

University of Economics in Katowice

Volume 16

2014

Journal of

**Economics &
Management**

Blandyna Puszer

Department of Banking and Financial Markets

University of Economics in Katowice

**THE EURO AS AN
INTERNATIONAL CURRENCY
IN THE OFFICIAL SECTOR**

Abstract

International currency is a currency that is used outside the country as unit of account, medium of exchange, and means of accumulation. International currency performs the functions of money in an international dimension. The international role of the euro refers to the use of the euro in global markets and by residents of countries outside the euro area. Non-euro area residents may use the euro, for instance, in payment transactions or financial market transactions with euro area residents or with other non-residents. In particular, the euro is used by the official sector of several non-euro area countries as a reserve currency, as an anchor currency or as an intervention. This article reviews official use refers mainly to the euro's role in third countries' monetary and exchange rate policies, in the form of an anchor or reference currency, a reserve currency or an intervention currency.

Keywords: *international currency, anchor currency, reserve currency, intervention currency.*

JEL Classification: *F360.*

Introduction

International position of international currencies including euro has been determined by the market and will be determined by the market in the future. Outside the territory of European Union euro can be used by the companies of different countries for the transactions inside these countries. In such situations euro is used as an international currency. Consequently, it is nationalized. Most economists claim that the world needs international currencies which function as money in private sphere as well as in official sphere. Private sector uses international currencies as currencies of invoices, price quotations, payments, exchange currency as well as the currency for financing and investment. Official sector uses them as reserve of currency, investment currency as well as the currency of reference. In official sector the level of international currencies use depends on political and economical significance of the country that issues the currency. The aim of this article is to present the evolution of euro significance in the public sector and to show the perspectives of the further internationalizing of the said currency.

1. International money's functions and conditions of its creation

In the subject literature international currency is defined in a various way. However, broad international use of the international currency is underlined. International currency is the currency used outside the country or the economic territory of the country issuing this currency¹. The currency is understood as international when it is used in international transactions². More precise definition is that international currency is the currency used by foreigners from outside the country issuing it in transactions with partners from the said country and with partners from other countries³. What is more, international currency has to fulfill classical money's functions, i.e. to be unit of account, medium of exchange as well as store of value. Traditionally, money's functions have their specificity depending whether they refer to private or official sector. Private sector includes use of euro by all the business (companies, banks and other financial institutions, public authorities and private citizens) functioning on the market. Official sector concerns mostly monetary authorities, i.e. mainly central banks⁴. The measure of international position of the currency is the use of the currency in:

- private sector: financing – earning means of finance, investment – storage of financial reserves, settlement currency – execution of effective payment regarding commercial contract, vehicle currency – execution of transaction in foreign currency concerning exchange in two different foreign currencies, quotation currency and invoicing currency – presenting prices and invoicing the supplies,
- in official sector: reserve currency, intervention currency and anchor currency⁵.

International status of currency is determined by the factors of structural character as well as macroeconomic stability of the country issuing the currency. Main factors of structural character are trade and production quantity as well as the magnitude of financial market of the country issuing the currency⁶. It should be emphasized that the greater participation of the country issuing the currency

¹ M. Chinn, J. Frankel, *Will the Euro Eventually Surpass the Dollar as Leading International Reserve Currency*, "NBER Working Paper" 2005, No. 11510, p. 4.

² P. Kannan, *On the Welfare Benefit in an International Currency*, "IMF Working Paper" 2007, No. 0749, p. 3.

³ E.G. Lim, *The Euro's Challenge to the Dollar: Different View from Economists and Evidence from COFER and Other Data*, "IMF Working Paper" 2006, No. 06153, p. 7.

⁴ L. Oręziak, *Międzynarodowa pozycja euro*, Euro od A do Z, NBP, Warszawa 2002, p. 172.

⁵ B. Puszer, *Międzynarodowa pozycja euro* [in:] *Finanse w dobie integracji europejskiej. Finance in enlarged European Union*, ed. R. Hanisz, K. Znaniecka, AE, Katowice 2004, p. 2005.

⁶ P. de Grauwe, *Economics of Monetary Union*, Oxford University Press, Oxford 2009, p. 258

in the world production as well as in world trade, the better opportunities for the currency to be used by the foreign business as invoicing currency and settlement currency. Consequently, financial authorities of the third countries will use it as anchor currency reserve currency and intervention currency. Taking into account the magnitude of the financial market of the country issuing the currency, i.e. the sum of stock market capitalization, value of securities as well as bank assets. Attention should be paid to the fact that the bigger financial market the better possibilities for the currency of a given country to be used by foreign business as vehicle currency or for financing as well as for investment. Simultaneously, monetary authorities of the foreign countries will be able to use it as reserve currency and intervention currency. The internationalization of the currency is determined by liquidity of the financial market and liberalization of the financial market (including the limits in the flow of capital) and it is also determined by variety of financial instruments understood as the range of investment capability. From the point of view international currency creation the magnitude of securities and shares market is more important. This value decides whether this monetary unit is able to function as the formal currency⁷.

