A CANADIAN BUSINESS PERSPECTIVE ON THE EURO

Notes for remarks
at Euro-Canada 2002

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INTRODUCTION

Ambassador Smadja, ladies and gentlemen, it is a pleasure to be here today at the Ottawa workshop of Euro-Canada 2002.

In the next ten minutes, I will try to give you an overview regarding the introduction of the euro from the Canadian business perspective.

In the interests of time, I will forgo the important but myriad practical impacts of introduction of the euro for Canadian business. Instead, I will focus on the competitive and strategic impacts of the euro for Canadian business.

FROM BCNI TO CCCE:

However, at the outset, let me say a few words about the Canadian Council of Chief Executives. For the past quarter century, it was known as the Business Council on National Issues.

We began this year with a new name and a new mandate. Building on a remarkable twenty-five year record of success, we decided to re-brand ourselves worldwide and pursue a three-fold mandate. With a focus on Canada, North America and the world, our work is channeled through three standing committees: the National Policy Committee, the North American Policy Committee and the Global Policy Committee.

The Council’s Global Policy Committee is co-chaired by Dominic D’Alessandro, President and Chief Executive Officer, Manulife Financial and Robert E. Brown, President and Chief Executive Officer, Bombardier Inc. This committee concentrates on international finance, trade, investment and development policy as well as key multilateral, regional and bilateral relationships beyond North America.

This includes the forward agenda of the European Union, its relationship with Canada, and developments such as the physical introduction of the euro this past January. In this regard, I welcome Ambassador Smadja's positive comments and briefing this morning with respect to the outcome at the most recent Canada-European Union Summit. The commitment to take a closer look at the future of our relationship was positive news from the Canadian business perspective and we sincerely hope for a constructive outcome at the next Summit meeting this December.

THE EURO: GROSSO MODO

The euro is one of the few really new concepts or initiatives that has been introduced in the world in recent memory.

People no less illustrious than Milton Friedman, one of many outspoken euro-skeptics here in North America, have commented that: "Never in history, to my knowledge, has there been a similar case in which you have a single central bank controlling politically independent countries."

The introduction of the euro and the policies on enlargement as embodied in the Treaty of Maastricht represent two defining moments for Europe. Indeed, the Treaty of Maastricht itself represents a truly important and visionary text in the history of Europe.

As we all know, the euro has been the official currency in Europe for everything except essentially street transactions for the past three years.

Nevertheless, the historic conversion of Europe's financial system to the euro was quite impressive not simply because of its scope but because the transfer itself was so smooth.

Many have suggested that the euro is akin to building castles in the air, that it may be a major leap of faith or more negatively an act of folly. Let me go back to Friedman for a second and simply conclude that rather than an act of folly, the euro is clearly an 'innovation'. Any innovation implies some risk, and possible future stresses – which I will get to in a moment – but any adaptation in a changing environment implies risk.

THE EURO: A MACRO ASSESSMENT

The euro meets all of the key qualifications of a major international currency – a sound currency. The mandate of the European Central Bank (ECB) to maintain the stable purchasing power of the euro is firmer than many if not all other central banks.

In total, the size of the twelve economies embracing the euro is roughly equal to that of the United States.

The euro has become the second major currency in bond markets. As of October 2001, the world share of bonds denominated in euros was 39 percent versus 46 percent for the United States. The euro financial system is rapidly approaching the size of that of the United States and has integrated quite rapidly into the world financial system.

In addition, the greater depth and liquidity of financial markets in the euro area have facilitated the development of financial instruments such as mutual funds and commercial paper.

This process of greater integration in European financial markets has coincided with a trend towards greater globalization and securitization already well underway.

The single currency with its greater depth and liquidity of financial markets has completely removed exchange rate risk for exporters and importers, and debtors and creditors across the twelve countries of the euro area. This means that the costs of hedging exchange rate risks vis-à-vis other euro area economies has been eliminated and means lower financial costs for corporations selling in Europe. This provides more euro-based opportunities for investment and financing.

Cross border trade, investment and financial transactions are facilitated, and, in particular, small and medium-sized enterprises are more encouraged to conduct business in euro zone markets. Other things being equal, the result is improved competition, better resource allocation and a more positive investment climate.

Monetary policy has achieved low inflation and low inflation expectations while keeping low nominal rates. This means that monetary policy credibility has been achieved.

