Jean-Claude Trichet: The European Monetary Union and the euro

Speech by Mr Jean-Claude Trichet, Governor of the Bank of France, at the Financial Forum 2003, organised by The Wall Street Journal Europe and The New Economy Forum, Madrid, 25 February 2003.

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Ladies and gentlemen, it is a great pleasure and an honour to be with you today, on the occasion of the "Financial Forum 2003", organised by the New Economy Forum and the Wall Street Journal Europe.

I would like to present my views on the successful set-up of the euro, on the economic and financial integration of Europe and on the challenges that the euro-zone will confront going forward.

The Euro: built on a successful set up

Set-up of the Eurosystem

The single monetary policy is formulated and implemented within a sound institutional framework, the Eurosystem, comprising the European Central Bank and the twelve national central banks of the euro area. Three principles underpin the Eurosystem: independence, transparency and decentralisation.

The ***independence*** of both the European Central Bank and national central banks is enshrined in the Treaty. When exercising their powers and carrying out their tasks and duties, neither the central banks of the Eurosystem nor any member of its decision making bodies shall seek or take instructions from Community institutions, from any government of a Member State or from any other body. Independence refers to institutional, operational and financial independence. We consider that independance as defined above contributes to the clarity and the credibility of the single monetary policy.

Transparency and accountability: elected authorities, key economic players, as well as all European citizens must be fully informed on the conduct of the single monetary policy. At the European level, the ECB maintains a permanent dialogue with the European Council and the European Parliament, as do national central banks with national institutions. The ECB is the only central bank in the world to enforce the concept of regular, frequent, real-time communication in the domain of monetary policy. Indeed, once a month, immediately after the meeting of the Governing Council, the President of the ECB holds a press conference.

The independence of a central bank and its democratic accountability are two sides of the same coin. In this respect, both public speeches and testimonies by the President of the European Central Bank and by the Governors of national central banks, to the attention of institutions as well as public opinion, are crucial. An important part of our collective duty consists of tirelessly explaining the rationale that underpins the Governing Council's decisions.

Lastly, ***decentralisation***: as the subsidiarity principle underlies the whole European construction, decentralisation is a major principle of the architecture of the Eurosystem. The Eurosystem is a team whose members work in close co-operation, and the team spirit is really strong and fruitful. Monetary policy decisions are taken, at the centre, by the Governing Council, and are implemented by the national central banks in a closely co-ordinated way.

ECB governance

On 3 February 2003, the Governing Council of the ECB unanimously approved a Recommendation for a European Council decision, which is aimed at adjusting the voting modalities in the Governing Council in an enlarged euro area, in accordance with article 10.6 of the Statutes introduced by the Treaty of Nice. This adjustment became necessary so as to maintain the efficiency and timeliness of the Governing Council's decision-making process. The Recommendation has been submitted to the EU Council. We hope that it will eventually be endorsed by the Heads of State and Government after both the European Parliament and the European Commission, which has already delivered its opinion, have been consulted.

As soon as the number of members of the Governing Council will reach 22, the total number of voting rights will be limited to 21. The six executive board members will have a permanent voting right and the NCB Governors will share the remaining 15 voting rights which will rotate among them according to pre-established rules. To ensure that all decisions taken by the Governing Council are representative of the euro area economy as a whole, Governors will be allocated to groups which differ with respect to the frequency with which their members will have voting rights. The allocation of Governors to groups will therefore be done in accordance with a ranking of their respective NCB's, reflecting mainly the size of economies and of financial sectors. All in all, this recent recommandation from the Governing Council is testimony to its ability to smoothly adapt its internal governance to the challenges posed by enlargement.

Strategy of the single monetary policy

The Maastricht Treaty clearly defines the ultimate objective of the single monetary policy, that is to say maintaining price stability. However, for attaining this goal, it is essential to clearly define price stability: we define it as a year-on-year increase in the overall Harmonised Index of Consumer Prices (HICP) of *below 2%* in the whole euro area.

