

Maurice O'Connell: The euro changeover in the Irish context

Statement by Mr Maurice O'Connell, Governor of the Central Bank of Ireland, to the Irish Parliamentary Joint Committee on Finance and the Public Service, in Dublin on 18 July 2001.

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Chairman

We are now less than six months away from the launch of euro banknotes and coin, three years after the introduction of the euro as a currency. The period of transition has been very long but this has been unavoidable because of the complex production and distribution process that is required. The euro will at last become a fully fledged currency on 1st January. For the first time the public in general will be able to relate to it as their own currency. This should have a very positive impact in terms of gaining acceptance of the new currency.

The changeover is a big undertaking for all countries of the euro area. The individual national central banks have worked closely together through the European System of Central Banks. There has been regular monitoring of production to ensure uniform quality of banknotes across the euro area. The overall production requirement for launch of the new currency is 15 billion banknotes and 50 billion coins. These figures are so large as to be almost incomprehensible. Each national central bank is charged with the responsibility of meeting requirements in its own country. In our case this means that we will provide more than 200 million banknotes and more than 1,000 million coins.

Members of this Committee will be familiar already with the banknote and coin denominations and the conversion rate against the Irish pound. May I remind you that the smallest coin (one cent) will have a value of less than a penny and the largest banknote (500 euro) will have a value close to £400. Traditionally the demand for high value banknotes in this country has been quite small.

The Central Bank of Ireland has three main functions in relation to the changeover:

- it must provide sufficient quantities of the new currency to meet the launch requirement and ongoing demand
- it must provide sufficient quantities of Irish currency right up to the end of this year and meet the peak Christmas demand
- it must withdraw the old currency after 1st January in an orderly manner.

The Central Bank is on course in the production of new banknotes and coin. Frontloading of coin to bank branches and major retailers will begin in September and frontloading of banknotes will begin in November. Contracts for distribution are being negotiated. For security reasons I would not wish to go into further detail on distribution arrangements at this time. In order to give the public the opportunity to familiarise themselves with the new coinage, starter packs of euro coins may be purchased from 17th December from banks and post offices. These packs will cost £5 and they will contain a selection of coins equal to 6.35 euro in value. It is understood that all member States in the euro area are taking a similar initiative. There will be no frontloading of banknotes to the public as this might effectively amount to bringing forward the launch date and it could generate undue confusion for both consumers and retailers at the busiest shopping time of the year. While the banks will be closed on 1st January, supplies of euro banknotes will be available from most ATM facilities.

The second leg of our responsibility is to maintain an adequate supply of Irish currency up to the end of this year. From the point of view of the Central Bank the timing of the changeover is by no means ideal as it comes immediately after the Christmas peak and in the middle of the Winter sales. The traditional pattern here is that demand for currency rises by 15-20 per cent between mid-November and Christmas. In recent times the Bank has tapered off production of Irish banknotes and coin because of the changeover. The Bank has, however, stocks of Irish banknotes and, particularly, Irish coin to ensure that the supply of cash to the system is adequate. The Bank has appealed to the public to release hoarded coin. In addition, a number of charities, with the full support of the Bank, will mount appeals for Irish coin in the autumn. It is hoped that these initiatives will secure a very positive response. The Bank is satisfied that there will be adequate supplies of currency in circulation to meet the requirements of the public over the Christmas period.

The euro will become legal tender on 1st January. The Irish currency will remain legal tender until 9th February. So there will be a period of 5-6 weeks during which the two currencies may circulate as legal tender. After that date the banks will accept Irish banknotes and coin for a period and, of course, the Central Bank will honour Irish banknotes and coin indefinitely. The intention is to withdraw Irish currency as quickly as possible after 1st January and retailers will be encouraged not to issue Irish currency in change. In this manner it is hoped that dual currency circulation will quickly be very limited and this should help to minimise any confusion that may arise. Obviously, the Central Bank cannot put precise figures on the quantities of Irish currency that must be withdrawn. I can tell you that there are roughly 180 million banknotes and 2½ billion coins on issue. The expectation is that the greater proportion of banknotes outstanding will be returned. As regards coin, we would not expect more than 80 per cent in overall value and considerably less in lower denominations.

The Minister for Finance has already indicated that the banks will not impose a handling charge on euro cash provided to retailers prior to 1st January. Also, there will be no charge on retailers for lodgement of Irish banknotes and coin during the dual circulation period and for a short time afterwards (up to 15th February). During this period the Central Bank will pay a lodgement fee to the banks in part compensation for the fee income that they will forgo. The cost is estimated at £5-£6 million. The total cost to the Central Bank of the changeover is likely to be in the region of £70 million; production materials will account for two thirds of the total outlay.

