

Speech

Deputy Governor Stefan Ingves

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Retail trade, EMU and the euro

Swedish Retail Federation

First a word of thanks for the invitation to speak about EMU. Less than twelve months have passed since the Riksbank last attended a meeting of the Swedish Retail Federation with information about EMU. Perhaps some of you were present on that occasion. Whereas the issue of EMU was still fairly new a year ago and not much discussed by most people, the situation today is different. In the interval we have experienced a marked increase both in what people know about EMU and in their interest in the matter. This naturally has to do with the rapid approach of the starting date. Today the move to Stage Three lies fewer than 500 working days ahead. Moreover, there is no mistaking the strength of the political determination in Europe to start on time. This was evident not least at the recent Ecofin meeting in the Netherlands when the EU finance ministers agreed on several important matters such as the stability and growth pact and ERM2.

Today I shall be outlining the process leading up to Stage Three of EMU and the changes that we already know will occur. I will also say something about EMU's consequences for retail trade.

Before considering practical aspects of EMU, permit me to begin with a look at some general economic features.

Sweden should join from the start

The Riksbank is in favour of Sweden participating in the euro area right from the start in 1999. The reasons for this have been spelled out in our submission on the

SVERIGES RIKSBANK

Telephone
+46 8 787 00 00

Telefax
+46 8 21 05 31

E-mail
registratorn@riksbank.se

Calmfors report, for example. As regards the economic arguments, we do not believe that, by remaining outside the euro area, Sweden would incur particularly large costs for stabilisation policy; in the event of economic shocks, it is structural changes rather than monetary policy that should be used in the first place to counter rising unemployment, for instance. On the political side, we share the report's assessment that the political costs of not participating would be substantial; as an outsider Sweden would not belong to the inner circle of countries that will be deciding Europe's future. It should also be realised that countries which belong to the euro area from the start will have more influence on how the European Central Bank (ECB) develops in the crucial early years, when the forms for its work are being established. Our possibility of influencing important decisions is also likely to be reduced in other fields beside monetary policy. If Sweden were to refrain from joining the euro area at all, there would be a risk of being marginalised as an outsider.

The preparations

What progress has been made in the move to EMU? The work of preparing for Stage Three is now in full swing in every EU body and all the member states.

A green paper on the practical arrangements for a changeover to a single currency was presented by the Commission in May 1995 and the European Council, meeting in Madrid in December, adopted a changeover scenario which fixed the timetable for the main decisions. It was agreed that Stage Three of EMU is to start on 1st January 1999 and that, in the light of which member states fulfil the convergence criteria on the basis of statistics for 1997, as early as possible in 1998 the Council is to confirm which countries will participate in the European currency area. On 1st January 1999 exchange rates are to be locked and responsibility for monetary policy is to be transferred to the ECB. The euro is to be introduced as an independent currency and all monetary policy transactions are to be in euro. For a time the national currencies will continue to circulate alongside the euro but legally they will be one and the same currency. If this seems odd, remember that Sweden's currency, for example, can be expressed in kronor as well as öre. Euro, however, will not be available for our wallets from 1st January 1999; euro banknotes and coins are to come into circulation on 1 January 2002 at the latest. That will initiate a massive exchange of existing national banknotes and coins. By 1st July 2002 at the latest the krona will cease to be legal tender, though of course the Riksbank will continue to exchange kronor for euro.

Which countries will be included?

The EU countries are now striving to fulfil the economic criteria for participation in the euro area. This is being accompanied by strenuous political efforts to remove any remaining obstacles. Today I can only say that it is not until the spring of 1998 that we will actually know which countries will be establishing the union. The EMI and the Commission will each be publishing a report and the Commission will issue recommendations on which countries should participate. On the basis of these reports and recommendations, the opinions of the European Parliament and the

national parliaments are to be heard, which is expected to occur in April. The decision about which countries will participate is to be taken around the turn of April at a weekend meeting of the Ecofin Council and the Heads of State or of Government. It is therefore unnecessary to speculate about this today. As far as Sweden is concerned, it looks as though we will in fact fulfil the convergence criteria. Whether or not we participate will therefore depend on the decision by the Riksdag (Sweden's parliament).

What is the Riksbank doing?

The Riksbank has to contribute to a situation whereby Sweden is able to participate in practice if a majority in the Riksdag so decides. That is why preparations are already necessary. A basic principle in this work is that it shall be voluntary - the requisite adaptations are a matter for each organisation to decide. All those concerned must of course also solve any problems they encounter as a consequence of EMU.

