Robert Holzmann: The euro in Central, Eastern and Southeastern Europe (CESEE)

Opening remarks by Dr Robert Holzmann, Governor of the Oesterreichische Nationalbank, the Austrian central bank, at the Conference on European Economic Integration (CEEI) 2024, Vienna, 21 November 2024.

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Ladies and gentlemen,
honorable guests, esteemed colleagues, dear participants,

It is a great pleasure for me to welcome you to this year's Conference on European Economic Integration. I am very pleased to see that so many distinguished experts and colleagues have come to discuss the euro in Central, Eastern and Southeastern Europe (CESEE).

We picked this topic for two reasons. First, 2024 marked the 25th anniversary of the introduction of the common European currency, which crowned more than seven decades of European integration. Second, the string of recent crises – including the energy and high inflation crises – has sparked an intense debate in the dynamic CESEE region about the advantages and disadvantages of adopting the euro participation compared with keeping their national currencies.

At this year's conference, we are also commemorating Olga Radzyner, former head the OeNB's Foreign Research Division. She was a trailblazer for our bank's research focus on CESEE. 25 years ago, Olga Radzyner died with her family in a tragic accident.

Olga Radzyner already studied the role of the euro in CESEE and the prospects for monetary integration at a time when the euro area was just about to come into being. Her dedication and commitment laid the foundation for the OeNB's extensive and well-established expertise on the region. A warm-hearted person and born networker, Olga Radzyner set up an outstanding network of international experts, connecting people from East and West and from many different institutions. We are proud to preserve her legacy by continuing to build on this network with our annual CEEI conference, honoring her memory now and in the years to come.

To set the stage for our conference topic, let me draw a historical parallel which offers valuable context for our discussions today. Roughly one hundred years ago, Europe witnessed the dissolution of a powerful transnational currency area – the Austro-Hungarian currency union. The breakup went hand in hand with the disintegration of the Habsburg Empire itself, one of the most influential political entities in European history. For over a quarter of a century, the Austro-Hungarian krone, or crown, had circulated as a single currency. As such, it fostered economic ties and trade across vast territories that are today divided into a number of modern nation states.

When that union fell apart, its currency did so, too. And the successor states of the empire established national monetary systems. Central banks emerged across the region as guardians of these new currencies. These central banks represented not only monetary sovereignty but also newfound national identities. As you know, the term "crown" for legal tender has not completely disappeared. Notably, the koruna, or crown, has persisted to this day in one of the empire's successor states, Czechia (formerly Bohemia and Moravia).

It is fitting, then, that we take this opportunity in 2024 to commemorate the centennial of two important central banks in CESEE: Magyar Nemzeti Bank of Hungary and Bank Polski SA, the predecessor of Narodowy Bank Polski, the central bank of Poland. Their establishment one century ago marked the beginning of a new chapter for their countries that was characterized by the interplay of national sovereignty and monetary stability.

In many ways, today's conversation about the role of the euro in CESEE echoes the challenges and opportunities these newly established central banks faced a hundred years ago. Back then, Europe was grappling with questions of monetary – though not only monetary – independence, integration and cross-border cooperation. Today, we are revisiting these same questions, albeit in a different context: in the context of a new transnational currency – the euro – a currency that has, over the past two decades, transformed Europe in profound ways.

Historical milestones for Europe: the euro and eastern enlargement

Two key milestones have shaped Europe in the recent past: (1) the introduction of the euro and (2) the EU's eastern enlargement. Separated by only a few years, these two events have had an enduring impact on European integration and have had a profound influence on the CESEE countries.

Launching the euro as an accounting currency in 1999 and as physical cash in 2002 was an unprecedented step toward deeper economic and monetary union in Europe. For the first time, millions of citizens and businesses across the continent shared a currency, which facilitated cross-border trade, travel and investment in ways that would have been unimaginable just a few decades earlier.

Despite pessimistic predictions, at 25 years, the euro has reached young adulthood. It has not only fulfilled its primary purpose – maintaining price stability – but it has also demonstrated sufficient resilience to withstand several shocks, crises and challenges. During turbulent episodes in particular, the euro has served as a key economic anchor not only for countries within but also outside the euro area, especially in CESEE.

In addition to being a global currency, the euro has become a symbol of unity and of European integration. And it is a testament to Europe's commitment to a shared future.

The second historic moment for Europe, just a few years after the euro had been introduced, was the European Union's "Big Bang"-style eastern enlargement in 2004, when eight central and eastern European countries joined the EU. This marked the most significant expansion in the history of the EU, bringing in nations that had long been on the periphery of European integration. A few years later, three more CESEE countries became EU members, and today, several other countries in the region are preparing to join the club in the foreseeable future.

