

EURO IS AT THE DOORWAY

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Keywords

- Euro - Legal tender - European Central Bank - European Monetary Union
- Euro zone -

Box 1. Currencies to be withdrawn from circulation:

DM
FRF
ITL
NLG
BEF
LUF
IEP
ESP
PTE
ATS
FIM
GDR

INTRODUCTION

As already known, from January 1, 1999, the European Monetary System entered its final stage: A unique currency (EURO) and a common central bank (The European Central Bank) were established. The transition plan toward this phase envisaged a 3-year transition period in which economic and monetary convergence within the member states will be further extended as

technical preparations for the physical replacement of the member countries' currencies with the new currency will be made.

Not more than half a year is left when the world will see this new currency circulate as the only legal tender in the market. From January 1, 2002, the new currency will physically circulate in all member countries of Economic and Monetary Union. Decision-making authorities decided a six-month transition period for all member states (from January 1 to June 30, 2002) to make the physical replacement.

Later on, this term shortened in two months. This means that from March 2002, the current currency denominations of member countries will stop acting as legal tender. This paper aims to closely analyse some specific and practical concerns related with the physical replacement of these currencies, actually circulating in our country.

1. How and when will the physical replacement of these currencies be made?
2. Where can this replacement be made?
3. Will it be expensive for the customers and who will pay for these costs?
4. What decisions ought to be taken by domestic authorities (the Bank of Albania and the commercial banks)?

1. HOW AND WHEN WILL THE PHYSICAL REPLACEMENT OF THESE CURRENCIES BE MADE?

The physical replacement will not be made on the same calendar for every member state. Every country has adopted a calendar of its own. However, the date when this replacement will initiate is January 1, 2002. The European authorities have decided this operation to complete by February 28 (although their intention is that this changeover be made within two weeks).

Thus, from March 1, 2002, ITL, DEM, GDR, etc., will simply remain historical relics. Since an enormous quantity of currency

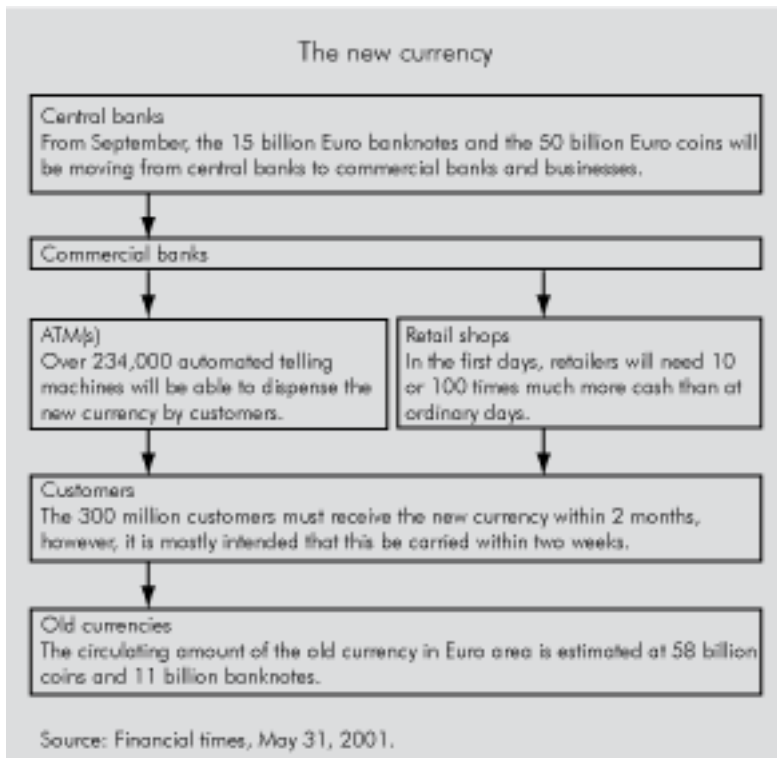
will be transported (also considered one of the biggest logistics challenges), Euro distribution by banks will start in September 2001. During September - December 2001, banks, on their side, will distribute Euro denominations in retail shops. Although the European Central Bank has rejected Euro distribution for customers before January 1, 2002, the very large size of this operation has created a kind of fear as to security and transportation of this extraordinary large amount of money (Euro 660 billion).

