the ERM2 (or the euro zone). There, the support is possibly greater, but the costs of an eventual failure are also exponentially multiplied²⁰³.

Given that, for most of the west-European countries, it is unanimously accepted the advantage of using the unique currency, it is hoped that also Romania, whose exterior commerce is oriented almost 2/3 towards this market, is to have real benefits from adopting the unique currency. The introduction of the euro must be a stability factor that will reduce a lot the losses of the national commercial agents, caused by the risks of exchange rate. The euro is to reduce the costs the companies support as consequence of exchange rates. These costs were estimated to 1-2% of the transaction value. also, due to the adoption of the unique currency, valuable time is saved in the management activity, the need of risk analysis and expenditure/profit report disappearing for each operation the company makes.

4. The euro adoption by Romania cannot be forced

In short, the euro adoption means giving up the monetary policy before having assured the necessity for real convergence and its sustainability. That is, before having eliminated the imbalances faced nowadays, and the phase shift of our economical cycle compared to the main economies of the monetary unions. The Romanian Economy represents 1.5% of the euro zone economy, which would make the Romanian inflation irrelevant for the CEB decisions. The CEB monetary policy may be inadequate from the Romanian economy problems' point of view. To the eventual relatively great volatility of production and inflation, an adequate answer is not strongly assured. After both the European Committee and the CEB will have confirmed the compliance with the convergence criteria by Romania, the EU Council is to adopt a decision according to which Romania can join the Euro Zone, time that dissolves the derogation concerning Romania's status as EU member country. At the proposal of the European Committee and after consulting the CEB, the EU Council will adopt a fix and irrevocable exchange rate between the LEU and EURO. With the passing to the Euro, the Romanian National Bank will be part of the *Eurosystem*, transferring to it the responsibility of adopting the monetary policy.

Some analysts proposed the adoption of the euro as soon as possible as a solution of avoiding costs showing up from the materialization of the exchange rate risk. The quick adoption of the

²⁰² Isăescu, M., *Probleme ale convergenței reale în drumul spre euro*, www.bnr.ro

²⁰³ Lazea, V., *Drumul spre Euro*, (<http://www.bnro.ro>).

euro would help the ones with great loans made in Euros, but are paid in currencies of countries aspiring to enter the euro zone. The rush of adopting the euro has its cost, which may be greater than the benefits given by the elimination of the exchange rate. The premature adoption of the euro means the premature elimination of the exchange and interest rates' modification of the adjustment processes, of the differences between Romania and the other monetary union countries. This involves putting the accent too much on the labor market and goods' prices adjustments. Practically, these are the only markets remaining to adjust.²⁰⁴ The adoption of the Euro needs a sufficient start in the plan of the real and nominal integration with the euro zone. In this process, continuing the convergence of the RBN monetary policy convergence with the one of the CEB is essential.

In conclusion, in order to participate at the ERM II and further adopt the euro, the efforts to make the nominal and real convergence of the Romanian economy must be accentuated. The euro adoption makes an irrevocable process, and therefore the convergence process must be made in a durable manner, not only in a certain moment. In order to reach a high degree of sustainable convergence, the efforts made by our country must be significantly intensified. These efforts refer mainly to the necessity of making and maintaining the price stability on a durable manner, and reducing the shown budgetary deficit, during the economical-financial crisis, in most of the member states and in our country, of making and maintaining an optimum level of the public finances. Creating a favorable environment for the sustainable convergence in Romania needs, among others, a monetary policy oriented towards stability and strict implementation of the fiscal consolidation plans. The adoption of the unique currency in a bad time can have more negative consequences than positive ones.

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