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# THE EURO, THE UK AND THE CITY OF LONDON

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The completion of the euro changeover at the beginning of this year is an event unprecedented in monetary history. It directly affects the lives of over 300 million people in 12 countries in Europe, and it has wider implications around the world.

This is what His Holiness the Pope had to say about it last month. "The Holy See pays careful attention to the building of a united Europe carried out in a spirit of negotiation and dialogue that has allowed nations that were once enemies to work together in a project of mutual co-operation that has now become a true community of nations. The single currency represents a further step in this evolution."

The President of the European Commission, Romano Prodi, said on 31 December: "The euro is your money. It is our money. It's our future. It is a little piece of Europe in our hands."

The President of the European Central Bank, Wim Duisenberg, pronounced the euro changeover a "tremendous success" and said: "On 1 January, the introduction of the euro banknotes and coins marked not only the completion of EMU, which is a crucial achievement in itself, but one of the major, if not the major step forward in the history of European integration. I am convinced that 1 January 2002 will appear in the history books in all our countries and beyond as the start of a new era for Europe."

Well, it is not for me as a humble director of a national central bank to comment on statements of this kind! But what I can do is to make a sober, if necessarily preliminary, assessment of how the changeover has gone so far, and its implications. To do this, I want to start by setting the changeover briefly in context by considering the broader significance of the euro's introduction. Then I shall move on to talk specifically about the completion of the euro changeover itself; the UK's approach to EMU; and the role of the City of London in the euro markets.

**The significance of the introduction of the euro**

The changeover to the euro is the culmination of a project for European integration which dates back literally half a century. And it is over 30 years since Economic and Monetary Union became a goal of the Heads of Government of the founding members of the European Union, as it is now known. Since then, the project has developed through a number of stages: market integration; monetary integration; and economic integration.

The underlying objective of market integration, through the Single European Market, is to enable a company operating in one European country to conduct its business on the same basis in any other European country. This has not been achieved by attempting to harmonise all the different national regulations involved. Politically, that would have been far too difficult, and in practical terms, it would have taken far too long. Instead, the Single Market has been implemented by agreeing in each case the minimum level of harmonisation required and, above that minimum, by mutual recognition of one country's rules in all the others. On this basis, the European Union has, over the past 15 years, made great strides towards implementing a Single Market. Of course, the Single Market is still not complete. But the European Union is much more of a single market now than ever before. And it is important to note that the UK is a full member of the European Union, both contributing to, and benefiting considerably from, the Single Market.

Although the Single Market intensified trade between different countries in the European Union, they retained separate national currencies. Initially, closer monetary integration in Europe took the form of a zone of monetary and exchange rate stability, with the Deutsche mark as its anchor. These exchange rate arrangements were put under very considerable pressure by German reunification. But this also gave a political boost to those advocating EMU. In effect, and put simply, a political agreement was reached between France and Germany that France would not object to German reunification, provided that Germany agreed to give up the Deutsche mark in exchange for a new single European currency. A Committee of European Central Bank Governors chaired by the President of the European Commission, Jacques Delors, was set up to decide how EMU should work, if there was the political will to achieve it. The Maastricht Treaty transformed the technical exercise into a political objective, with a deadline set for EMU to begin no later than 1 January 1999.

There was still a question of which countries should be eligible to join. The prevailing view was that EMU would not work unless there was a sufficient degree of economic convergence between the participants, not just at a particular point in time, but sustainably over an indefinite period into the future. An objective way had to be found of measuring economic convergence. That was the origin of the famous Maastricht convergence criteria.

