A TEORETICAL APPROACH ON ERM II

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Abstract: : This article presents an overview of the European Exchange Rate Mechanism and of the effects of this mechanism on the new Member States from the point of view of the stability of the exchange rate, of the convergence with the macroeconomic policy and of the inflation stabilization. There will be outlined the contradictions which may appear between the preparation of the EU accession conditions and those regarding the accession to EMU, with the intermediate stage ERM II, including the effect Balassa-Samuelson. Another important element is to set the central exchange rate for ERM II because this central exchange rate will be similar or almost similar with the future exchange rate as opposed to Euro.

JEL classification: F36, F 31

Key words: ERM II, exchange rate, exchange rate stability

1. INTRODUCTION

The EU institutions with attributes of including new members, respectively the European Commission, ECOFIN, the Central European Bank have coordinated their requirements and have set an elaborated strategy regarding the exchange regims for the new members along the inclusion stages in EU and Eurozone, as the final stage of the economic and monetary integration process; although this stage is orientatively, it has to be followed and complied by all candidate countries.

After the inclusion in EU, but not at the same time and neither too fast the new member countries will access ERM II (Exchange Rate Mechanism II) for a minimum period of two years before the accession to Eurozone, this being one of the criteria of the Maastricht Treaty.

ERM II established by the European Council in Amsterdam, June 1997, is a bilateral monetary agreement which provides the stability of the exchange rates between Euro and the currencies of the countries which are not in the Eurozone. The functioning mechanism of this regime of monetary exchange rates relies on a variation band determined by a pivotal rate compared to Euro; the rates are stable, but adjustable, with a margin of +/- 15%.

The participation to ERM II is a precondition for the inclusion in Euroland, ERM II being the successor of the first mechanism of currency exchange, which ceased to exist in 1999 when UEM was introduced. ERM II is designed for all countries willing to be included in the Eurozone, so for all Member States of EU which were not included from the beginning in this mechanism, as for example Denmark, Great Britain, Sweden, for which there was no compulsory clause of participation in the mechanism, or for the Euro adoption.

ERM II is not an antechamber for the Euro adoption, but a bilateral currency agreement for the new Member States or for the old Member States which are not members of the Eurozone, but which are willing to become, in which the currencies of the participant countries are related to Euro; ERM II sets a central parity for each national participating currency and which may fluctuate along the central parity up to +/- 15%. The two standard margins where the appreciation or depreciation of a national currency appears are wide enough to take over some imbalances as the ones determined by capital movements.

According to the ERM II protocol and the Resolution of the Council on the establishment of ERM II, in force from 1 January 1999, the essential requirements of the mechanism can be summed up as it follows:

Taking part in ERM II for at least 2 years before the examination is compulsory;

Depreciation of the central rate in the period of 2 years is not allowed being considered as a violation of the criterion of exchange rate stability.

Fulfilling the criterion means maintaining the fluctuation of the exchange rate in the margin of +/- 2,25% around the central rate (parity) "with no severe tensions".

When the fluctuations are going out of the margin, we have to distinguish between the two barriers, the superior and the inferior margin.

The Central and European countries – the 10 members accepted to EU on 1 May 2004 - , EU10, as well as the ones included on 1 January 2007 – Romania and Bulgaria - have participated from the accession to EU as EMU members, as Member States which are derogated from such a clause in the accession treaties, so that Euro would be gradually adopted, and for the adoption of the single community currency as a national currency, the newly included countries or the countries which are going to be included in EU have to go through the ERM II stage.

ERM II is a bilateral agreement for the exchange course which was significantly different from the existing regimes in most of the 12 new Member States, which cover the entire range of exchange regimes: fixed, intermediary and free, in the following way: the anchor of the monetary council is the Euro – Estonia, Bulgaria and Lithuania (initially as in relation to USD and from 02.02.2002, as opposed to Euro), fixed course as opposed to SDR, the case of Latvia and as compared to a currency basket consisting of Euro, USD, and pound for the case of Malta and crawling peg with a fixed Euro rate and fluctuations allowed with a +/- 15 % margin, Euro rate of +/- 2,25% as opposed to the central parity and administrated parity, in the case of the monetary policies but with different goals. Taking into account the different exchange rates, the effort of bringing these regions in line with the Euro in ERM II was and will be different.