Bearing in mind this objective, our monetary policy strategy is based on two "pillars".

We have first assigned a key role to the monetary aggregate M3. This "pillar" is based on a *reference value* which is set at 4.5% for the annual growth rate of the broad monetary aggregate M3. The concept of a *reference value* does not mean that the Eurosystem is committed to automatically correcting deviations in monetary growth in the short term. Naturally, we also follow the components and counterparts of M3 closely. In this regard, the development of loans to the private sector, as well as the evolution of government finance and capital flows with the rest of the world, deserve a particular attention.

However, it is common sense to say that monetary developments do not account for all the risks to price stability. This is why we have defined a second "pillar" for our monetary policy strategy, consisting of a broad range of variables that are referred to as indicators for the euro area price outlook.

The relatively low yields on long-term euro-denominated bonds confirm investors' confidence in the new currency. This was not the case four or five years ago. At that time, financial markets were convinced that the euro would be the weighted arithmetic mean of its legacy currencies and would not inherit the level of confidence and credibility of the strongest of these. The euro has actually been founded on a benchmarking principle, not on a convergence towards an average. This may explain why the interest rates of the euro were the lowest in Europe from the outset.

To sum up, we consider the maintenance of price stability over the medium term to be the Eurosystem's greatest contribution to fostering an environment which is conducive to sustainable growth and employment. And, it is also its greatest contribution to limiting unnecessary volatility of output and employment in the short run.

The success, thus far, of our strategy does not mean that our current monetary policy strategy is engraved in the marble. With the benefit of hindsight, 2003 seems the appropriate point in time to take stock of our experience thus far and to reflect on the various elements of the strategy. This issue is actively dealt with our Eurosystem's staff and we plan to complete this evaluation in the course of the spring and to publish it. Needless to say that the decision to undertake an in-depth assessment of our experience does not necessarily imply that substantial changes are contemplated.

Successful technical framework

The launch of the euro on the financial markets, on 1 January 1999, has been an indisputable success from a technical point of view. This is a great achievement since many observers doubted of the immediate success of a technical challenge of such a magnitude. Three orientations still shape this success:

- the **monetary policy framework** includes a set of instruments chosen with a view to observing the principles of market orientation, equal treatment, simplicity, and transparency. The decentralisation of operations has undoubtedly contributed to the smooth functioning of the framework. Maintaining a close contact between commercial banks and their national central banks has helped financial markets to quickly adopt the harmonised practices relating to open market operations, eligible collateral for credit operations and minimum reserve systems.

- **operational efficiency** is highlighted by the precise adjustment of banking liquidity and effective steering of short-term interest rates; the Eurosystem has demonstrated this efficiency, in the days after the tragic events of 11th September 2001, by acting quickly and by ensuring a smooth and orderly functioning of the European financial markets. Here again, doubts had been previously raised on the ability of the Governing Council to make decisions swiftly.
- **security** is provided by the procedures and systems implemented, both for the execution of inter-bank transactions, and vis-à-vis large-value payments. The inter-bank market has become highly integrated thanks to the setting up of the Target system for the real-time transfer of large-value payments throughout the euro area and in other EU countries.

Let me turn now to the introduction of euro banknotes and coins, which has been the last step of a now more-than-twenty-year process of monetary integration.

Euro changeover

On 1 January 2002, the euro banknotes and coins were issued and became legal tender in the countries of the euro area. This was a unique and highly symbolic milestone for Europe.

Let me first stress that, thanks to national efforts and the co-ordination by the European Commission and the Eurosystem, almost 100 % of **cash transactions** in the euro area were being carried out in euro only two months after the changeover.