For the Riksbank, a highly important task in Sweden's preparations is information about and consultations with the financial sector on matters to do with the changeover. To this end we have formed a consultative group (SIFS) and five sub-groups to work on the practical preparations together with the financial sector. This collaboration has led us to conclude that the financial sector can cope with a changeover to euro on 1st January 1999. We also consider that in some respects joining later would make the preparations more difficult. The worst alternative would be a long period of uncertainty about our participation, what we usually call a "soft no". Costly double systems would then be required in several areas. We have also observed concern in the financial sector that staying outside the euro area would entail increased costs, competitive disadvantages and risk various forms of discrimination.

"Wait-and-see" may be less attractive

A common opinion at present seems to be that a soft no is not unlikely and would not involve appreciably higher economic costs than participation from the start. Deferring participation for some years would not exclude us from the euro area for good.

In our cooperation with the financial sector, however, we have seen that uncertainty about participation is causing many financial agents to make preparations for handling euro as well as kronor. The nub of the matter is that euro services will be called for whether or not we join the area. The use of euro will be directed by the market. Naturally the euro would not replace the krona as Sweden's currency if we remained outside but we could probably expect a demand for euro from some agents. According to the Stockholm Stock Exchange, trading in the shares of major companies will gradually switch to euro because handling two currencies would be too costly. In time the money and bond market may be affected in that renewals and new issues are denominated in euro and account for a growing proportion of bond trading. According to the Securities Dealers Association, for instance, large companies and financial markets will also become less interested in kronor. It is too early to say how this transition from kronor to

euro will occur in detail. Neither can we foresee how quickly it will proceed or how far. Probably it will be gradual and ultimately also affect private individuals. If the euro turns out to be stable and strong, households will also prefer to have pension savings, for example, in euro securities. Thus, this scenario points to a development where financial markets, companies and even individuals are active in euro, while the public sector continues to use kronor as declared, for instance, in the report from the Ministry of Finance on practical preparations for the euro. Such a situation would no doubt lead in time to the public authorities also encountering a demand for euro services, perhaps ultimately leading to the euro being accepted to a greater extent than desired at present. If so, the "wait-and-see" alternative would finally amount in practice to the adoption of the euro. We can only speculate about the practical consequences of a gradual transition but it would probably entail increased costs as well as greater uncertainty for firms as well as society. If we intend to join the euro area in a not too distant future after 1999, the recommendation therefore seems to be: participate from the start and avoid unnecessary and costly solutions for firms as well society.

Still a large need of information

When talking about the monetary union we should be clear that in Sweden the debate about Europe and EMU is relatively new. Elsewhere in Europe the issue of integration has been discussed much more and for far longer. The debate in Sweden has been rather low key and not particularly widespread. So it is hardly surprising that people here are hesitant and want more information. That the discussion has now got going is all to the good.

I was therefore pleasantly surprised by the submissions to the Ministry of Finance on the EMU report. Of 56 submissions, only 4 were negative about EMU. The proportion in favour of Sweden participating from the start in 1999 was as high as 46 per cent, while 13 per cent wanted to wait and see and 33 per cent did not voice an opinion about participation. Many of the interested parties are for EMU: the Federation of Swedish Industries, the Retail Federation, the Bankers' Association, the Confederation of Professional Associations and the Employers' Confederation, to mention just a few. In general it seems that the discussion of EMU has spread from the financial sector to companies, authorities and large organisations but has not yet reached the man in the street. The time ought now have come for us all to consider the matter.

How does EMU affect retail trade?

The details of how EMU will affect retailing in Europe are not yet clear. We do not even know which countries will make up the euro area from the start. Still, I shall try to present some general features. EMU is intended to strengthen and deepen European integration and promote the mobility of capital, goods and services. In time, therefore, a single currency is likely to make retailing more efficient and cheaper. Inside the area, prices will be more transparent and there will be no exchange risk.

Decreased costs for currency exchange and hedging suggest that in time retailing will benefit from EMU, an opinion I share with the Wholesale & Retail Research Institute. In the short run, however, the union involves retail trade in a great deal of work. Shops will be in the firing line when the euro notes and coins are introduced. Cashiers will have to handle kronor and euro side by side for a time and customers will no doubt have many questions about prices and conversion rates. Besides calling for resources as well as training, this will require a good deal of adjustment in retail trade. I shall now consider some of the foreseeable changes and also take this opportunity of commenting on the requirements formulated by the Research Institute for a changeover to euro.