Financial stability has also been achieved in the wake of the tragic events of September 11, 2001. The ECB injected liquidity into global financial markets to minimize volatility stemming from the terrorist attacks.

The final element of macro stability from the perspective of the euro is fiscal stability. Overall, the Growth and Stability pact and structural reforms put in place over the past three decades have resulted in a degree of convergence on deficits and debt and have also contributed to a more stable environment. However, there are and will be ongoing pressures.

The result is that euro reinforces macroeconomic stability in the form of exchange rate stability (internally), price stability, financial stability and fiscal stability (within the confines of the Growth and Stability pact).

THE EURO: MICROECONOMIC ASSESSMENT

The microeconomic benefits of the euro are all well know to us and include:

- increased price transparency for importers in particular;
- increased competition and productivity;
- progressive price harmonization in the euro zone;
- lower transaction costs resulting from less hedging and lower to negligible exchange rate risk within the euro zone.

The creation of the euro zone, with its increased size, also has the potential to lead to greater merger and acquisition activity and to improve the pricing mechanism for imports and exports.

The bottom line is that a single currency with a fully developed single market will improve trade and competition through the elimination of exchange rate risk and through more transparent prices; it will reduce transaction costs, again increasing trade and investment; it will benefit everyone traveling in Europe; and it will lower long-term interest rates, again good for investment, growth and jobs.

EURO ZONE FINANCIAL SYSTEM CHALLENGES

In the area of stock markets, a number of benchmark indices now exist for the euro area as a whole. As well, derivatives markets have been established promoting a sector perspective to financial decision-making. But the euro zone financial system has had its challenges.

There are reforms required with respect to the somewhat fragmented financial system. There are also institutional barriers holding back the development of a single market for money. Securities-market regulations are still not harmonized. With the exception of Euronext, most stock markets are still national in scope. Also, there are still multiple settlement systems in place across the euro zone.

Reform in these areas would obviously enhance the stature of the euro in the international arena. This is a familiar refrain in the Canadian context as well. Most recently, the Chief Executive Officer of the Toronto Stock Exchange has suggested that our securities markets also need greater consolidation – a position supported by the Canadian Council of Chief Executives.

COMPETITIVENESS IMPLICATIONS: ONE CURRENCY – TWELVE ECONOMIES

Monetary union by itself is insufficient. Further policy measures will be needed to shore up the success of the single currency and to ensure that the macro and micro benefits alluded to above can be fully realized with the hardest part of integration to come – moving to a single market.

The European Round Table of Industrialists (ERT), a counterpart organization to the Canadian Council of Chief Executives, has suggested that the euro zone plus the so-called ‘pre-ins’ should be the world’s most competitive and dynamic knowledge-based economy by 2010.

The ERT has highlighted the following competitiveness issues on the road to a single market:

- active labour market measures to introduce greater labour market flexibility and dynamism;
- integrated securities and risk capital market by 2003;
- liberalization of European energy markets;
- an internal market in services;
- a single consolidated corporate tax base;
- simpler and higher quality regulations;
- increased research and development, infrastructure, patenting, training and skills creation.

Frankly, this list of suggested micro reforms has many similarities to the Canadian Council’s recommendations for action by Canadian governments.

Indeed, if I may depart from the euro topic for a moment, the goal of the Canadian Council with respect to Canadian prosperity is simple: to make Canada the best place in the world in which to live, to work, to invest and to grow. We need to make Canada a more attractive place for companies to put their head offices here and to invest in this country.

The single currency needs a single economy in which to operate. European business has already begun to press for the elimination of overt and tacit barriers between countries that prevent the European Union from becoming a true single market.

Indeed, many have concluded that these and other reforms leading to a single market may be the logical consequence of the euro. Still others have suggested that the euro may in fact act as a catalyst to spur on some of these moves toward further economic integration.

But the point is that the impediments facing small, medium and large enterprises in Europe are the same ones facing their Canadian counterparts – those I have already mentioned as well as the perennial issues related to regulatory, administrative and legal impediments to trade and commerce and to the mobility of labour.

CONCLUSION:

Many have suggested that a currency is a very important symbol of national sovereignty. This is debatable.

However, in the euro zone context, it is clear that citizens of the euro area have acknowledged the economic benefits of a single currency. They further were prepared to give up the use of their own national currencies in favour of the euro.

The next step in this grand project will be to eliminate other forms of barriers between the countries in the euro zone.

Thank you.