Although the practical changeover to the euro might be considered as an outstanding achievement, we should remain vigilant on the following issues:

- First, **price stability**. Although some increases in prices of a certain number of consumer goods and services have been reported, the first evidence shows that, overall, the effect of the changeover on price stability has been marginal. But consumers must keep alert, while companies and retailers remain responsible as regards price setting. In the end, competition should also contribute to lowering the prices in the short-to-medium term.
- Second, we must closely monitor the risks of **counterfeiting of notes and coins**: the information **campaign of the Eurosystem** "The Euro. Our money" was aimed at familiarising all the European citizens with their new banknotes and coins (and their security features) and, by doing so, it helped them identify the obviously fake banknotes. All institutions concerned, both national and European, are co-operating closely to prevent and fight counterfeiting. Right now, counterfeit banknotes are scarce and conspicuous.

The credibility of the Eurosystem and of the single monetary policy, and the successful changeover to the euro represent major achievements. They certainly contribute to the efficient functioning of EMU and to European economic and financial integration, as I will explain it right now.

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EMU: a balanced concept fostering economic and financial integration

EMU is an economically sound and well-grounded concept.

A few years ago, it was necessary to convince a great number of sceptics that the euro would really be launched. The opinion that the single currency would never exist has of course been disproved by the facts. Nevertheless, objections are still being raised from time to time, on the alleged grounds that the euro area economy comprehends inconsistencies that could endanger and challenge the viability of EMU, all the more so since the European Union is about to welcome new members.

Some observers thus claim that the lack of co-ordination between European economic policies, in the absence of a political federation, is likely to deprive the area of an appropriate policy-mix. Others blame the lack of instruments allowing us to tackle asymmetric shocks that may arise, and underline the lack of flexibility or the absence of mobility of the European labour force. Others claim that the presumed economic divergences and structural gaps among euro area countries are too large to ensure a viable monetary union.

How do we respond to these important objections?

(1) It is not disputable that for EMU to function well, Member States, especially the major ones in terms of GDP, must be aware of the spill-over effects that national economic policies may trigger. The existence of spill-over justifies the implementation of a close co-ordination between national economic policies. This is embodied in the Treaty itself, which obliges Member States to consider national economic policies “as a matter of common concern” and subject them to a multilateral procedure.

Practically, member States have designed institutions and mechanisms to promote appropriate co-ordination. We can now say that EMU has in turn been beneficial to the European economic and financial integration as a whole. Indeed, a coherent operational framework has been provided for the co-ordination of economic policies through close mutual surveillance (under the responsibility of the **“Euro Group”** and the **Ecofin Council**) and through the implementation of the **Stability and Growth Pact**. Moreover, the **Broad Economic Policy Guidelines**, discussed each year by the Heads of States and Governments, help monitor macroeconomic and structural developments in the Member States.

I would like to briefly recall why the Stability and Growth Pact plays such an important role:

- By supervising the fiscal policies of the euro area Member States, the Pact together with the Broad Economic Policy Guidelines contributes to ensuring an appropriate policy mix within the euro area. It is essential for conducting a meaningful monetary policy, to counterbalance the fact that Europe does not have a significant federal budget.
- By setting up a penalty system for excessive deficits, the Pact also helps prevent well-managed economies from having to bear an unjustified risk premium which would be transferred from poorly managed economies to them through the channel of the single currency.

As regards the second common criticism against EMU, that is to say the lack of instruments to respond to asymmetric shocks, I would like to stress that the Stability and Growth Pact helps countering this argument. Indeed, by urging countries to aim at a fiscal position “close to balance or in surplus” in the medium term, the Pact enables them to let fiscal deficits increase, if need be, providing that they do not exceed the 3% reference value. In short, it allows them to create a fiscal buffer during normal economic periods, that can be drawn on to counter economic divergences or asymmetric shocks.

The last set of criticisms focuses on presumed economic divergences between economies within the euro area. To answer this last objection, I would like to put forward a few ideas:

- Firstly, monetary union does not necessarily imply that, at any given point in time, all participating countries will have the same rate of inflation or growth, even though the creation of the euro was based on the successful completion of a convergence process. For example, inflation divergences across countries or regions may be accommodated in a monetary union as part of the process of convergence of productivity and living standards.
- Secondly, I would like to quote Professor Robert Mundell, who made, at the beginning of 1998, an interesting clarification of the Optimal Currency Area theory, and argued that in the event of a shift in demand from one member country to another, creating unemployment in the first and inflationary pressure in the second, flexible exchange rates would not necessarily be able to solve the problem. I quote: “If the argument for devaluation were valid, it could be applied to every state, province or sub-region in any country, with a proliferation of new currencies, so they could be devalued!”.