The fixed rates as opposed to Euro with a fluctuation margin lower than +/- 15% were compatible with the time mechanism while the monetary councils have to have their compatibility with ERM analysed, the fixed rates as opposed to other Euro currencies, the free rates or the crawling peg rates are not compatible with the ERM II requirements. The farther the exchange rates from the ERM II requirements, the more substantial are their modifications and their transposition in real economies.

2. FASTER OR SLOWER INTEGRATION IN THE EUROZONE?

A country which enters the European Union is not forced to enter immediately the Exchange Rate Mechanism (ERM 2) and may choose between a faster adopting of Euro (at least 2 years) which means the immediate accession after the integration in ERM 2, or it can postpone the moment. The moment of joining ERM2 is the decision of each Member State, this being able to request the accession to ERM 2 anytime without fulfilling any formal precondition. It is very important when joining ERM2 to register an adequate level of nominal and real convergence with the countries which are already in the Economic and Monetary Union in order to be able to avoid a currency crisis.

From the point of view of the economic fundamentals pointed out by the theory of the optimum monetary zones (Mundell, 1961[1]), the interest of all EU acceding countries for the Euro zones is to join this zone as fast as possible. These countries are too small, too open and too vulnerable for the speculations on their national currencies in order for them to be considered optimum monetary zone. The economic studies (Grauwe, 2004 [2], Darvas si Vadas, 2005 [3]) show the fact that in the European Union, 27 states, the Euro adopting will not lead to a monetary zone. The major argument is related to the fact that there is a pretty high correlation between the shocks, but between the countries from Eastern and Central Europe and the Eurozone this correlation is reduced. Moreover, for some countries, as the Czech Republic, Slovenia, Slovakia, Lithuania and Latvia the correlation with the Eurozone is negative, which means that these countries are in different stages of the economic cycles as compared to the member of the Eurozone. In the case of Romania, the correlation is almost zero.

The countries from the Central and Eastern Europe in Eurozone.

On one hand these countries and especially the best prepared ones are in favour of joining the Eurozone as fast as possible. EU considers that the best time for these countries to join the Eurozone is the moment when they are prepared for this, respectively when they meet the convergence criteria agreed in Maastricht, but to these criteria there are some preconditions and administrative barriers which require a long process of adjustment and preparation.

The EU institutions would rather choose a special discretion for this scenario. If there is the case of a premature accession, of some countries to the Eurozone, this could be associated with some risks from both sides.

For EU the risks come from the careful approach related to the joining period in the Eurozone, as for example:

The inclusion of some weak currencies in the Eurzone which could affect the stability and credibility of Euro;

Financial assistance to help the new Member Countries fight against different asymmetrical shocks;

Disturbing the process of taking decision in CEB;

Affecting the single monetary policy in the system of the Eurozone;

For the candidate countries the risks are generally the same as for the new member countries from EU, and some risks are more accentuated, as it follows:

Giving away too soon the sovereignty in the field of monetary and exchange policy of a supranational authority – the Central European Bank, the influence of these countries being small in this court even if the governors of the central bank take part in the decision making process in the CEB structures. When the respective countries suffer from asymmetrical specific shocks and if the alternative adjusting mechanisms, as the flexibility of the salaries, do not give satisfactory results, the respective countries could register a certain decline in the rhythm of growth and in the employed staff. Due

to the fact that such alternative adjusting mechanisms have not been frequently used in the period before entering ERM II, the risk of these countries is still important taking into account the authorities of the respective countries. The best solution to eliminate such risks in the preparation and participation period to the ERM II system could be taking some measures in order to eliminate the causes of the internal asymmetric shocks and to improve the alternative adjusting mechanisms so that these could become more flexible and efficient.

The inobservance of the limit of 3% of the budget deficit under the circumstances where the new Member States have the national control over the major elements of the economic and fiscal policy, disregarding these conditions leads to some sanctions from EU.

Imposing severe economic constraints as subjects of the discipline of the EUM policies in the monetary field, of the exchange and fiscal rate, with the risk of jeopardizing or delaying the economic growth.

