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## Issues in Economic Policy

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Does EMU Membership  
Contribute to Economic Stability?

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## **The Unification and Ramifications of the Euro**

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On January 1<sup>st</sup>, 2002 euro cash was introduced in the twelve countries of the euro area, replacing the former national currencies which are no longer legal tender. This was done to unify Europe's currencies and eliminate the problems associated with pricing, exchange rates and importing/exporting. This solution was supposed to help fix some of the economic problems that several European countries were experiencing, but after a year of use, there are still old and even new problems in the system. The assumption was that this "unification" of currency would bring economic stability and allow the Euro to be more like the U.S. dollar. Countries had to agree that their individual economy would grow at a certain rate and a breach in this contract would result in penalties. I believed that I would find data showing positive economic growth throughout the 12 countries. By checking the change in GDP of individual countries, I found that not all of the participants in this unification had succeeded to stay within the boundaries set by the EMU. I thought that by unifying to a common currency and spending billions of dollars to do so, there would be more stability for all countries involved with the Euro. But, that turned out to not be the case. Leaving me to ask, "How could a multi-billion dollar project end up not fulfilling all the expectations of those who designed and participated in it"?

In the beginning of 2002, the European Economic and Monetary Union (EMU) was formed and the common currency it introduced is known as the Euro. There are 12 countries participating in this currency unification and they consist of Belgium, Germany, Spain, Greece, France, Italy, Ireland, Luxembourg, The Netherlands, Finland, Austria and Portugal. In order to manage this new currency, the Eurosystem was created, which consists of a collection of Central Banks throughout Europe. One of the main reasons for the formation of the EMU is that there was fear that the Single Market would be endangered if exchange rates were not locked together.

The EMU had to collect valuable information about the European countries and what their economic status was. They collected such information as national debt, inflation rates, interest rates, exchange rates and budget deficits. One of the factors that the EMU stressed upon in order to qualify for admission was its debt to GDP ratio. This meant that countries had to have its debt less than 60% of its GDP. This posed a threat for many countries especially in the case of Italy in which they successfully met the deficit criteria but were not near the numbers to qualify as a result of its debt issues. Along with this and all the other information they were able to see which countries fulfilled the criteria and from there they would make their decision. Only one country, Greece, didn't qualify and the UK, Denmark and Sweden chose not to join.(Solomon)

In order to guarantee stability, a Growth Pact was agreed upon and it provided certain rules in which the countries involved had to obey. It consisted of a general rule that deficits should not exceed 3 percent of GDP, but if a country's GDP were to fall by 2