Banknotes and coins

The Madrid meeting in 1995 agreed that euro notes and coins are to be introduced at the latest by 1st January 2002. Many people have reacted to an introduction at the turn of a year, which is when retailing tends to be most hectic. The agreement, however, stipulates 1st January 2002 as the *latest* date, so perhaps a start might be made in the autumn of 2001. The alternative of spring 2002 has also been mentioned. This matter is still being discussed; the Riksbank shares the trade's opinion that the turn of a year should be avoided and is therefore working for another date. The timing of the practical changeover arrangements is to be decided by each country; for Sweden the Riksbank hopes that it can be managed in a much shorter period than the maximum of six months. The public will be informed in good time about how the changeover is to be carried out. Information about security details and appearance will also be made available. We now know that there will be seven banknotes and eight coins, which is somewhat more than Sweden's denominations at present. One face of the coins will carry a national motif that each country decides. The notes may also display a national symbol.

Nickel in the coins?

The question of nickel in the coins has also been discussed, for instance among finance ministers and central bank governors. Swedish retailers have demanded that coins denominated in euro and cent are not to contain nickel; the Riksbank and the Ministry of Finance have both worked hard to achieve this but are fighting rather a lone battle. Today it does look as though four to six out of eight coins will be nickel-free, which must be regarded as a major success for the Swedish position. A decision, however, is not due until the summer.

Double currencies

For a period of up to six months there will be two currencies to handle and retailers have demanded that the period be limited to three months. We can understand their argument in principle. Much will be required of traders. Instead of the present five denominations of notes there will be twelve and instead of four coins there will likewise be twelve. The value of cash holdings in retail trade (cash liquidity) will be greater than usual, with an increased risk of counterfeit notes and robbery, for example. Retailers will also have to consider temporary storage space for cash-boxes and additional transport requirements. The Riksbank is likewise

working to make the period with double currencies as short as possible. There are, however, other aspects to consider. Incorporating euro in the system will take time. Just the work of distributing the new banknotes will be time-consuming. We shall be looking into what is feasible in practice. Time will also be needed to adapt the automatic teller systems (Bankomat and Minuten) to the new currency. Another matter to be investigated is whether the distribution of euro to banks, post offices and possibly retailers can start before the date on which the new currency becomes legal tender. Moreover, some consumer interests, for instance, have said that many consumers would prefer a relatively long changeover period in which to get used to the new currency. The question of the period with double currencies therefore calls for further discussion in order to arrive at a solution that everyone can accept.

Retailers have also put forward the view that it should be possible to provide change only in euro from day one. We believe this may be difficult both in practice and on the grounds of the accepted changeover principle of "no compulsion - no prohibitions". It has been said that people in general are to be free to decide whether to use euro from the start on 1st January 1999 or to wait until the changeover is completed in 2002. During this period no one is to be compelled to use euro, though this will be encouraged. Kronor and euro will both have the status of legal tender, so we must be prepared to handle them both during this period. But the discussion of this question should continue.

Responsibility for information

The retail trade report considers that society must be responsible for information about the new currency system. At the same time the Ministry of Interior and others consider that information at points of sale, for example, is primarily a business responsibility. This makes me somewhat uneasy. I believe we must all be prepared to accept an additional responsibility for information about these matters. Otherwise there is a risk of people feeling they are getting insufficient guidance, with an increased risk of the changeover being arduous for everyone. At the Riksbank we will try to do our bit. Brochures about the new means of payments will be distributed, possibly accompanied by ready-reckoners for the conversion rates. Our Payment System Department is working on this.

Price information

Retailers will be obliged to work for a period with some form of double pricing. The practical arrangements for this are mainly a matter for the retail trade and consumer interests.

Rounding

In Sweden we have grown used to having the total sum rounded to the nearest 50 öre. Retailers have expressed a wish that this should continue to be possible with the euro, in which case an active introduction of the 1 and 2 cent coins would not be called for and we could round to the nearest 5 cents (approximately 43 öre). We appreciate this view and have promoted it at various levels but without gaining much support. So we do not yet know the outcome.

It must be realised, however, that if we join the euro area, even the smallest denominations will be legal tender. So there is no way of entirely avoiding the small coins in Sweden.

Cash receipts

Today's cash registers are capable of recording total sums in two currencies. If each item is to be registered in both currencies, however, it seems that all the existing cash registers would have to be replaced. I agree intuitively with retailers that it would hardly be reasonable to do this throughout Sweden in order to register two currencies for a period that is likely to be shorter than six months. Perhaps we can make do with receipts that give the total in euro as well as kronor together with the conversion rate. That would be much the same information as the banks have agreed to provide on statements of account. Once again, however, this is a matter where retailers and consumers must get together and discuss what is reasonable.

As I have said, EMU will affect each one of us. So let me conclude by mentioning some other changes in fields where retailing is not directly involved.