For many of these countries, EU membership represents the culmination of years of reform, democratization and economic restructuring. But it also raises important questions about their future monetary paths – specifically, whether and when they would join the euro area. In principle, all EU member states are obliged to introduce the euro once they fulfill the convergence criteria. The only exception in legal terms is Denmark, whose "opt-out clause" exempts the country from the obligation to adopt the euro.

Of the eight CESEE countries that joined the EU in 2004, five have since adopted the euro. Slovenia was first in 2007, followed by Slovakia in 2009, Estonia in 2011, Latvia in 2014 and Lithuania in 2015. More recently, we have seen further progress. Croatia became a member of the euro area in 2023. And Bulgaria has been preparing for euro are membership; it started participating in the Exchange Rate Mechanism II in July 2020.

The path toward euro area membership remains open and attainable for those willing to meet the necessary criteria. Each of the new member countries underwent a rigorous process of economic convergence to meet the Maastricht criteria and align their monetary policies with those of the Eurosystem. Their experiences offer valuable insights into the benefits and challenges of joining and functioning within the euro area, insights that are particularly relevant for countries that have yet to become members.

The euro exerts a decisive influence beyond the euro area

This brings me to the point where I would like to emphasize that the euro's influence extends far beyond the formal boundaries of the euro area. Even non-euro area countries remain deeply interconnected with the euro area: They experience spillovers from the ECB's monetary policy as they maintain significant financial, trade and real economy ties with euro area countries. The euro is often used in these countries for trade invoicing, financial transactions, as a store of value and as an accounting unit in national enterprises even if the countries retain their national currencies. In short: Although they are not yet part of the euro area, the euro is present in these economies already in many ways.

This is especially true for countries with a high level of unofficial euroization or, even more so, for countries that have unilaterally adopted the euro as legal tender. This creates complex dynamics: While these euroized countries benefit from the stability and credibility of the euro, they also face significant costs and risks. The challenges range from their own monetary policy being less effective and efficient in addressing adverse spillovers to the fact that the scope for addressing such issues is limited as the countries are not part of the euro area's decision-making bodies.

This raises important questions: How should non-euro area countries – especially highly euroized ones – balance the related benefits and risks? And what role should the euro area institutions play in supporting these countries as they navigate such challenges?

In this context, I would like to stress that the ECB and the Eurosystem are fully aware of their responsibility as guardians of a global currency and of financial stability. In particular, euro area institutions provide liquidity lines to non-euro area central banks under certain conditions to address possible euro liquidity needs in the event of market dysfunctions. More specifically, the Eurosystem's swap and repo lines are monetary policy instruments which help prevent tensions in international funding markets that could otherwise hamper the effective transmission of monetary policy within the euro area.

I can proudly say that the Oesterreichische Nationalbank strongly supported the creation of the Eurosystem's current repo facility, the so-called EUREP. It was established in swift reaction to the disruptions caused by the pandemic shock. Based on this recent experience and ongoing geopolitical tensions, the Eurosystem has adapted its framework for euro liquidity lines so that it will be able to respond to future funding shocks in a more agile and flexible manner.

Lessons from recent crises

The keyword "shock" brings me to the next topic, which I touched upon earlier and would now like to elaborate on. The past two decades have been marked by a series of profound crises that have tested the resilience of economies across Europe, both within and outside the euro area. The Global Financial Crisis of 2008, the subsequent sovereign debt crisis and the COVID-19 pandemic have all had significant economic and social impacts on the global economy in general and on the euro area and the CESEE region in particular. More recently, the energy crisis of 2022–2023, primarily caused by Russia's invasion of Ukraine, and the parallel inflation crisis have further intensified these challenges.

For euro area countries, these crises have driven home the value of belonging to a larger, more integrated economic bloc. The ECB's monetary policy response to the Global Financial Crisis and the subsequent sovereign debt crisis, for example, played a crucial role in stabilizing the euro area's financial system and restoring confidence in the euro. On a broader scale, the coordinated monetary and fiscal responses to the COVID-19 pandemic, including the NextGenerationEU recovery fund, provided critical support to all EU countries. This helped them manage the economic fallout from the pandemic. Yet, it is important to emphasize that the aftereffects of the extraordinary fiscal and monetary measures implemented during the pandemic now need to be carefully contained, unwound but also critically evaluated to ensure long-term stability.

Non-euro area countries experienced the crisis episodes in quite different ways. Some CESEE countries faced significant challenges, including currency volatility, fierce recessions, rising inflation and unemployment. Others fared better in navigating the crises. In certain cases, the advantages provided by flexible exchange rates and independent monetary policies may have played some role.

In many countries outside the euro area, the recent crises have reignited debates about the risks and benefits of joining the euro area. Deliberating such a move involves comparing it with the advantages of maintaining autonomous and potentially more flexible monetary policies and exchange rate arrangements.