At the same time, the advantages of the countries entered in the Eurozone, can be quantified both on a micro and macroeconomic level, as it follows:

The elimination of the fluctuation of exchange rate, the currency risk in the Eurozone trade, the main partner with an average of more than 60%, reducing the costs of transactions, eliminating the costs with the conversion of the currency the transparency of the prices;

Obtaining the quality of legal participant in the internal market, respectively the capital market of the EMU countries, obtaining lower installments for the credits on these markets ;

The reduction of the inflation and interest rates;

Increasing the credibility of the economic and fiscal policies of the countries after the countries have joined the discipline of the monetary union.

Another argument for the sooner inclusion of the Member States in the Eurozone is that in the process of accession to EU, these countries have to liberalize almost completely their capital account. These countries are exposed to the volatility of the speculative capital movement, especially in the period before the accession to EU or EMU, under the circumstances where they do not have the EU tools and support.

After these countries are included in the Eurozone, their exchange rates stop being the object of speculative attacks and they can adjust, if there are serious asymmetric shocks, the balance of payments deficit.

In consequence, the desire of the new Mmeber States to be in the first group of those who will adopt the Euro before time depends on the above mentioned advantages and on some political reasons or some reasons of proud to be the first one in such an adventure.

3. EUROISATION – AN ALTERNATIVE TO ERM II?

In recent years in the debates from the academic and political world, the concept of euroisation has gained an increasing importance, after the lexical model of dollarization. The debates became more and more interesting as the fulfilment of the Maastricht criteria is an extensive and intensive temporal process in requests, which makes the euroisation an option which has to be taken into account. This process consists of abandoning the own currency and adopting Euro before meeting the nominal convergence criteria. It is a process of unilateral adoption of Euro which can be

accomplished after the central bank has purchased enough quantities of Euro and after it has changed a large amount of currency reserves.

Some economists (Bratkowski and Rotskowski [2]) were in favour of this unilateral adoption method and argue in 2001 that the central banks from the candidate countries had enough currency reserves for the unilateral Euro adoption as a national currency.

For example, Romania can decide to adopt the Euro. This means that Romania is giving up its national currency and that the single authority which can issue currency is the Central European Bank. Romania and EU use the same currency, Euro, issued by CEB, and the Romanian citizens have to exchange the Lei in Euro for a certain exchange rate. This is a sudden strategy of accession to the monetary union, as compared to the gradual one (Maastricht) which involves going through some stages.

For Romania, such a sudden strategy could offer an important advantage. First of all the inflation rate could go down on the level registered by EU, without any costs in terms of unemployment. The economic operators from Romania are aware of the fact that the inflation in Romania is on the level of the one from EU and that it confirms the inflationist predictions for Romania. Romania will benefit directly from the CEB reputation and from welfare earnings generated by the monetary union. Therefore, Romania should reduce the inflation rate before joining the monetary union, so it would not need a monetary reform.

Another advantage would be the increased trust in foreign investors, which could lead to higher foreign direct investments flows, to the reduction of the interest for external borrowings on similar levels with the ones from the Eurozone. The reduction of the internal interests on very low levels is very useful especially for the countries which register high budgetary costs with the interests, as a consequence of the high public debt.

It has been noticed that the announcement of accepting the accession candidature made the politicians from the Central European countries to show more freedom in the fiscal, salaries, restructuring and privatization policies. That is why the monetary policy should be taken as soon as possible out of the hands of the national authorities and oriented towards the more peremptory reforms.

Besides these positive effects, there are a series of disadvantages for the fast euroisation. First of all the fact that the accession of poor countries like Romania and Bulgaria need a particular approach in the aligning strategies which are quite different from the stabilization strategies. There are some certain disparities between the economies of these poorer countries and the European one in facing the asymmetric shocks; It is required an independent monetary policy and even the postponement of the euroisation process up to the stage when the degree of convergence between the Romanian economy and the EU economy is high enough.

A unilateral adoption of Euro as a national currency without the consensus or agreement of EU, although technically seems to be possible, is not advisable from a political point of view. Otherwise, if we refer to the EU10 countries, or to the countries accepted in 2007, this thing is not possible due to the explicit clauses regarding the Euro adopting through participation in ERM II. The Euro adopting or euroisation can be an alternative, exciting policy for the candidates but only if this is accomplished in a longer period of time. An immediate adopting of Euro can be a not very prudent measure if there is no fundamental stability and no strengthening of the financial

system. The development of a fiscal discipline is also essential in order to eliminate the disparities from the common monetary system.