I have outlined the changeover programme of the Central Bank. We are also involved through a publicity campaign run by the European System of Central Banks in promoting familiarity with the new currency. We work in close co-ordination with other agencies such as the Euro Changeover Board of Ireland and Forfás and the Office of the Director of Consumer Affairs and I would like to acknowledge the contribution that these are making to preparations.

There is understandable concern that the changeover may boost inflation as traders may take advantage of the situation and round up prices or seek compensation through price increases for changeover costs that they may incur. In Ireland it is part of the folklore that decimalisation in the 1970s had inflationary consequences at the time. May I say, in relation to decimalisation, that an examination of the facts will demonstrate that it did not have any significant inflationary outcome. As regards the euro changeover the expectation is that any inflationary fallout should be small. This is the view of the European Central Bank which is monitoring developments on a euro area wide basis. It is considered that market competition and price transparency can soon reverse any inflationary effects of the changeover. At the same time there is need for vigilance as the opportunity for price increases is heightened in the months ahead. Fees and charges administered by Governments across the euro area will be price neutral or revised in favour of the consumer. Here at home there is a national code of practice whereby subscribers commit themselves to carrying out the changeover fairly and to seek no advantage from the conversion.

The European Central Bank has agreed that banknotes may be frontloaded outside the euro area from 1st December. It is likely that there will be significant demand for the currency outside the euro area. There is already considerable anecdotal evidence of high value banknotes being returned to central banks.

Another factor that must obviously demand attention at European level is the risk of counterfeiting. The European Central Bank is acutely conscious of this threat and it has in place arrangements to respond effectively and in a co-ordinated manner to any such danger, should counterfeiters seek to take advantage of the unique situation. As a precaution, the information campaign on the security features of the euro banknotes has been delayed as long as possible. The security features will be unveiled on 30th August.

There seems to be a perception that cross border retail money transfers of the new currency within the euro area may be much cheaper and simpler than before. Regrettably, this is not the case in the short term at least. The reality is that the national payment systems, including cheque clearing systems, have not so far been harmonised and there are no short term plans to develop a standard cross border system. In any event there would seem to be particular difficulty associated with developing a cross border paper based system. Customers may of course use their credit card and ATM cards cross border as before. The use of cheques in the euro area varies hugely. In Ireland and France cheques are still the most widely used payment instrument, accounting for almost one half of all non-cash transactions. In Germany and Austria, on the other hand, they account for less than 5 per cent of such transactions. I am aware that the European Commission is taking an interest in the cost of cross

border transfers within the euro area with the aim of achieving equalisation of banking charges as soon as possible.

From September onwards publicity campaigns for the euro introduction will be intensified both at European and national levels. In such a large logistical operation, it is probably inevitable that there will be some local difficulties. There is a strong confidence, however, that in general the changeover will go well and it will help to establish the euro as a powerful symbol of European identity.

I have outlined the various operational issues that arise in relation to the launch of the euro. It is appropriate to reflect at this point on why a single currency is being introduced. It is seen as essential to full exploitation of the single marketplace and to the economic integration of Europe. It is necessary for the evolution of a single monetary policy. With a multiplicity of currencies there are always extra costs and additional barriers to cross border trading. There is also a lack of transparency in pricing. In the new order it will be possible to compare prices directly from one country to another and this should be of considerable benefit to the consumer. A single currency will also lead to broader and deeper financial markets in Europe, thus increasing the choice of financial products for businesses and consumers. Europe also needs a single currency if it is to be a leader on the international stage. The US dollar will continue to be the dominant international currency for the foreseeable future but, in time, the euro may be able to challenge this dominance. Certainly, there was never any prospect that a fragmented Europe might be a serious challenger.

The euro has been weak against the dollar and other major currencies for an extended period since its introduction. The essential reason for this has been the net flows of European capital into the US economy in particular, as European investors have been attracted to higher returns in the US market. These flows would have occurred in any event if no currency change were taking place. It may be also that novelty and the absence of a track record have worked against the euro; it takes time to establish credibility. A currency without cash tends to be artificial, perhaps, even in the financial markets. All of this is about the change. The arrival, at last, of banknotes and coin will bring a new sense of permanence to the new currency.