As a result, the monetary authorities have requested military intervention (besides the security and police forces). Excluding Germany, in all other countries, the customers may change the old currency with the new one at every bank agency. In Germany, banks will replace the currency only for their customers. Thus, every customer must open an account during this period. This measure has been taken to prevent money laundering that most analysts believe may enter from Eastern European countries.

Albanian customers, business-persons, foreign exchange dealers and other economic agents use and circulate various countries' currencies. Most circulating currencies correspond to member countries of the European Monetary Union, which will be removing them from circulation to replace with the new currency. This means that every bearer of such currency (see box 1 on currencies to be expelled from circulation), may start their physical exchange from January 2002. Is it important that Euro exchange be made according to the fixed terms for member countries? No, it is not because Euro components are not legal tender in our country, (they mainly function as reserve assets - thus as savings). So, although the changeover may start from January 2002 even in our country, their exchange is expected to take up to a 10-year term. (This term is decided as available for member countries of the Euro area). However, the old currencies can be used in no trade transactions, any more.

Anyone travelling in one of these states, from March 1 can not perform any kind of payment in the old currencies, except for Euro.

This period is most important for the Albanian businesspersons, performing trade transactions with one of these states. From January 1 onward, all imported goods payments from these states will be made in Euro, only. As a result, all businesspersons must contact with the banks where they hold accounts to receive necessary information from them.



How will the physical changeover be made? As already known, participating coins in the European Monetary Union have a fixed exchange rate against Euro. Thus, the ITL, the DEM and other circulating coins have got a fixed exchange rate against the Euro.

Table 1 Bilateral exchange rates

Countries	Exchange rate
Germany (DEM)	1.95583
France (FRF)	6.55957
Italy (ITL)	1936.27
Netherlands (NLG)	2.20371
Belgium (BEF)	40.3399
Luxembourg (LUF)	40.3399
Ireland (IEP)	0.787564
Portugal (ESP)	166.386
Spain (PTE)	200.482
Austria (ATS)	13.7603
Finland (FIM)	5.94573
Greece (GRD)	340.75

Reading the above table means that to buy Euro 1 you must hand over DEM 1.95583 or ITL 1936.27. Or if you have DEM 1000, you will receive Euro $511.3 = \text{DEM } 1000 / 1.95583$ when bank exchanged.

This is the fixed exchange rate of the Euro zone. The Bank of Albania must take a decision on enforcing all banks to perform the exchange, observe this level of exchange rate. If someone decides to exchange Euro currency in US dollars, Euro exchange rate (hence, Euro component currencies) will be flexible. Thus, in this case, the customers must follow Euro exchange rate performance in the market.

2. WHERE WILL THE PHYSICAL REPLACEMENT OF CURRENCIES TAKE PLACE?

In member countries of the Euro zone, the physical replacement of currencies will be made at banks, financial institutions, ATMs, post offices or retail shops. Bank accounts will be automatically exchanged in the new currency (this has already been made); equity or debt security entitlements will also be expressed in Euro, as well.

What about the Albanian citizens holding these currencies outside the banking system and/or with banks?

If these countries' currencies are bank held, everyone would be able to attract the new Euro currency, as banks are preparing for their physical changeover.

If someone holds the currencies of these countries as household savings, thus not with the banks, their physical exchange at bank windows is still enabled.

However, the Bank of Albania must officially nominate banks (or foreign exchange bureaus), or make public announcements to this end. This would evade the possibility for speculations to the detriment of unprotected customers.