Other changes

Securities The countries in the euro area may, and should, denominate new sovereign issues in euro. A country wishing to convert its outstanding debt into euro will be allowed to do this, too. We can also pass national laws enabling, for instance, the Stockholm Stock Exchange, OM and the Securities Register Centre (VPC) to switch to euro right from 1999. Many institutions and agents are in favour of this. The above institutions as well as participants in the Swedish securities market, banks, financial institutions and others unanimously recommend a big-bang solution - a quick, concerted changeover from kronor to euro right from the beginning of 1999.

With a single monetary policy and no exchange risk, the only factor behind interest rate differentials for sovereign securities will be the credit risk. The market for Swedish government paper will be more or less integrated with the euro market for government securities. Given a reasonably similar debt situation, government bonds issued by different countries can then be handled in a similar way.

Banks. During 1996 the banks have worked on strategies and routines for changing over to euro. It has been agreed that during the changeover period banks, the postal giro, the bankgiro and the private giro will handle kronor as well as euro. Cashiers will redenominate payments in the currency used for the institution's system, regardless of which currency the customer has used. Bank branches will provide two versions of their forms, one for kronor and one for euro; new cheques and other forms will therefore be produced. Statements of account will specify the rate at which the currency has been converted. The automatic teller systems (Bankomat and Minuten) will also have to be adapted.

Moreover, banks must be prepared for people who want to make giro payments in euro right from the beginning of 1999. Some large companies may also wish to pay out wages in euro before the new currency is available in the form of banknotes and coins. As mentioned earlier, it is difficult to foresee the magnitude of demand

for euro services and how soon companies and individuals will switch from kronor to euro.

Monetary and exchange rate policy. A single currency implies a single monetary policy, which in EMU will be decided by the ECB. The Riksbank and the other national central banks will have the task of executing this policy. The changes for Swedish banks and other financial institutions will probably not be all that great. The Riksbank is likely to remain the financial sector's counterparty. The main differences from today for Swedish banks are a much larger market for intra-day money and counterparties located all over Europe.

The detailed conduct of monetary policy is not yet clear. The final decisions are due when the ECB has been established in 1998. Consequently it is the countries participating from the start that will be able to influence the conduct of policy and the organisation of activities in the new European central bank.

Target. The conduct of a single monetary policy calls for a single system with which to handle the associated payments. TARGET, the payment system that is now being built up, will link up all the national systems. A payment from, say, Stockholm to Milan will normally be executed in a matter of seconds, whereas at present it often takes a day or more. TARGET's main purpose is to enable the ECB to conduct monetary policy but it also amounts to the establishment of a new expressway for commercial transactions. The extent to which banks and other companies use the system will probably depend on the price. What this will be is not yet clear but costs are to be covered in full.

All the national central banks in the EU area will be entitled to join TARGET, whether or not they are participating in the euro area. There is a significant risk, however, that countries outside the latter area will have more limited possibilities of using TARGET, for instance due to restrictions on intra-day euro credit, which is important for countering fluctuations in payment flows. One of the matters discussed is that outsider banks should close the system at an earlier hour. The Riksbank has acted forcefully to oppose this threat of discrimination. The decisions on this and certain other matters have been deferred, however, and will now be taken by those countries that join the euro area from the start. TARGET is to be tested this summer and is to be fully ready for use by 1st January 1999.

Summary and conclusions

Most of the evidence today suggests that the economic and monetary union will move to Stage Three on 1st January 1999. For Sweden the question is whether we should join the euro area from the start, wait a while or try to remain outside for good. I hope that we will soon be having a more lively debate on this very important issue. The question of EMU has now been largely examined and discussed by the financial sector, the authorities and big businesses. The time has come to spread the debate and information to other groups in society.

In time the krona will lose ground

Even if Sweden decides to stay outside, the single currency will affect us. Our analyses, together with other organisations, of what might happen in that event point to a relatively sizeable use of euro, particularly in the securities market. In

time, the use of euro may spread like water rings to other parts of society. The extent to which the euro is used will among other things depend on its strength relative to the krona but also on market assessments of the probability of Sweden joining. A good guess seems to be that the shorter the interval before participation, the quicker will be the changeover to euro.

The world will not be the same

The creation of a monetary union just outside Sweden's borders will change the world as we know it. Individuals and firms will both be affected by the euro's introduction whether we participate or not. In our efforts to keep the financial sector informed about EMU we can see that good progress has been made with the preparations. Among those concerned we also experience a strong desire to participate as early as possible so as not to get left behind. Swedish banks and other companies want to have a chance of competing on equal terms and do not wish to risk losing business opportunities.

Finally I therefore wish to underscore that saying no to the single currency is not the same as status quo. As I said, the euro's introduction will affect us all, whether or not we participate. EMU will probably accelerate the globalisation, concentration and integration of the world's financial markets. It is therefore of the utmost importance that we all do what we can to find out more about these complex matters.