



european community

NEWS

November 8, 1993

No. 56/93

MAASTRICHT TREATY FREEZES THE COMPOSITION OF THE ECU

Henning Christophersen, EC Commissioner for Economic and Financial Affairs, announced today that the composition of the basket comprising the European Currency Unit (ECU) was frozen on November 1, 1993 in accordance with a provision of the Maastricht Treaty which entered into force that same day.

The provision (Article 109g) fixes the basket composition as defined on September 21, 1989, the last time the basket was adjusted. No further recompositions of the ECU basket will be permitted until the ECU becomes a currency in its own right.

According to Commissioner Christophersen, freezing the monetary amounts (composition) of the ECU basket has several advantages:

1. As the ECU will be adopted as the single European currency in Stage III of European Monetary Union (by 1999 at the latest), it is essential that it continues to evolve as a strong and stable currency in the meantime. With no possibility of further basket recompositions, this objective will be achieved as economic convergence between member states continues.
2. By freezing the monetary amounts of component currencies within the ECU basket as opposed to irrevocably fixing the weight attached to each currency in it, uncertainty associated with the use of the ECU in financial and commercial transactions will be reduced concurrent with a further hardening in the value of the ECU.

BACKGROUND

The ECU is a currency basket composed of fixed amounts of each of the currencies of the EC member states. Its value can be calculated in terms of any of the component currencies, and this value can in turn be used to derive the weight of each currency within the basket.

To date, there have been two recompositions of the ECU basket: in 1984 (when the Greek drachma was added to the basket) and 1989 (when the Spanish peseta and Portuguese escudo entered the basket). In between these revisions, no alterations to the monetary amounts of each currency in the basket were permitted. By excluding the possibility of further basket recompositions, the monetary amounts of each currency composing the ECU basket, as defined at September 21, 1989, will henceforth be irrevocably fixed until the beginning of Stage III, at which time the ECU will become a currency in its own right. (The EC is currently in Stage I; Stage II begins in January 1994.)

Freezing the composition of the basket does not imply that the weights deriving from the monetary amounts of component currencies will subsequently be fixed. In fact, as the value of any component currency fluctuates on the foreign exchange markets in response to prevailing supply and demand conditions, so will its weight in percentage terms.

../.

Since the last revision of the ECU basket on September 21, 1989, the weight of the stronger currencies has increased over time, from 70.8 percent to 74.66 percent, at the expense of weaker ones whose weight decreased accordingly from 29.2 percent to 25.34 percent. As a result, the ECU's resistance to devaluation ("hardness") has increased.

The use of the ECU in financial transactions in particular has grown very rapidly in recent years due both to its role as the future single European currency, but also to its inherent, risk-management characteristics. As a weighted-average of Community currencies, the purchase of ECU paper allows investors to enjoy the benefits of a diversified, pan-European portfolio without the degree of risk exposure involved when using a variety of national instruments.

Removing the risks associated with a modification of the monetary amounts of component currencies within the ECU basket will encourage further increases in the depth and liquidity of ECU financial markets and will better facilitate their smooth function:

- for those market participants who stabilise the ECU exchange rate by taking positions in the ECU against the basket.
- for all operations in the ECU clearing system, where the interest rates are computed on the basis of the basket composition.

The ECU clearing system, which facilitates intra- and cross-border payments in ECU (which arise due to commercial or financial activities) is one of the most efficient clearing systems, providing same day value payment with an average daily turnover of approximately ECU 50 billion.

Press Contacts: Ella Krucoff
Tel: (202) 862-9540

Maeve O'Beirne
Tel: (202) 862-9549