3. WHO WILL PAY THE COSTS?

Issuing new currencies has a certain cost as to printing paper, etc. According to the European Central Bank guidelines, the physical changeover of the currencies will not be accompanied with costs for customers. This process related the national central banks of member countries, which are concurrently responsible for the issue and distribution of currencies in circulation and would normally afford costs.

The physical exchange, in the case of countries outside the Euro area, must be made in formal agreement between central banks.

This means that the Bank of Albania must enter in negotiations with central banks of the Euro area to contract bilateral agreements on the currency exchange. It must be under the Bank of Albania's responsibility to decide contractual terms as to the hand-over of the existing currencies, reception of new ones, their distribution, etc. The Bank of Albania must take respective decisions to cover the costs from this process. Principally, these costs must be covered either by the Bank of Albania or be shared with the commercial banks. It would be pointless for customers to cover these costs.

4. WHAT DECISIONS MUST THE MONETARY AUTHORITIES OF THE COUNTRIES TAKE?

According to a European Central Bank decision, banks, financial or credit institutions will have the right to furnish bank branches, subsidiaries or their institutions outside the Euro area with the new currency. The Bank of Albania must enter in contacts with these institutions, in order to coordinate this process through formal agreements, ensure a normal transition and close the speculation gaps that may be established.

The Bank of Albania must address the operation of monetary exchange by officially nominating banks as exchange operators. It must ensure adequate supply with the new currency. This requires it subscribes a binding contract with the central banks of the Euro area to specify the details of this process, and with the commercial banks operating in Albania.

The Bank of Albania must also take care, so that this process has a smooth transition. This also requires an intensive campaign of public awareness, information, details related to this process etc.

5. IS THIS PROCESS RISK-EXPOSED?

The European Central Bank and the Euro area authorities have launched detailed instructions on security problems that will accompany this transitory phase. Although the new currency denominations go to Euro 500 denomination, no problems are expected ahead.

There is no reason to believe that this process may bear risks for the saving consumers or other economic agents of our country. The exchange process does not include an expiry date. The central banks of the Euro area will have the right to perform physical changeover on longer than 10-year term, although the current currencies can not be used. This means that the Bank of Albania in subscribing agreements with these countries' central

banks must envisage physical exchange possibilities on a longer term, as well. In essence, this process will be the same with any currency exchange, previously experienced in our country (as withdrawal of old denominations from circulation).

The physical exchange of currencies in circulation may be an occasion for money laundering through banks. Indeed, that is the biggest concern of the European banking system. It may happen that banks perform Euro exchange for counterfeit denominations, actually in circulation. This may be for the long queues that will be created at bank windows and the impossibility of bank officials to control every unit of the currency requested for exchange.

Although such a thing is not so likely to happen in our country, the Bank of Albania must deliver detailed guidelines to be applied by domestic banks and accompany this process with a prudential supervision.

The Euro is a new and non-counterfeit currency. However it may be exchanged for counterfeit denominations of ITL, DEM, etc., that may be either circulating in our country or enter from other countries of the region, where the most circulating currency is mainly in DEM.

Another concern relates to the exchange rate. If customers will not be willing to convert their household savings in ITL, DEM or GDR, etc., into the Euro, and select USD as their most preferred currency in the domestic market, this may set Euro under depreciating, artificial or speculative pressures. The Bank of Albania must play a restraining role in this direction, through prudentially pursuing the foreign exchange market situation and make the necessary interventions to prevent the likely speculations. Possibilities for speculation may be created especially in the informal foreign exchange market.

Concluding:

We believe that there is no reason to be worried about the physical exchange of other than USD household savings and/or

with the banks. This process will have an adequate time spread. The Bank of Albania must undertake the necessary steps to precede this process by a prudential supervision.

The Bank of Albania must make the necessary technical preparations for this process, deliver the necessary guidelines for banks and foreign exchange bureaus, familiarize customers with the new currency, etc. The Bank of Albania departments must highlight the specific matters related to this process and be prepared in due time.

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