Favourable factor for internalizing currency appears stable economic policy including stable monetary policy as well as stable fiscal policy. Main determinant for stable monetary policy is inflation rate which presets percentage average increase in prices. Significant increase may particularly effect use of currency as reserve currency. Increase in inflation may have negative effect on use of currency on debt market. It is because of higher interest rates as well as higher variability of exchange rate. Instability in value of given currency brings higher investment risk simultaneously diminishing its role as measure of hoarding⁸. Stability of purchasing power is not the only factor determining macro-economic stability. Full financial stability is also created by such fiscal parameters as: budget deficit. The result of this stability is building the trust in currencies which is important for enforcing all the functions of international money. Trust in legal and institutional conditions results from its political stability. Taking this fact into consideration, we may claim that only a politically stable country can issue international currency. It is because this stability is the base for economic stability and lack of this stability is the cause of currency collapse. Internationalization is also determined by network externalities which means that the more frequently the currency is used in trade the more probably it will be used, i.e. the more

⁷ *Międzynarodowa rola euro III*, Departament Integracji ze Strefą Euro (DISE), NBP, Warszawa 2011, p. 4-6.

⁸ E.G. Lim, op. cit., p. 7.

frequently the said currency is used as means of payment the lower transactional costs and higher flow on the market which improves attraction among new participants on the market. Force of habit using the currency is also an important element. It happens very often that when objective factors influencing internationalizations of currency disappear, the currency is still used as international currency. That is the reason why there are several international currencies but only one is dominating. The process of changing the status is long. The example of this are raw material markets where the habit and favourable circumstances are the reason that the dominating currency remains US dollar⁹.

2. Use of euro as anchor currency

Internationalization of currency includes its official use in monetary politics and exchange rate policy by third countries as anchor currency reserve currency and intervention currency. Its function as anchor currency is extremely important in the process of internalization. It is because it determines in indirect way the choice of reserve currency as well as intervention currency. Anchor currency is the currency which is the base for stabilization of the exchange rates and simultaneously it is also the base for defining currency parities. Taking this into consideration euro wide spectrum of reference is visible from loose to tight coupling as show in Table 1.

Table 1. Countries and territories with exchange rate regimes to the euro (as at end May 2013)

Region	Exchange rate regimes	Countries
1	2	3
EU (non-euro area)	ERM II	Denmark: Participates in ERM II with a +/-2.25% fluctuation band. Latvia*: Participates in ERM II with a +/-15% fluctuation band. Latvia continues with a fluctuation band of +/-1% as a unilateral commitment. Lithuania: Participates in ERM II with a +/-15% fluctuation band. Lithuania continues with its currency board arrangement as a unilateral commitment
	Euro based currency boards	Bulgaria: Maintains a peg to the euro within the framework of a currency board arrangement
	Management floating regime with the euro as reference and an inflation target	Czech Republic, Romania
	<i>Pro memoria:</i> free-floating regime with inflation target	Hungary, Poland, Sweden, United Kindon

⁹ I. Pszczółka, *Współczesne waluty międzynarodowe*, CeDeWu, Warszawa 2011, p. 23.

table 1 cont.

1	2	3
EU acceding, candidate and potential candidate countries	Unilateral euroisation (no separate legal tender)	Kosovo, Montenegro
	Euro-based currency boards Stabilized arrangement with euro as a reference currency	Bosna and Herzegovina, Former Yugoslav Republic of Macedonia
	<i>Pro memoria</i> : Free-floating regime with an inflation target	Albania, Iceland, Serbia, Turkey
	Euroization	European microstates: Republic of San Marino, Vatican City, Principality of Monaco and Andorra. The other countries and jurisdictions are entitled to use the euro as their official currency. Liechtenstein uses the Swiss franc as its official currency. Saint Barthélemy, Saint Martin and Saint-Pierre and Miquelon are French overseas collectivities, but use the euro as their official currency. Some French overseas collectivities
	Pegs based on the euro	CFA franc zone: WAEMU (Benin, Burkina Faso, Côte d'Ivoire, Guinea-Bissau, Mali, Niger, Senegal, Togo) and CEMAC (Cameroon, Central African Republic, Chad, Republic of Congo, Equatorial Guinea and Gabon). CFP franc zone: New Caledonia and the French overseas collectivities of French Polynesia and Wallis and Futuna. Cape Verde, Comoros, São Tomé e Príncipe
	Other arrangements using the euro as a reference currency	Switzerland: On 6 September 2011 the Swiss National Bank issued a statement establishing a minimum exchange rate for the euro of CHF 1.20 per euro. As stated in the Swiss National Bank's annual report for 2011, the Swiss National Bank would "enforce this minimum rate with the utmost determination and was prepared to buy foreign currency in unlimited quantities"
	Crawling peg involving the euro	Bostwana
	Pegs and managed floats based on the SDR and other currency baskets involving the euro (share of the euro)	Algeria: Managed floating regime with no preannounced path for the exchange rate. Belarus: The currency was pegged to a basket comprising the euro, the US dollar and the Russian rouble at the beginning of 2009, with a fluctuation margin of 10%. In April 2011 the Belarussian rouble lost more than a third of its value against the US dollar after the central bank introduced a free floating exchange rate for trade between banks. Fiji: The currency was pegged to a basket of international currencies in May 2007. Iran: Maintains de jure a managed floating arrangement against a basket of currencies including the euro, the US dollar and the Japanese yen. Kuwait: The currency was pegged to a basket of international currencies in May 2007. Libya: The rate of exchange is established using a basket of SDR currencies with a fluctuation margin of 25%. Morocco: Bi-currency basket comprising the euro (80%) and the US dollar (20%). Russian Federation: Trade-weighted currency basket for monitoring and setting ceilings for real appreciation (combined share of euro and euro-linked currencies of around 60%); since February 2005 US dollar-euro basket for daily

table 1 cont.