These issues are, of course, primarily debated among economic experts and policymakers. However, it is equally revealing to contrast expert discussions with perceptions at the grass roots: How do people view the euro, relative to national currencies, and how have their views been affected by recent crises?

Here, the periodic OeNB Euro Survey offers valuable insights. Since 2007, we have been surveying individuals in CESEE countries that have not adopted the euro. The survey shows that in these countries, on average, trust in the euro is higher than trust in the national currencies. In several CESEE countries, including some EU member states, this trust gap is surprisingly wide: Trust in the euro is sometimes more than twice as strong as trust in the local currency. This relatively solid trust in the euro is one of the factors shaping the extent of unofficial euroization. Trust in the euro tends to strengthen even further, compared to trust in national currencies, during crises such as the recent energy and inflation crises.

In recent survey rounds, respondents were also asked whether they believed the euro has had a positive or negative impact on euro area economies. 25 years after the introduction of the euro, it is only in Bosnia and Herzegovina, Hungary and Romania that a majority of respondents think the euro has had a positive effect. In Czechia, by contrast, less than 40% of people interviewed share that view, while around one-third of them believe the euro has had a negative impact.

This microdata evidence clearly shows that the euro remains a hotly debated topic, capable of dividing opinions not only among experts but also among the public.

Ultimately, however, and in economic terms at least, the question of whether and when to adopt the euro boils down to the critical issue of convergence: Should countries first achieve a high level of economic alignment with the euro area before joining or can adopting the euro itself help accelerate the convergence process? While the Maastricht criteria remain the key legal benchmark for assessing a country's readiness for euro adoption, recent experience suggests that economic convergence is not a one-size-fits-all process. Some countries may benefit from adopting the euro earlier during their convergence journey, while others may need more time to align their economies more closely with the broader euro area.

Completing the Single Market: the next chapter

Such considerations might be perfectly valid from the perspective of individual countries. However, from the euro area's standpoint, achieving and maintaining a high level of economic convergence among its members is essential to move closer to the economic ideal of an optimal currency area. Although the euro has shown remarkable resilience and strength over the past quarter of a century, we cannot afford to rest on our laurels. The euro area is still far from being a textbook example of an optimal currency area.

As we look ahead, one of the key challenges facing the euro area is the need to complete the Single Market, particularly in the areas of banking and capital markets union. Despite the progress that has been made over the past two decades, significant gaps remain in the integration of Europe's financial markets. These gaps not only limit the resilience of the euro area but also hinder economic convergence across the broader European Union.

The Letta Report of early 2024 is a timely reminder of the benefits that can be achieved by reinforcing and completing the Single Market. By eliminating the remaining barriers to cross-border trade and investment, we can create a more integrated and efficient financial system – one that supports innovation, growth and job creation across Europe. At the same time, a more integrated banking and capital markets union would help mitigate the risks of future financial crises by enhancing the stability of Europe's financial system.

Similarly, the recent Draghi Report refers to the importance of building greater fiscal capacity at the European level to complement monetary union. The euro area has made significant progress in recent years, particularly with the creation of the European Stability Mechanism and , also with the NextGenerationEU recovery fund. However, more homework, more realism and more efforts are needed to strengthen Europe's fiscal architecture and ensure that the euro area is prepared to respond to future crises.

To finish on a positive note, even as we acknowledge the work that remains to be done, it is also important to recognize how far we have come over the last 25 years. We should remember that the process of building a fully integrated economic and monetary union is not a quick one. Large-scale monetary unions take time to develop and mature. It took the United States, for example, over a century to establish the Federal Reserve and to create a unified monetary system. Europe, by comparison, has made remarkable progress in just a few decades, but we must remain mindful of the challenges that lie ahead.

The next 25 years will be crucial for the euro and for the broader European project. We must continue to work toward completing Economic and Monetary Union. And we must complete the banking union and build a capital markets union. At the same time, we must remain flexible and open to new ideas, recognizing that the path toward deeper integration will require ongoing reform and adaptation. Having now shared some ideas, I look forward to our discussions. My special thanks go to our distinguished speakers and panelists and to all of you for contributing your valuable expertise and to my staff for organizing this conference.

Now, it is my great pleasure to introduce our first keynote speaker, Professor Catherine Schenk from the University of Oxford.

Catherine is Professor of Economic and Social History at the University of Oxford and a Fellow of St. Hilda's College Oxford. Her academic career has brought her to a number of renowned academic institutions in Europe, Asia and in New Zealand. She is a Visiting Academic at the Bank of England and currently works on an EU-funded research project that explores the evolution of the global payments system from 1870 to 2000, with a particular emphasis on the changing pattern of cross-border correspondent banking and the governance of global payments architecture.

Catherine, please share with us what you can read for the future of the euro from the history of Economic and Monetary Union.

The floor is yours, Catherine Schenk.