4. THE EFFECTS OF PARTICIPATION TO ERM II

The effects of ERM II on the new participating Member States should be analysed from the point of view of the stabilization of the exchange rate, of the convergence with the macroeconomic policies and of the stabilization of inflation.

The exchange rate stabilization after anchoring the expectation is one of the positive effects of participating to ERM II, which contributes to the focus of the convergence towards the level of the EU developed member states. The CEB commitment to assist the new member states in the interventions for the maintenance of the currency fluctuation in the margin will strengthen the stabilizing role of ERM II. If the fluctuations of the currency will be situated at +/- 2,25% as opposed to the central rate, these intra-marginal interventions will not be applied very often, and we have to take into account the fact that the CEB support in such interventions is not automatically, thus reducing the stabilizing role. On the other hand, the standard fluctuation margin of+/- 15% around the central rate is broad enough to allow the normal evolution of the exchange rate, and the central rate can be the subject of the bilateral decision for adjustment in the case of the strong appreciation tendencies from those countries, this situation being able to limit the stabilizing role of ERM II.

Another argument is that the participation to ERM II involves pressures on the responsible for the macroeconomic policies in the sense of consolidation and reform of the public finances. In order for the fixed rate to be efficient, there should be health and consistent macroeconomic policies, knowing the fact that its efficiency is decreasing in the case of some long fiscal deficits or when the salaries increases are higher than the increase of the labour productivity.

Due to the fact that the new member countries of the globalized financial world have registered and will register increases in capital flows under the circumstances when the broadness of the margin of the ERM mechanism allows speculations and attacks on the currencies from the respective countries, the case of Hungary 1993, which has the same fluctuation margin of de +/- 15%,so that such attacks are possible if the speculators consider that the macroeconomic policies are not consistent with the exchange rate regime.

In this situation, the restructuring policies, the sustainable fiscal policies should be applied before the introduction of the fixed rate regime in order to sustain the restrictions regarding the fluctuation of the exchange rate, so that the maintenance of the fixed exchange rate could be a consequence of these policies.

In what inflation is concerned, the participation to ERM II is advisable due to the capacity of the mechanism to encourage its low volatility.

The fixed exchange rate contributes to the anti-inflationist development through the stabilization of the prices of imports and the inflationist expectations; this situation does not pose important problems for the new member states which have lately registered satisfactory results, and even good results in some cases, for this indicator. From this point of view, the problem gets complicated in the case of the countries which set as a monetary policy strategy aiming at inflation, defending two goals in this way – sustaining the central parity and aiming at inflation – of the monetary policy, situation which can affect the credibility of the central bank due to this conflict of goals. The solution for this situation is the participation for a short period of time to ERM II.

A special importance is setting the central exchange rate of that country, the rate of joining ERM II. If a new EU member country wished to be included in ERM II as fast as possible, it has to accept a new central exchange rate which should be under-evaluated than over-evaluated because it is crucial to eliminate the possibility of depreciation of the currency in the period of the two years of participation to the mechanism, so that it would not fulfil the criteria of exchange rate stability. If there will be a depreciation, the risk of inflation growth will appear, situation which will be discussed for the fulfilment of the other convergence criterion, that is the stability of the prices.

Choosing the most correct exchange rate for ERM II can have vital consequences because the central agreed exchange rate will be identical or almost identical with the future exchange rate towards Euro.

The newly accepted countries to EU with floating exchange regimes have to agree with CEB and ECOFIN, in order to enter ERM II, the central exchange rate and the width of the margin which will be different according to each country, but which will be in the broad band. Under this aspect we mention the case of Hungary which after it abandoned the exchange rate regime with crawling band, it has introduced unilaterally in October 2001, a regime of the exchange rate reported to Euro, with a fluctuation band of +/- 15%.

Taking into account these aspects, the new member states are interested to join ERM II with an under-evaluated course, as in the case of Greece, which should allow them to reach an area closer to the margins of the fluctuation band especially when these margins are under depreciation pressure from some external shocks, depreciation which may induce lack of trust and in consequence the possibility for some speculations.