1	2	3
		<p>exchange rate management (since February 2007 the euro's share has been 45%). The Bank of Russia does not target a specific exchange rate level against the currency basket.</p> <p>Samoa: The central bank maintains an exchange rate peg based on a basket comprising the currencies of Samoa's six main trading partners and countries that represent primary sources of tourism revenue, namely New Zealand, Australia, the United States, and the euro area. The exchange rate can fluctuate within +/- 2% band.</p> <p>Singapore: Since 1981 a managed floating regime against an undisclosed basket of currencies maintained within an undisclosed target band.</p> <p>Syria: In August 2007, the authorities changed the de facto exchange rate regime from a peg to the US dollar to an SDR basket within a relatively wide fluctuation margin.</p> <p>Tunisia: The de facto exchange rate regime is a conventional peg to an undisclosed basket of currencies.</p> <p>Vanuatu: Weighted basket comprising (undisclosed) currencies of Vanuatu's major trading partners</p>

* Latvia 1.01.2014 introduced the euro.

Source: Based on: *The International Role of the Euro*, ECB, Frankfurt am Main 2013, p. 67.

It can be claimed that most of the countries which decided to relate their currency to euro had practically no real alternative. These are mostly European Union countries like Bulgaria, Denmark, Lithuania and Romania and European countries like San Marino, Vatican, potential candidates like Bosnia, Serbia, Kosovo, Montenegro, and members of French franc zone. What is more, some other countries of the world mostly African ones for example Malta, Congo, Benin, Niger, Latvia and other have related their country's currencies to SDR or to some other currency baskets which included euro. It is important to pay attention to such a solution called "euroization" which means one sided resignation from their own currency and accepting euro as the only legal mode of payment¹⁰. It is explained as the countries (Kosovo, Montenegro) aspire to form a solid base for stabilization of their economy.

Decision to stabilize exchange rate of their currency by forming a nominal base of relation for their domestic prices as well as relating their currencies to foreign currencies including euro is made mainly by their economic authorities. Additional important benefit is restriction of exchange rate and promotion of export¹¹.

¹⁰ L. Oręziak, *Międzynarodowa pozycja...*, op. cit, p. 172.

¹¹ J. EScriva, G. Garcia-Herrero, G. Nuno, J. Vial, *After Bretton Woods II*, "BBVA Working Papers" 2008, No. 0806, p. 6.

The role of euro as anchor currency is mostly the result of situation inherited because of domestic currencies of the countries belonging to euro zone. The main reason for using euro as the currency that stabilize exchange rate of related currency is close cooperation in trade. What is more, use of euro as the base for other currencies is the expression of trust in stable monetary policy made by ECB. It is worth mentioning that this choice is also one-sided (without ECB obligation). Most frequently countries geographically close to euro zone are interested in euro as anchor currency. It is distinguishing feature between euro and US dollar which is used as the base by the countries from most of the continents.

Discussing the role of euro as anchor currency it should be mentioned that it is part of SDR basket (Table 2).

Table 2. Currency basket SDR

Years	USD	EUR	JPY	GBP
2001-2005	45%	29%	15%	11%
2006-2010	44%	34%	11%	11%
2011-2015	41,9%	37,4%	9,4%	11,3%

Source: Based on: *Currency Composition of Official Foreign Reserves (COFER)*, IMF, 2013, www.imf.org (15.11.2013).

The share of euro in the SDR basket has increased from 29% to 37,4% since 2011. What is more, simultaneously the share of US dollar and Japanese yen has decreased. It mostly is the result of increase in nominees reserves which are in euro (kept outside the euro zone) and which have been analyzed for five years. To lesser extent it is because of increase in participation of euro zone in export of four economies (euro zone, Japan, United States and Great Britain). At present the problem of accepting more currencies to SDR basket is under debate. Next review of SDR basket is planned in 2015.

3. Use of euro as reserve currency

The main determinant showing international importance of the currency is the participation of this currency in official reserve assets. Reserve assets can be described exchange resources, foreign securities and gold managed by central bank. They are one of the most important part of financial security system of every country. There are four reasons for keeping and collecting foreign reserve assets:

- Precautionary motive – the level of reserves influences credit assessment of the country; the high level of the reserves enhances investors trust in financial situation of the country. What is more, it limits the outflow of the capital.

- Transactional motive – foreign exchange reserves are used in order to balance the payments.
- Intervention motive – foreign exchange reserves are used in foreign exchange interventions which is important while using the policy of stable foreign exchange rate.
- Income motive – foreign exchange reserves are used as the source of income for central bank¹².

