

Fabio Panetta: Unleashing the euro's untapped potential at global level



SPEECH

Introductory remarks by Fabio Panetta, Member of the Executive Board of the ECB, Meeting with Members of the European Parliament

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The introduction of the euro has undoubtedly been one of the most profound changes in the international monetary system since the collapse of the Bretton Woods system. Right from the start, the ECB has monitored developments in the international role of the euro, not only in order to measure our currency's global appeal, but also because a stronger global role for the euro may have tangible consequences for the conduct of monetary policy.

Today, I would like to briefly present the main findings of our recent report on the international role of the euro. Next, I will discuss monetary policy considerations associated with a stronger use of the euro internationally, before moving on to the policies that could unleash the euro's untapped potential at global level. I will stress the alignment between policies that will strengthen the euro's role internationally and policies that will make the euro area more robust and fit for the future.

The role of the euro in global markets

The euro remains the world's second most important currency. This is one of the main findings of the [19th annual review of the international role of the euro](#), which we published on 9 June 2020. At around 19%, the euro's share in international currency is lower than the approximately 50% share of the US dollar, but well ahead of any other currency.

Developments since the outbreak of the coronavirus (COVID-19) pandemic have not changed the picture: investors rushed to the safety and liquidity of the US dollar in March 2020, confirming its pre-eminent role in the global monetary and financial system.

In some areas, however, such as the global green bond market, the euro has had a head start relative to the US dollar. In 2019, for instance, almost half of global green bond issuance was denominated in euro.^[1] The euro's leading role not only reflects the prevalence of green bond issuers based in the euro area; issuance of euro-denominated green bonds is also strong among non-euro area residents, which accounted for almost 30% of total euro-denominated green bond issuance in 2019. In the future, the swift implementation of an EU taxonomy of sustainable economic activities would provide a credible and standardised framework, ensure greater investor confidence and also contribute to strengthening the international role of the euro.

The effects of international currency status on the ECB's monetary policy

Since the launch of Economic and Monetary Union, the Eurosystem has advocated a policy of neutrality towards the international role of the euro.^[2] This position reflected two differing views – one that emphasised the economic benefits of international currency status, and another that emphasised the costs. Two decades on, the balance between these benefits and costs has shifted.

The [18th annual review of the international role of the euro](#), published last year, looked in detail at how the balance of benefits and costs has changed since 1999. With rapid financial globalisation, rising challenges to multilateralism and the adoption of new monetary policy frameworks by major central banks, the relevance of some of the traditional effects of international currency status has declined, while other effects have become more apparent.

For instance, international currency status strengthens the transmission of monetary policy, notably if stronger use of a currency as an international funding unit amplifies the cross-border effects of monetary policy impulses. Through spillback effects, the resulting impact on demand across the world may give monetary policy a wider, and possibly larger, domestic impact. This could be particularly true for an economy such as the euro area, which is more open to trade than other major economies.

Moreover, international currency status lowers exchange rate pass-through, which helps shield inflation from foreign shocks. It lowers external financing costs – the traditional “exorbitant privilege”. And finally, it can be argued that the traditional argument against a stronger international role for a given currency – that it increases the volatility of monetary aggregates – has declined in prominence.

All in all, changes in the global role of the euro may have consequences for the conduct of monetary policy, all of which must be understood and taken into account when designing the ECB’s actions.

Unleashing the euro’s untapped global potential

The euro’s global potential has not been fully realised, however. But the right policies could unleash it.

The ECB has repeatedly stressed that the international role of the euro is primarily supported by a deeper and more complete Economic and Monetary Union, including advancing the capital markets union, in the context of the pursuit of sound economic policies in the euro area. The COVID-19 pandemic underlines the urgency of these policies and the ECB supports the necessary reform efforts.

Moreover, as I have also stressed recently, the euro’s international role will grow only if we can better share its benefits, or “privilege”.^[3]

It is for Europe to provide common instruments that generate safe assets for all Member States in times of crisis, thereby ensuring that necessary fiscal reactions do not cause further instability and fragmentation. The €750 billion recovery fund proposed by the European Commission is an excellent example. It will provide a forceful European fiscal response to the COVID-19 crisis and the foundation for a deep, common capital market backed by safe euro assets. Unfortunately, however, the recovery fund is both temporary in nature and relatively small in relation to the size of the European sovereign bond market.

The ECB also plays its part. A global currency requires a central bank that acts as a credible backstop to safeguard liquidity conditions in the financial system. Over the past few months, the ECB has deployed forceful monetary policy measures to avoid fragmentation, dispel tail risks in financial markets and stabilise the euro area economy.

Yet the pandemic crisis has also made clear that, in times of stress, managing a global currency also requires the ECB to play a prominent role at the international level.

Shortly after the outbreak of the pandemic crisis, the ECB reactivated a number of swap and repo lines with major foreign central banks. On 25 June we went further still and established a new precautionary backstop facility to address pandemic-related euro liquidity needs outside the euro area. The Eurosystem repo facility for central banks (EUREP)^[4] reflects the importance of the euro in global financial markets and will support the smooth

transmission of our monetary policy. In particular, it will reduce risks related to sell-off episodes of euro-denominated assets and spillovers of market dysfunctions from other economies to the euro area, including through global confidence effects.

Looking beyond the immediate aftermath of the pandemic crisis, the acceleration of the digitalisation of money may have implications for the euro's global role.

Thanks to the recent launch of the European Payments Initiative, Europe has stepped up its efforts in meeting the challenge to create a true European and modern payment solution that meets the needs of both people and businesses.^[5] This is essential to ensure the autonomy of the European payments market, in the face of increasing dominance by foreign players.

The ECB will continue to monitor how new technologies change payment behaviours. Regardless of the choice of technology, the stability of money and payment systems should continue to rest on the firm foundations central banks provide. Maintaining the unit of account, guaranteeing the finality of payments, providing liquidity and conducting oversight remain essential public goods that are provided by central banks. They are paramount to maintaining trust in a currency and safeguarding monetary sovereignty.

This is why the ECB intends to remain at the forefront of discussions concerning the nature of money in a digital world, including the exploration of the desirability and feasibility of establishing a central bank digital currency (CBDC).

A CBDC would have domestic implications for the euro area in areas such as monetary policy, financial stability and payment systems, which would need to be thoroughly assessed.

But, if the CBDC is allowed to be used outside the euro area, it is likely to have implications for the global monetary and financial system too. For instance, the euro's international role could be strengthened if the CBDC represented an attractive payment vehicle or store of value for non-euro area residents. It could have implications for capital flows and the exchange rate of the euro, with potential knock-on effects on euro area and global economic developments. It could amplify the real and financial cross-border spillovers of domestic monetary policy shocks by creating a new channel for their propagation. The magnitude of such effects would depend on the design of the CBDC.

Conclusions

Allow me to conclude.

The euro became an international currency at birth.

How and whether this international status will evolve in the future remains in the hands of European policymakers. The European Parliament has a key role to play in delivering reforms that will further strengthen people's

confidence in the European project and in the euro.