The central exchange rate may be revaluated upon request of the country. If ERM II is maintained for a longer period of time and the real appreciation of the exchange rate is adopted by the appreciation of the nominal exchange rate, the relatively wide fluctuation margins of the band may become ”narrow” according to the intensity of the effect Balassa-Samuelson. The adjustment (re-alignment) or the fluctuating exchange rate from the upper part of the ban may lead to the phenomenon of self-stabilization of the appreciation of the exchange rate with unfavourable consequences on the recovering process of the disparities towards the developed countries. If there are systematic pressures on the exchange rate from the upper part of the band –as in the case of Hungary- after the introduction of the Euro system- or the central exchange rate is constantly appreciated, it means that the stabilizing role of ERM II is deficient, the system being a simple inflation objective.

At the same time an over-evaluated exchange rate is going to affect competitiveness, to reduce the export and growth, the experience of Portugal being an example, because it registered a slowdown of the export, an economic growth and a current account deficit, and in 2001 it registered a budget deficit of 4,1% of GDP, which meant the violation of the requirement of the Stability and growth pact and the application of sanctions from EU.

Taking into account the relatively high width of the fluctuation margin (+/- 15%), when the currency fluctuates towards the margins, the regime is getting close to that of managed flotation with smaller effects on the stability of the respective currency and with a deficient framing in complying with the respective criterion.

The possibility of fluctuation in the ERM II mechanism towards the margins of the band is possible because there are expectations or fears of growth of the volatility of the exchange rate.

An essential element for the food functioning of the ERM II system is the credible fixation of the central rate of a national currency when entering the system and the economic, monetary, and fiscal policies of the respective country in order to provide a stable macroeconomic development.

It has been pointed out the fact that between the preparation of the accession condition to EU and those required for EMU, with the intermediate stage ERM II, there can be major contradictions. On one hand, for the EU accession, the priority is to meet the real and nominal convergence criteria which implies the amplification of the economic rhythm of growth, the development of the restructuring process, drawing foreign capital and others. All these aspects lead to the real appreciation of the exchange rate. The appreciation process of the exchange rate is amplified by the action way of the phenomenon Balasa-Samuelson. On the other hand, the effect Balassa-Samuelson generates a growth of inflation which makes the fulfillment of the accession conditions to EMU difficult. As we know, the annual rate of inflation for the candidate countries to Eurozone should not exceed with more than 1,5 percentage points the average of inflation of the other three countries with the lowest inflation in Eurozone.

From the moment of introduction, the convenrgence criteria have generated debates in the academic world, starting wtith the need for such conditions but especially related to the connection between such macroeconomic convergence criteria and the properties of the *optimum monetary areas* (economic zones where the production factors are mobile in order to accomplish an adjustment if there is an asymmentrical shock).

The analysis of the Maastricht criteria, have demonstrated that two of the criteria: *the criteria of inflation* and the *criteria of the exchange rate* are contradictory, under the circumstances when the countries have to face the catch-up process. At the same time, it has been notices the contradiction between *the real and nominal convergence criteria* for the countries that want to join as soon as possible the Economic and Monetary Union.

The accession to EMU of the new member states involves *finding the most favourable compromise* between the *real and the nominal convergence*, under the circumstances when after two years of ERM II a country has to fulfil the Maastricht criteria. When the inflation which is going to be measured with a single figure, we will be able to take into account a stability of the exchange rate which should be included in the requirements of the Maastricht Treaty.

The most difficult problem in this case is the participation in ERM II and the exposure to the risks involved in this mechanism. The participation to ERM II involves setting the conversion exchange rate on the future evolution of economy.

Therefore, *the accession to the Eurozone at pretty high exchange rate would determine a lower competitiveness of the exports, which could affect negatively the process of economic growth; in exchange, an exchange rate where the currency is depreciated in relation to Euro will generate the growth of inflation.*

In this context, ERM II represents a testing stage of the central rate and of the sustainability of the convergence in general; the exchange rate should reflect the relative economic performances in the Eurozone; this rate will be the consequence of the expectations of the financial markets.

For the new member countries which register higher productivity incomes and a nominal appreciation of the currency, the revaluation of the national currencies is more probable (the case of Ireland) than the devaluation (the case of Greece).