One of the main motives for keeping foreign exchange reserves is to have a good monetary service for foreign trade exchange as well as to provide foreign currency for business¹³. Following factors are needed when we consider the level of the use of given currency as reserve currency. First, the size of the economy that supports the currency and the most important is the position of the said economy in the world's economy (its participation in the world's trade exchange) and the perspective of its change. Secondly, trust in the currency which is based on economic policy as well as on institutions-legal conditions. Consequently, attention should be focused on monetary policy which influences stability of prices as well as remaining relatively low level of long-term interest rates¹⁴.

There are following determinants of the currency as international currency:

- Tendency of monetary authorities to keep the foreign exchange reserves in the currency of main trade partners,
- Monetary structure of foreign debt which influences the allocation of foreign exchange reserves.
- Mechanism (policy) of foreign exchange rate in use, relating national currency exchange rate to foreign currency exchange rate,
- Accepted strategy of risk diversification,
- Size and flow of debt securities market,
- Changes of foreign exchange rates¹⁵.

Analysing the importance of euro in official reserves in the period 1999-2012 it should be mentioned that there is a certain mistake in the process. It is because the data is not complete as some countries for example Asian countries do not report all details to International Monetary Fund. In the statistics there is

¹² *Mechanizmy funkcjonowania strefy euro*, red. P. Kowalewski, G. Tchorek, NBP, Warszawa 2010, pp.161-162.

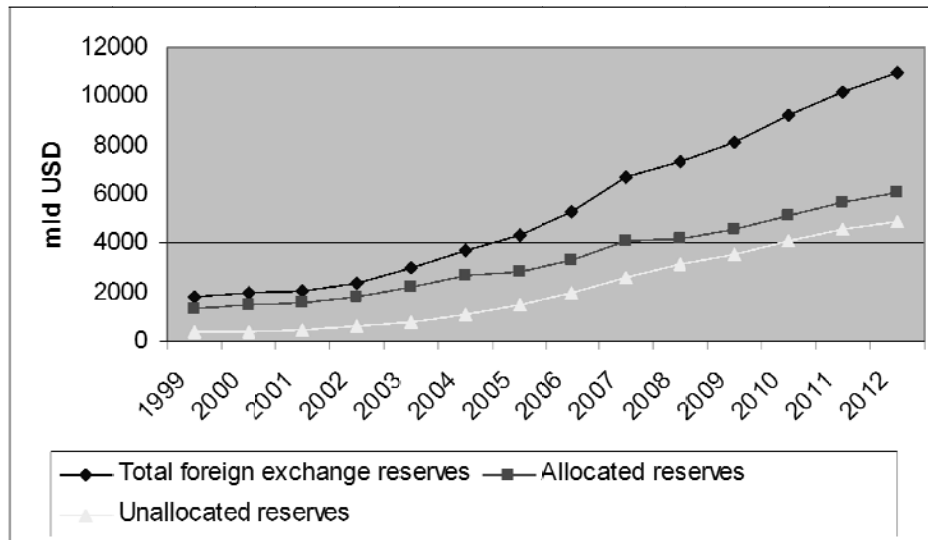
¹³ Oręziak L., *Euro – pieniądz międzynarodowy, Europejska Integracja Monetarna od A do Z*, „Bank i Kredyt” 2008, No. 1, p. 8.

¹⁴ *The International Role of the Euro*, ECB, Frankfurt am Main 2013, pp. 36-38.

¹⁵ E. Papaioannou, R. Portes, G. Siourounis, *Optimal Currency Shares in International Reserves: The Impact of the Euro and the Prospects for the Dollar*, “NBER Working Paper”, 2006, No. 12333, pp. 11-12.

a division into allocated reserves and unallocated reserves. Additional problem is that much faster increase of unallocated reserves value than allocated reserves (see Figure 1).

Figure 1. The level of world's foreign exchange reserves in 1999-2012



Source: Based on: *Currency Composition of Official Foreign Reserves (COFER)*, IMF, 2013, www.imf.org (15.11.2013).

Taking into consideration the participation of euro in world's allocated foreign exchange reserves (Table 3, Figure 2) relative stability of participation of main currencies in the world's foreign exchange reserves is observed. It is because of the combination of factors including foreign exchange rate mechanism (anchor currency) their flow and security features.

Table 3. Currency composition of official foreign exchange reserves (mld USD)

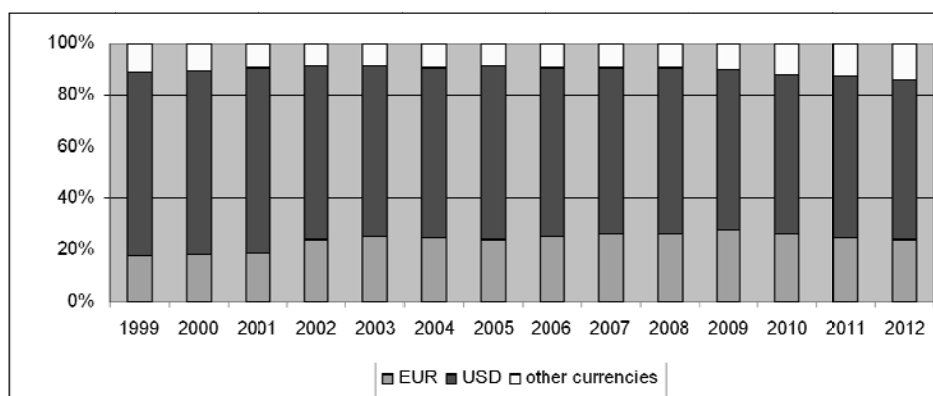
Year	USD	EUR	Other Currency
1	2	3	4
1999	979,8	246,9	153,0
2000	1079,1	277,7	161,4
2001	1122,4	301,1	146,1
2002	1194,2	424,7	176,9
2003	1454,9	556,5	221,5
2004	1739,2	655,2	260,6
2005	1891,4	679,3	272,8

table 3 cont.