Even though the EMU relates to a single monetary policy, it also relates to the harmonisation of other markets, i.e. goods and services, as well as financial markets. In these areas, the integration process is well on track.

EMU fosters economic and financial integration

Financial Europe under construction: the reorganisation of capital markets

In 1999, as soon as the euro was launched, one of the expected advantages was the prospect of deeper, larger and more integrated capital markets contributing to reducing the cost of capital for businesses and giving Europeans a greater range of saving options. These expectations have become reality in both the money market and longer-term capital markets.

On the ***euro money market***, the unsecured deposit inter-bank market is highly integrated. EONIA and EURIBOR have provided the market with uniform benchmarks that are fully accepted by all market participants. This is reflected, for instance, in the huge development of the euro interest-rate swap market.

On the ***euro bond market***, the integration process has registered three main developments:

- *a rapid internationalisation*: The introduction of the single currency has fostered the euro-denominated private bond market, by enlarging the potential pool of investors, notably international investors.
- *increased competition between issuers*, which has encouraged the standardisation of sovereign bonds, the gradual convergence towards “best practices”, the development of a range of attractive and actively traded benchmark issues (especially for sovereign bonds). Besides, competition has also enhanced liquidity as issuers have increased the average size of outstanding bonds.
- the *modernisation of market structures*: besides the rapid development of electronic trading, the consolidation of Central Securities Depositories is also paving the way for a more efficient functioning of Delivery-versus-Payment procedures, and easier and safer channels of settlement of cross-border securities transactions. This last point is of particular relevance for the Eurosystem, as the smooth functioning of European securities settlement infrastructure is key for the practical implementation of monetary policy.

On the ***equity market***, the elimination of the currency risk within the euro area has led investors to shift from a domestic orientation to a more international, sectoral one. The creation of a wide range of pan-European sectoral indices was, thus, a direct consequence of these changes in investor strategies.

Additionally, the introduction of euro has been a strong catalyst for mergers and acquisitions in the financial sector. For instance, in this respect, we can stress current trends in mergers or close co-operation between banks, stock exchanges, securities settlement systems, clearing houses. Had the euro not been created, would it have been thinkable for the Amsterdam, Brussels, Lisbon and Paris security exchanges to jointly create EURONEXT?

The large European goods and services market.

Such changes in the European financial landscape have significantly improved the efficiency of capital allocation. The euro contributes to enabling European savers to easily select the most efficient investments. It also helps the productive sector and companies to achieve significant economies of scale, enhances the transparency of the market and boosts competition and innovation to the benefit of consumers.

Moreover, the pace of internationalisation of the euro area economy has been further spurred by the euro. Allow me to give just one example: the level of accumulated foreign direct investment abroad by French residents since 1999 amounted to EUR 380 billion (i.e. four times its pre-1999 level). Indeed, capital flows between the Euro area and the rest of the world mirror a high degree of attractiveness: over the years 1999-2001, the Euro area has registered total inward direct investments worth 719.8 billion Euros.

At this point, one may wonder which conditions are required to ensure the success of the euro and EMU in the medium term. I believe that we have to tackle three main challenges: structural reforms, financial stability and the accession to the EU of new Member States.

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Challenges ahead

Structural reforms

The first challenge is, beyond dispute, to implement structural reforms in the euro area's economies. Structural reforms were crystallised at the European level in what is called the Lisbon strategy. The first objective of this strategy is to substantially raise our potential output growth. The second is to make our economies more competitive.