The ECE have registered a significant appreciation of the exchange rate, explained both by the productivity incomes, as well as by the foreign direct investments flows and the speculative capitals. The appreciation in real terms was carried out either through an appreciation in nominal terms of the national currency as opposed to Euro, or through a depreciation of the currency which is inferior as opposed to the inflation differences in the Eurozone.

The percentage modification of the nominal exchange rate suggests that the fluctuation margins of ERM I are wide enough to avoid a variation of(+/- 15 %) as opposed to Euro for two years; *Buiter and Grafe*(2002 [5]) estimate that the Balassa-Samuelson effect (B-S) determines an annual average appreciation of the currency between 1,5 % and 2,5 % for the countries from the centre of Euro; taking into account the impact of reducing the capital costs on productivity and the salaries from the sectors which produce tradable goods, the impact of the B-S effect would be of almost 3,5% per year. In consequence, ERM II offers a high flexibility in order to alleviate this effect. If the effect B-S is significant, the authorities from the countries with a fixed exchange rate can be constrained to maintain very restrictive fiscal and monetary policies in order to reach the inflation imposed by the Maastricht Treaty, reducing in this way the rate of economic growth. On the other hand, the authorities from the countries with a flexible exchange rate can be constrained to allow a fast appreciation of the exchange rate, this leading to drawing speculative capital and to worsening the competitiveness.

In order to solve this dilemma, two solutions have been identified:

- Imposing a restrictive fiscal policy ;
- Nominal appreciation of the exchange rate in ERM II .

Imposing a restrictive fiscal policy. The monetary policy cannot act on its own only for the accomplishment of the nominal and real convergence with EU; the monetary and fiscal policies should be coordinated in order to meet this objective. (Mishkin, 2000, [6]). Halpern and Wyplosz [7] They argue that in a developing economy, a growth of incomes would lead to a higher growth of the demand for services, and from here on, we will see an accentuation of the Balassa-Samuelson effect. *Stopping the growth of the demand for services could be accomplished through a higher taxation of the incomes* which will contribute to the reduction of the inflationist pressures. An alternative measure *would be the reduction of the governmental request for the "non-tradable" goods.* These measures for the restrictive fiscal policy will lead to the reduction of the impact of inflation without affecting the exchange rate.

The nominal appreciation of the exchange rate in ERM II

Applying an appreciation policy for the nominal exchange rate in ERM II could deliver a natural adjustment mechanism. *This policy of appreciating the exchange rate in nominal terms practically corresponds to a reinterpretation of the criteria exchange rate from the Maastricht Treaty without a renegotiation.* The replacement of the restrictive fiscal policy in the Central and Eastern European Countries will lead to a real appreciation of the national currency in the ERM II period, under the circumstances of maintaining the inflation under control.

Even the European Commission has signalled that the fluctuation band of +15% presupposed by ERM II is wide enough to allow the Member States the

application of some macroeconomic policies which should correspond to their structural evolution and the needs specific for each state, so that they could face the requirements of the Maastricht Treaty.

Putting into practice such a solution: the nominal appreciation of the exchange rate ERM II has as starting points: "the Irish model" and "the Greek model" put into practice by the two states in the period before the accession to the Economic and Monetary union.

In what the stage of the countries from May 2004 is concerned, it is presented in the following way: Estonia, Lithuania and Slovenia have joined ERM II in 28 June 2004. In this moment they adopted a central rate for their national currencies, as it follows: 1 Euro = 15,6466 Estonian kroon, 1 Euro = 3,45280 Lithuanian litas and 1 Euro = 239,640 Slovenian tolar. Latvia and Slovakia have also become members of ERM II, starting with May 2005 and respectively 25 November 2005. The central exchange rate of their national currencies was of 1 Euro = 0,702804 LVL and 1 Euro = 38,4550 SKK The Czech Republic, Poland and Hungary have not joined ERM II and Poland does not have a date for the Euro adopting.

On the level of Central and Eastern Europe, Bulgaria is the singla state maintains its positions regarding the Euro adopting. The other states as Poland, the Czech Republik or Hungary have posponed the moment of accesion for an unlimited period of time dueto the financial crisis which affected the economies.