1	2	3	4
2006	2157,6	827,2	330,7
2007	2631,3	1076,2	411,8
2008	2684,9	1103,5	421,8
2009	2847,9	1269,6	472,4
2010	3191,9	1342,5	627,5
2011	3523,9	1393,9	733,3
2012	3729,2	1469,9	887,9

Source: Ibid.

Figure 2. Currency shares in foreign exchange reserves with disclose composition – all countries (at current exchange rates)



Source: Ibid.

Inertia of US dollar position in world's reserves is particularly connected with the following fact: the process to limit the participation of dominating the reserves asset must be slow, otherwise the seller will notice the decrease of the portfolio. Despite this, the participation of the individual currencies in exchange reserved has been slowly changing. In 1999-2001 the dominating currency was US dollar and its participation in the world's reserves was 71%, while euro – from 18% to 19%. In this time the main hindrance to the process of changes in some of the exchange reserves was the weakness of euro exchange rate on exchange market. In view of that the central banks of the developing countries we not very much interested in diversification their reserves. This trend started changing since the year 2002. It was because of systematically growing trust in euro. In 2009 allocated reserves in US dollars were 61% of world's reserves while euro was more than 27%. This

change was taking place systematically not radically. It was not only at the expense of US dollar but other currencies as well. Since 2009 the stability of the US dollar participation 62% in world's reserves has been taking place. While the participation of euro has decreased to 24% which has confirmed significance of US dollar as the most important international currency. What is more, it is particularly visible in time of international financial crisis. Since the year 2010 decrease of euro participation in the world's reserves is observed. However, euro is the second reserve currency which may be the reason of debts crisis in euro zone. In the research conducted by the Royal Bank of Scotland among administrators of the reserves from 39 central banks keeping 35% of global world's exchange reserves, more than 80% respondents indicated that debt crisis influenced their strategy of exchange reserves management. Possible changes in portfolios as a part of nominal segment in euro were based on increase in participation of euro zone issuers' securities. The issuers had proper fiscal positions. In addition issuers from European Union with AAA rating were also accepted (for example European Financial Stability Facility started issuing bonds in euro which interest central banks and sovereign wealth funds). The shifts in reserve portfolios of central banks coincided with adjustments in Euro zone governmental bonds belonging to private investors. This reflects deteriorating fiscal situation in euro zone countries. What is more, it is connected with higher credit risk of numerous financial institutions in euro zone. Since the beginning of the crisis the tendency of stronger involvement in Japanese yen and other currency is visible. It concerns such currencies as raw materials currency, Australian dollar, Canadian and New Zealand dollar. These issuers of the above mentioned currency have higher interest rates and relatively better fiscal perspectives. Continuation of the relocation financial resources from dollar's market into other currency may face some limits in flow examples of that are Australian and New Zealand's markets. Potential of increase in participation in reserves the „other” groups is limited by the local market of bonds. As the precautionary motive together with investment motive is one of the main reasons for keeping reserves. Any significant increase in investments on less liquid markets is unlikely. Limits in currency and instrumental diversification may intensify particularly in case of further reserves increase¹⁶.

Analysing the participation of euro in world's exchange reserves attention should be paid to the use of this currency by central banks of developed countries as well as rising and developing countries (Table 4-5, Figure 3-4).

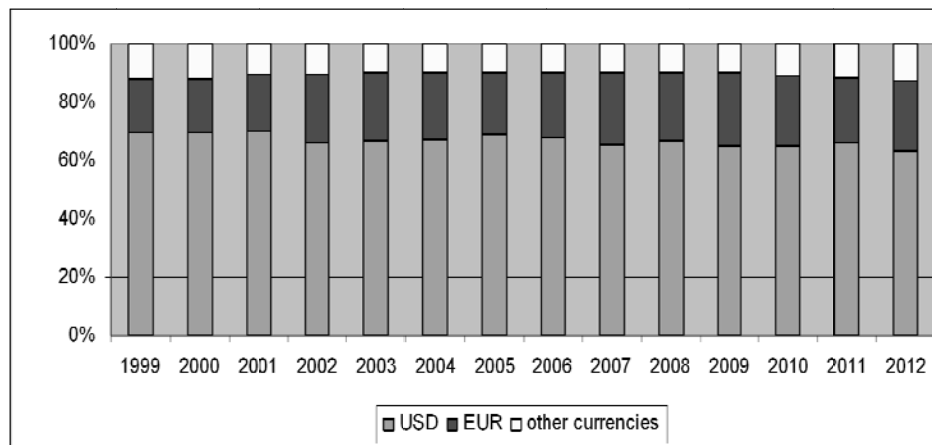
¹⁶ *Miedzynarodowa rola...*, op. cit., pp. 16-17.