Implementing the reforms: the Lisbon strategy

The European Council meeting held in Luxembourg in December 1997 explicitly mentioned structural policies among the items selected to achieve enhanced co-ordination. The Lisbon European Council, held in March 2000, further enhanced the medium-term strategy to introduce structural reforms in the Union. This strategy aims to make the European Union the world's most dynamic knowledge economy by 2010. It has since been amended so as to include social issues (at the Council of Nice in late 2000) and environmental issues (at the Council of Gothenburg in mid 2001).

What has been achieved to date in the field of structural reforms is quite encouraging. Noticeable successes have already been registered with regard to policies, such as new rules in telecommunications, electricity and gas markets. The current 2002 Broad Economic Policy Guidelines evaluation exercise is an opportunity to check on the progress accomplished in reforms that were agreed in Lisbon and recently reasserted in Barcelona. Before reviewing the priority areas where fresh impetus is required, I wish to briefly make two remarks:

First, the responsibility for structural reforms in the European Union rests with the individual Member States. Consequently, there is a wide variety of institutional solutions and regulatory arrangements across countries and sectors. I nevertheless consider that such a decentralised approach should be considered as an opportunity, rather than a disadvantage. It encourages "cross fertilisation" of best practices through increased co-ordination of Member States' structural policies.

My second remark relates to the changeover to the euro. This event has been a major structural reform in itself, i.e. a powerful drive towards restructuring the European economy.

An important objective consists in raising the potential output growth of the European economy

If France and Europe seek to secure sustainable growth at levels that are as high as possible, the key variable is potential output growth. There are three ways of raising the level of potential output growth:

First, to boost investment: the more we invest and the lower inflationary pressures, the stronger potential output growth. For example, a two-point increase in the productive investment ratio (productive investment / GDP, 11,4 % during the last five years in France) over the next decade would bring about an average acceleration of more than 0,5 point in potential output growth over the same period.

The second way of raising potential output growth is *to increase the quantity of actual labour*: The European Council of Lisbon set as a central objective the rise of the employment rate of our populations from 60 to 70 % in 10 years. The Council also fixed two sub objectives: to raise the employment rate of women to 60 % and employment rate of older workers (from 55 to 64 years old) to 50 %. As a comparison, the same overall employment rate stands at 75 % in the USA. Although some progress has been achieved in this area, the lack of substantive change and the tendency in some member states to continue to use early retirement schemes remain causes for concern.

The third way of raising potential output growth is to promote ways to boost gains in labour productivity: This can be achieved by increasing competition, encouraging enterprise and innovation, and improving the workforce's skills. Indeed, on the basis of hours worked, productivity in the EU reached in 2001 83% of the level of that in the US, which points some room for improvement.

That strategy should be pursued whilst increasing the overall competitiveness of our economies

The Euro area displays sound macroeconomic fundamentals and satisfying price competitiveness. Sound macroeconomic fundamentals make the Euro area an attractive place to invest in : no major imbalances may be observed contrary to other major areas. Indeed, the Euro area provides for a low and stable inflation environment, roughly balanced external accounts, abundant private savings, and sound financial systems.

Then, in terms of real effective exchange rate, the Euro area has constantly gained in competitiveness over the past few years. In the 3rd quarter of 2002, even though the Euro real exchange rate deflated by unit labour costs in total economy versus the rest of industrialised countries appreciated by 5.4% year-on-year, it is still below its long term average (1987-2001) by 12.3%, according to the European Commission calculations.

If I refer more specifically to what has been observed in the past in France, an economic strategy, based on a moderate increase in unit costs of production, gave us an important edge: the considerable improvement in the cost competitiveness of the French industrial sector from the mid-1980s has contributed extensively to boosting growth. The French economy grew faster than major euro area economies from 1997 to 2001 (+ 15,4 % in France compared to + 13,4 % in the euro area), while repeatedly recording a large current account surplus. This improvement in our overall cost-competitive situation has progressively materialised into growth, job creations and solid external accounts.

Competitiveness is also linked to European harmonisation in other fields, for example in the service industries. Most of the barriers to trade in services appear to be due to national regulations and should be abolished or alleviated.