Poland which initially wanted to join ERM II in the first half of 2009, recognized that the goal was too optimistic and decided to postpone the moment until the state will be prepared to make this step. The Czech Republic and Hungary, although did not regard this step as belonging to the near future,have announced that they will postpone their decison untiș the world economic recession will decrease.

In April 2009, the International Monetary Fund has made a report according to which the fast Euro adoption by the Eastern counteis should be the most efficient eay of stopping the crisis which made a lot of countries to asl for financial help from this institution. According to IMF, the Central and Eastern European countries facing the global financial crisis should have given up their currencies and adopt the single European currency even if they did not formally enter the Eurozone.

The Eurozone should have made its rules not so rigid so that the members of the European Union from the former communist space could join the 16 member states of the Eurozone as quasimember, without holding positions in the management board of the Central European Bank (CEB), say the officials of the fund. The Central European Bank rejected the IMF idea. The idea was considered by the CEB strategic members, and the president Jean-Claude Trichet, not viable and dangerous for the Euro currency, which could loose its credibility. In the European Union the opinions of the officials and of the comentators were split. Some of them said that this idea may not be sustainable for some states with floating exchange rates, as in the case of Poland and the Czech Republic, but it could represent a viable solution for the smaller states with fixed exchange rates as in the case of Bulgaria and the Baltic states.

5. CONCLUSIONS

The participation to ERM II of the new EU member states is compulsory, for at least two years, in order to obtain the "good practice" certificate; it is a compulsory condition for the accession in the Euro-system and of the finalization process of definite

integration in the EU structure in order to take advantage of all the advantages coming from the membership to the most developed regional integrationist structure.

Although ERM has a stabilizing potential which should provide a calm inclusion in the Eurozone field, we showed that we also have to look at the opposite way, the dangerous potential of destabilizing ERM II.

Phenomena as the possibility of financial and currency crisis, the conflict between the objectives of the monetary policy, the difficulties encountered in fulfilling the convergence criteria, the postponement of the Euro adopting because of ERM ii, are possible especially in the countries which are confronted with massive direct investments inflows which can create pressure, because of the appreciation of the currencies which joined the mechanism; all these phenomena have unconsolidated financial policies and high budget deficits to which we can add problems coming from the pension, social insurances and health system reform.

Taking into account the possible adverse effects, I think a realist approach is necessary, an approach based on serious analysis of the decisions regarding the moment of joining ERM II; the new EU member states should have a longer period of pause from the moment of acceding the EU and before joining ERM II, period when these countries should take some measure in order to continue the reforms.

A feasible approach of joining ERM II, would be the participation for the shortest compulsory period, of almost 2 years, and when there is the certitude that the other Maastricht criteria can be complied with.

The recommendation of scheduling the accession to ERM II has not been put into practice by 6 of the 10 countries which have already become members, but we are talking about the smallest countries in this group, some of them being Cyprus or Malta which do not belong to the transition countries and which have already proved that they have stable exchange rates which comply with the European requirements for the entire reference period, and Estonia, has practiced the fixed rate in its toughest form – the monetary council- from the beginning of the transition period, with no change, so that it could not create any instability for its economy.

At the same time, adopting the Euro – the euroisation- by introducing directly the Euro as an official currency in order to avoid the destabilizing potential of the mechanism is a technical possibility, which is not forbidden by the EU legislation, but the relevant EU authorities are sceptical towards this possibility, the ECOFIN representatives and the CEB president have announced publicly that the adoption of Euro in conflict with the principles of the Maastricht Treaty would not be welcomed by EU.

The fact that the other countries, after the moment of their first enthusiasm, have become more prudent regarding the deadline of joining EMU, deadlines which have been revaluated by many of these countries in the sense of setting further targets of adopting the Euro, lead to the fact that the most reasonable attitude recommended in these conclusions, is to schedule the moment of joining ERMI I. The compulsory participation of the new EU member states to ERM II is an exercise through which they have to gain the trust of the markets but they also have to prove that they can manage under the circumstances of some more or less fixed exchange rates of their national currencies.

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This work was supported by the strategic grant POSDRU/89/1.5/S/61968, Project ID61968 (2009), co- financed by the European Social Fund within the Sectorial Operational Program Human Resources Development 2007 – 2013