Table 4. Currency composition of official foreign exchange reserves – advanced countries (mld USD)

Year	All Allocated reserves	EUR	USD
1999	1010,8	182,9	705,6
2000	1107,9	203,9	772,5
2001	1123,1	213,5	792,4
2002	1278,9	297,4	849,7
2003	1556,9	359,1	1045,1
2004	1825,6	417,2	1227,9
2005	1821,5	387,0	1261,3
2006	1982,2	440,5	1350,5
2007	2156,9	522,2	1423,5
2008	2197,5	511,2	1475,9
2009	2428,6	616,4	1582,0
2010	2707,9	646,7	1761,9
2011	3012,0	672,4	2003,9
2012	3281,9	792,5	2045,5

Source: Ibid.

Figure 3. Currency shares in foreign exchange reserves with disclose composition – advanced countries (at current exchange rates)

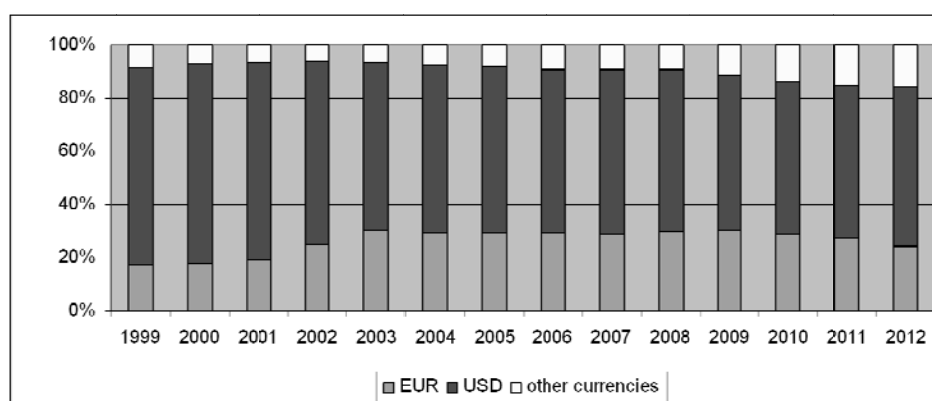


Source: Ibid.

Table 5. Currency composition of official foreign exchange reserves – emerging and developing countries (mld USD)

Year	All Allocated reserves	EUR	USD
1999	368,9	63,9	274,1
2000	410,4	73,8	307,5
2001	446,4	87,6	330,1
2002	516,8	127,3	344,5
2003	666,1	197,4	409,8
2004	829,4	238,0	511,2
2005	1022,1	292,3	630,1
2006	1333,3	386,8	807,1
2007	1962,3	553,9	1207,8
2008	2012,7	592,3	1209,0
2009	2161,4	653,2	1265,9
2010	2454,1	695,8	1429,9
2011	2639,1	721,5	1520,0
2012	2802,1	667,4	1680,7

Source: Ibid.

Figure 4. Currency shares in foreign exchange reserves with disclose composition – emerging and developing countries (at current exchange rates)

Source: Ibid.

In case of developed countries the main reserve currency was US dollar. However, its participation decreased from 70% in 1999 to 63,5% in 2012. Simultaneously, participation of euro increased from 18% in 1999 to 23% in 2012. Steady increased in foreign exchange reserves was notice in rising and developing countries and it was disturbed only for a short period as a result of global financial crisis. Evaluation of the currency composition of given country is im-

peded because most of the countries do not reveal this information. Table 6 presents the euro participation in foreign reserves in selected countries. Reserves are kept in euro in EU countries or countries candidates for EU. It is not so frequently used by the countries in Asia or Latin America. Some reserves of the USA, Canada, Russia or Switzerland are also kept in euro.

Table 6. Currency composition of foreign exchange reserves for selected countries (share the euro in the total foreign exchange reserves holding percentages, at current exchange rates)

Country	2007	2008	2009	2010	2011	2012
Non-euro EU Member States						
Non-euro EU Member States	68,6	61,3	63,7	61,1	60,9	58,0
Bulgaria	99,1	99,1	99,1	99,6	99,9	99,9
Croatia	84,1	76,6	71,7	73,7	75,9	n.a.
Czech Republic	54,0	62,6	61,3	57,4	60,1	58,7
Latvia*	38,8	60,5	63,1	58,3	57,0	51,4
Lithuania	96,1	97,3	96,9	98,9	94,9	83,4
Poland	36,3	33,7	36,7	35,0	30,4	30,9
Romania	67,8	63,2	65,2	67,2	77,8	73,0
Sweden	46,9	48,5	48,1	50,0	37,0	37,1
United Kindon	68,4	41,4	65,5	59,0	59,1	60,4
Candidate and potential candidate countries						
Turkey	55,2	46,0	44,6	46,5	40,3	27,3
Other industrial countries						
Canada	47,5	40,4	41,9	40,0	37,0	34,9
Norway	44,0	48,3	47,2	36,4	36,1	35,9
Russia	38,8	40,0	33,2	43,1	42,1	40,4
Switzerland	40,2	47,9	55,6	54,9	57,0	50,1
United State	37,9	53,7	54,0	54,2	53,5	57,0
Latin American countries						
Chile	34,8	37,3	34,8	35,2	35,5	20,3
Peru	11,9	14,9	17,4	16,8	38,0	30,0

* Latvia 1.01.2014 introduced the euro.