While the Eurosystem acts mainly as a stimulus in the process of structural reforms, it also plays a leading role in ensuring financial stability. This brings me to the second challenge that EMU will have to take up.

Financial stability

Like any independent central bank, **the Eurosystem has to fulfil two main functions: firstly, ensuring price stability**, which is a key condition for sustained growth, **and secondly, preserving financial stability**, which has become a critical challenge in a globalized world economy. I insist on the highly complementary nature of these two objectives, as price stability is the foundation on which financial stability is built.

The adequacy of European institutional arrangements for financial stability

The adequacy of European institutional arrangements for financial stability has been reviewed in depth at the EU level. In two reports, in April 2000 and April 2001, the Economic and Financial Committee (EFC) took stock of the supervisory and regulatory mechanisms in the EU and examined the issue of financial crisis management. It concluded that the current arrangements provided a coherent and flexible basis for safeguarding financial stability and recommended a further strengthening of cross-border and cross-sector co-operation.

I fully share the assessment put forward in these reports and I would like to stress here the special responsibilities of central banks, due to: their position at the heart of financial systems, their role as liquidity supplier to the economy, their close and constant contact with credit institutions, their contribution to banking supervision and to the safe and efficient functioning of payment systems, and at least for some of them, their contribution to the safe and efficient functioning of securities clearing and settlement systems. To sum up, an institutional framework in which the Eurosystem's responsibilities for monetary policy in the euro area are coupled with extensive supervisory responsibilities of NCBs in domestic markets, and with reinforced co-operation at an area-wide level, seems appropriate to tackle the changes triggered by the current financial trends and the introduction of the euro.

Two points of particular relevance for the financial regulatory framework

Let me conclude on this important topic by stressing two points of particular relevance for the European financial regulatory framework:

- There are still some barriers to further integration of EU capital markets. In this regard, the Eurosystem welcomed the objective of the European Council meeting in Lisbon in March 2000, to accelerate completion of the internal market for financial services, and to set a tight timetable so that the Financial Services Action Plan can be implemented by 2005. This Plan is regularly reviewed by European authorities, and progress is being made.
- The Eurosystem also supports the strategic conclusions of the Committee chaired by A. Lamfalussy on the integration of the European securities markets, ratified by the European Council meeting in Stockholm in 2001 and approved by the European Parliament in early 2002. We are convinced that the implementation of these broad guidelines and the new cooperation structures at the European level will help make it possible to take full advantage of the introduction of the euro.
- In the field of financial regulation and supervision, ECOFIN Council (December the 3rd 2002) approved a report by the Economic and Financial Committee which made proposals concerning the cooperation structures at the European level for financial regulation and supervision. These new arrangements are now being implemented. In this regard, one of the statutory tasks of the Eurosystem is, according to the Treaty, to contribute to the smooth conduct of prudential supervision policies and the stability of the financial system. I am therefore convinced that the involvement of central banks in this issue will remain absolutely crucial.
- Finally, since the tragic events of 11 September and their impact on financial stability, concerns over the potential abuse of the financial system for the financing of terrorism have received top priority in international and European regulatory discussions. The international community and, within it, the financial community, should step up its efforts to hunt down money used by organised crime and terrorism. We shall not be successful overnight, but, today, there is a strong political determination on the part of the international community to co-operate on this issue. As far as the fight against organised crime and terrorism is concerned, we can no longer accept that certain players are not prepared to observe the rules of international legal co-operation.

Beyond structural reforms and financial stability, the accession of new Member States to the European Union and to EMU is the third challenge that I have identified. The last challenge but not the least.

Accession of new Member States to the EU and EMU

Twelve countries from central, eastern and southern Europe are currently negotiating accession to the EU, of which ten, according to the calendar endorsed by the European Council, will join the E.U. as early as the 1st of January 2004. This provides further evidence of the attractiveness of the European framework, which has provided us with both political stability and economic progress for half a century.

The accession countries have accomplished significant progress in stabilising and strengthening their economies and institutions. Observing the accession countries since the beginning of the nineties, we see the major improvements that these countries have made on the road towards convergence with the EU.