Source: Based on: *The International Role...*, op. cit., p. 66.

To sum up, more serious significance of euro as reserve currence is visible. However, US dollar still remains as dominating currency. The significance of euro as reserve currency is the most visible in countries bordering euro zone as well as in countries having institutional connections with EU. The analyze of the participation of given currencies in the world's foreign currency reserves show

the process of US dollar deposition has already started and multipolar system is presently visible. Positive impact on the role of euro as international currency may have issuing common European treasury bonds (stability bonds). However, because of political reasons it is very far perspective if possible at all. Apart from that more significant role of euro may influence further extension of Economic Union as well as Monetary Union and positive decision of Great Britain. That would be a great impact for increase of common financial market as well as participation of the euro zone in trade particularly with Asian countries.

4. Use of euro as intervention currency

Next function of international currency in official turnover is intervention currency function. Intervention currency it is the currency used by monetary authorities in order to intervene on financial market. Banks intervene to achieve different goals for example to limit inflation, to have effective allocation of resources, to sustain international competitiveness, to have dynamic economic increase as well as to have financial stability. The choice of the this type depends on the level of economic development of given country, on the level of the development of its financial market as well as on sensitivity to economic shocks. In order to accomplish the goals central banks try to keep the certain level of exchange rate. Consequently, they want to secure its stability as well as to diminish its changes and regulate the level of foreign exchange reserves¹⁷. Efficiency of intervention depends on transmission channel it includes: signaling channel, portfolio balance channel and monetary policy channel. Signaling channel in other words expectation channel works when the market is aware of the actions taken by the central bank. It means efficiency of verbal intervention. Portfolio balance channel is efficient only while intervention is in progress. Otherwise, demand and supply on financial market do not change. In monetary policy channel attention is focused on significance for forming exchange rate as well as for difference in interest rates on domestic and foreign market. Change in difference of real interest rate as the result of monetary policy may effect the change in exchange rate, particularly when it was not expected¹⁸. To sum up, talking about transmission channels we can distinguish three types of interventions:

- real, when the market is conscious (intervention takes place exactly on the day when the rumours appear),

¹⁷ R. Moreno, *Motives for Intervention* [in:] *Foreign Exchange Market Intervention in Emerging Markets: Motives, Techniques and Implications*, "BIS Paper" 2005, No. 24, p. 4.

¹⁸ D. Arche, *Foreign Exchange Market Intervention: Methods and Tactics* [in:] *Foreign Exchange Market Intervention in Emerging Markets: Motives, Techniques and Implications*, "BIS Paper" 2005, No. 24, p. 40.

- real when the market is unconscious (it is done officially without any rumours),
- presumptive intervention which was not officially done despite the rumours¹⁹.

The choice of intervention currency is the consequence of its use as reserve currency as well as anchor currency. The most important determinant for the choice of intervention currency is its flow on the foreign currency market and the common acceptance. In case of countries that relate their currency to selected international currency the main currency used for interventions is the currency of reference.

Central banks perform interventions in order to gain different economic goals. Motives and the choice of currency in which interventions are performed can change. It depends on the economic level and financial development of a given country. As far as rising and developing countries are concerned most frequently interventions support exchange rate policy; central banks usually play the role “market maker” and they are the source of flow for poorly developed foreign exchange market. Significant feature of these interventions is their high efficiency, The example of that are the interventions performer by the central bank of Czech Republic, Hungary, Singapore (including use of euro). In developed countries with floating exchange rate, interventions are usually used for stabilization the fluctuations in exchange. In addition they are used when the market overvalues the exchange rates as well as to support the flow on the market during crisis.

Significance of euro as intervention currency is particularly visible in countries bordering euro zone and in the countries which have institutional connections with EU. The examples of that are countries which currencies participate to ERM II (Denmark and Lithuania). There is bilaterally agreed bandwidth of fluctuation for Danish crown $\pm 2,25\%$, Lithuania participates to ERM II with standard fluctuation margin $\pm 15\%$. Interventions in ERM II as a rule are performed in euro and in the currencies using the mechanism. EBC and national central banks of the countries which currencies participate to ERM II inform each other of every foreign exchange intervention on the edges and in frame of possible bandwidth of fluctuation. Interventions on the edges of permitted bandwidth of fluctuation have never been performed.

After the crisis on financial market in 2008 main central banks started to have stronger influence on the foreign currency rates. The examples of that is The Swiss National Bank (SBN), which intervened in order to bring down appreciation pressure on Swiss franc, in the second quarter of 2010. What is more, G-7 countries performed the coordinated foreign exchange intervention and one of the currency was euro. It was the first intervention like that in the period of ten years. Last coordinated intervention like that was performed in 2000. On

¹⁹ I. Pszczółka, op. cit., p. 129.