Nevertheless, there is also general agreement on the fact that the gap in terms of average GDP per capita between the accession countries and the euro area, although diminishing, still remains quite significant. On average, GDP per capita in terms of purchasing power parity is around 44% of that of the euro area, while in terms of current exchange rates it is only around 22%. The size of the gap, combined with the limited growth differentials between the two groups of countries, suggests that the process of real convergence will be very gradual. Indeed, real convergence is essential to create economic cohesion within EMU and promote integration between Members States, thereby helping to minimise the risk and the effects of asymetric shocks.

The Eurosystem, and notably the Banque de France, is following the enlargement process with a great deal of attention. Let me stress a few points of particular relevance for the Eurosystem and for accession countries themselves, on the road towards catching up with the EU and achieving convergence.

- **Firstly**, nominal convergence, which is requested in order to adopt the euro, must be sustainable and therefore constitutes a medium-term objective, rather than a short-term priority. Indeed, the EU Treaty calls, as a prerequisite for adopting the euro, for a high degree of sustainable convergence in the fields of price stability, government fiscal position, stability of the exchange rate, and long-term interest-rate levels. Therefore, nominal and real convergence should be pursued in parallel, and are not antagonistic, in the interest of both accessing countries and the euro area.
- **Secondly**, I note that many accession countries have already expressed their intention to join ERM II as soon as possible after EU entry. This intention is to be welcomed. However, it should be clear that the ERM II is not expected to be adopted by new members immediately after EU accession, nor is intended to be limited to only two years, which is the minimum period of time prior to adopting the euro. It would be misleading to consider ERM II as a mere "waiting room" before euro. On the very contrary, ERM II is to be considered as a "training room". This mechanism will allow countries to retain some limited exchange rate flexibility during the catching-up process. ERM II membership also offers a meaningful, flexible but credible framework for :
    - increasing convergence with the euro area,
    - tackling the challenges faced by accession countries on the road towards the adoption of the euro,
    - contributing to macroeconomic and exchange rate stability,
    - helping determine the appropriate level for the eventual irrevocable fixation of parities. This is to be accomplished in the best interest of the candidate countries themselves.
- **Thirdly, a sound and efficient banking and financial system is key**. Significant progress has been made over the past few years in rehabilitating the banking sector and encouraging structural reforms and foreign ownership. Progress in corporate governance, the enhancement of the legal and supervisory frameworks that support the banking sector are also crucial. They are conducive to achieving the macroeconomic objectives of the accession countries.

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To conclude, let me stress two words: ***rapidity and stability***.

Rapidity is a key word. We have not much time to meditate, decide, implement. The structural reforms, that we are badly in need of, must be implemented as rapidly as possible if Europe is to be up to its historical challenges. The Chinese say "It is later than you think" has never been so true. In any case, history itself does not wait for us. And when I look back, over the last twenty years, it seems to me that an unfortunately well-founded criticism could be that we have constantly under-assessed the rapidity of the stream of history: the rapidity of the deterioration of the situation in the USSR, the rapidity of the collapse itself, the rapidity of the enlargement process, the depth, the strength and intensity of the "desire of Europe", which is spreading over in the countries in transition.

Second word: *stability*. Economic and financial stability, in a period of excessive volatility and of wide boom-bust episode, financial and real stability appear to be a very precious asset. We have built a new world: technology has permitted instantaneous communication and incredibly powerful real-time computation. Globalization has created new cultural, conceptual, commercial and financial links between all economies including previously centrally planned systems; together technology and globalization are progressively driving us to a unified planet of universal rules and regulations, code of conduct and practices, market procedures and market instruments, accounting standards, etc. In this new world, phenomena which had traditionally a local or a national impact may be amplified and become dangerous at the global level: amplification of financial cycles, herd behaviour, global contagion.

Analysing the opportunities and the risks, and understanding the functioning of our system with a view to making it as stable as possible is a very exciting, ambitious and urgent task.

I thank you for your attention.