22th of September, EBC, monetary authorities of the USA, Japan, Canada, and Great Britain intervened against further depreciation of euro in relation to US dollar. Additionally, on 3rd, 6th and 9th November there were unilateral EBC interventions which were the continuation of coordinated intervention of 22nd of September²⁰.

Central banks decide to intervene different transmission channels for example monetary policy channel was used by the central bank of the Czech Republic and the central bank of Hungary, portfolio balance channel like central banks of Czech Republic, Hungary, Turkey and Singapore. Expectation channel was used by the central bank of Czech Republic Hungary and Turkey. It is the result of interventions performed to achieve different goals in different time.

Conclusions

Euro in relatively short period of time became the second international currency in the official sector. ECB – accepted the neutral position, it does not accept the internalization of euro as a goal. What is more, it does not force the use of euro by the countries that are not in the euro zone. The use of euro as international currency in official turnover should be based on economical and financial development as well as on politics that are inside and outside euro zone. Additionally, it is based on decisions made by the participants of financial markets. Essential role is played by such factors as the level of integration, liberalization, reliable monetary policy focused on internal price stability, legal regulation, reduction and proper management of public debt and finally, it depends on EU extension.

International position of euro was in the past and will be in the future determined by market. Developing liberalization and globalization of international financial markets is the reason for restricted possibilities of direct influence on international use of certain currency by monetary authorities. In view of that the increase of international euro significance will mainly depend on reasonable progress in construction of uniform financial market in frame of European Union territory. Despite of previous action financial market of European Union is not uniform. There are still differences in legal regulations of euro zone countries. International position of euro in official turnover in future will depend on the pace of development of such countries like China and India. Many simulations show that China will strengthen its position in world's economy as well as in international trade. However, it is unlikely that Chinese currency will be commonly used international currency in the nearest future. Considering the fact that

²⁰ *Międzynarodowa rola...*, op. cit., p. 19.

China as well as other countries of south-east Asia accumulated the majority of currency reserves in US dollars. It is mainly the policy of these countries will depend for the future of American currency. We may expect, that countries that have the largest foreign reserves in US dollars will continue further diversification of their reserves in case of further depreciation of the said currency. We cannot expect the radical tendency towards euro in the near future. However, we cannot exclude the situation the euro will be dominating currency. On the other side it is difficult to imagine the changes that would have to appear in American economy to make the role of US dollar less important. Considering the role of US economy in international trade, all the sudden changes that would happen could influence world's economy. In view of that, it is important for all the countries to be sure that all the changes that take place in monetary system are harmonious and made very gradually. Reforms that are introduced and carried out by euro zone countries should facilitate further development of our economics and make the more competitive. Particularly they will be to compete with two most important partners the USA and Japan. It is the chance for gradual harmonious growth of euro significance, which has already become stable and appreciated currency in the world.

References

- Arche D., *Foreign Exchange Market Intervention: Methods and Tactics* [in:] *Foreign Exchange Market Intervention in Emerging Markets: Motives, Techniques and Implications*, BIS Paper 2005, No. 24.
- Chinn M., Frankel J., *Will the Euro Eventually Surpass the Dollar as Leading International Reserve Currency*, "NBER Working Paper" 2005, No. 11510.
- ECB, *The International Role of the Euro*, ECB, Frankfurt am Main 2013.
- EScriva J., Garcia-Herrero G., Nuno G., Vial J., *After Bretton Woods II*, "BBVA Working Papers" 2008, No. 0806.
- Grauwe P. De, *Economics of Monetary Union*, Oxford University Press, Oxford 2009.
- IMF, (2013), *Currency Composition of Official Foreign Reserves (COFER)*, www.imf.org (15.11.2013).
- Kannan P., *On the Welfare Benefit in an International Currency*, "IMF Working Paper" 2006, No. 0749.
- Lim E.G., *The Euro's Challenge to the Dollar: Different View from Economists and Evidence from COFER and other Data*, "IMF Working Paper" 2006, No. 06153.

- Mechanizmy funkcjonowania strefy euro*, ed. P. Kowalewski, G. Tchorek, NBP, Warszawa 2010.
- Międzynarodowa rola euro III*, Departament Integracji ze Strefą Euro (DISE), NBP, Warszawa 2011.
- Moreno R., *Motives for Intervention* [in:] *Foreign Exchange Market Intervention in Emerging Markets: Motives, Techniques and Implications*, „BIS Paper” 2005, No. 24.
- Oreżniak L., *Euro – pieniądz międzynarodowy, Europejska Integracja Monetarna od A do Z*, „Bank i Kredyt” 2008, No. 1.
- Oreżniak L., *Międzynarodowa pozycja euro*, Euro od A do Z, NBP, Warszawa 2002.
- Papaioannou E., Portes R., Siourounis G., *Optimal Currency Shares in International Reserves: The Impact of the Euro and the Prospects for the Dollar*, “NBER Working Paper” 2006, No. 12333.
- Pszczołka I., *Współczesne waluty międzynarodowe*, CeDeWu, Warszawa 2011.
- Puszer B., *Międzynarodowa pozycja euro* [in:] *Finanse w dobie integracji europejskiej. Finance in enlarged European Union*, ed. R. Hanisz, K. Znanińska, AE, Katowice 2004.