In the event, 11 European countries were judged as qualifying to join EMU at the outset. The UK and Denmark opted out, and Sweden also chose not to join. Greece did not meet the necessary hurdles until 1 January 2001. So EMU currently has 12 participants. It is possible that both Sweden and Denmark will hold referenda in 2003 on joining EMU. And in due course, given the political will, the European Union will be enlarged to include a number of new members, mainly from central and eastern Europe. The European Summit at Laeken last December determined to bring accession negotiations with candidate countries that were ready to a conclusion by the end of this year, so that they could take part as EU members in the European Parliament elections in 2004. The Summit expected that ten candidate countries would be ready. If and when they joined the EU, these countries would be obliged eventually to join EMU, once they had qualified to do so.

It was agreed that Monetary Union should involve the introduction of the euro as a single currency in place of the national legacy currencies (Deutsche marks, French francs and so on). This was partly because a single currency was politically neutral. But there was also a question of credibility. Fixed exchange rates are like locking the door and keeping the key. Replacing national currencies with a single currency is like locking the door and throwing away the key.

You cannot have a single currency without a single monetary policy. And a single monetary policy means a single short-term interest rate set by a single central bank. In the euro area, the central bank is a system, consisting of the European Central Bank, based in Frankfurt, and the national central banks of the participants (the Bundesbank, the Banque de France and so on). Together they form the Eurosystem.

In implementing this single monetary policy over the past three years, there is a widespread consensus that the decisions which the ECB has taken about interest rates, in both directions, have been entirely appropriate, and certainly no-one is in an informed position to second-guess the ECB. But equally, the ECB is well aware of the market's view that the communication of its decisions has not been quite as successful.

The monetary aspects of EMU have never seriously been in dispute. But it has been far harder to agree on what is required on the economic side. By contrast to the US, the EU has only a very small central budget of just over 1% of EU GDP – and I see no-one arguing to increase it. The 12 participants in EMU continue to decide at national level how public money should be spent, and how revenue should be raised to finance expenditure. This creates a risk of 'free riding'. So, recognising this, the authors of the Maastricht Treaty agreed that fiscal policies should be constrained under a Stability and Growth Pact, which is designed to limit national budget deficits to no more than 3% of GDP, save in the most exceptional circumstances. In the case of EMU members, this limit is backed by the threat of fines. As budget deficits vary at different points in the cycle, the 3% limit means aiming to be broadly in budget balance over the cycle as a whole.

There is a consensus that the Pact is essential to make EMU work, to avoid excessive strains being placed on the single monetary policy. But adhering to the Pact is not without its challenges, when economic growth is relatively weak, as at present. And, in a broader sense, the institutional structures and inter-relationships underpinning EMU, including between monetary and fiscal authorities, are still bedding down. This is, I think, almost inevitable, with EMU still in its relatively early stages.

It is possible that the novelty and complexity of these institutional structures underpinning EMU have affected the euro's exchange rate over the past three years, and held back the euro's development as an international reserve currency. For example, some market practitioners argue that it will take time for the European Central Bank to acquire fully the credibility of the Bundesbank. But all sorts of other explanations have also been offered for the comparative weakness of the euro against the dollar since EMU began. Some market practitioners now say that the euro began life at too high a level, though this was not said at the time. Others say that euro-area growth has not matched the market's expectations, even though euro-area growth – now and in prospect - is not as subdued as in the US. Others point to capital outflows from the euro area to the US, because of the high rate of productivity growth it has enjoyed over a long period and its more 'business-friendly' environment. And recently the argument has gained ground that there would not be a sustained recovery in the euro in the foreign exchange market until the euro became a 'complete', rather than just a 'virtual', currency. In fact, the euro's external value did jump, quite sharply, by around two cents on the first day of trading after the New Year, on relief that the launch of the euro notes and coin seemed to be going well. But the euro has since settled back into its recent trading range, below 90 US cents.

**The completion of the euro changeover**

This changeover of course began three years ago with the launch of the euro, legally and in the wholesale markets. From that moment, the exchange rates of the component currencies were locked, and this was therefore by far the most economically significant event. Nevertheless, the completion of the changeover marked the euro's transition from a virtual to a complete currency.

In the Bank of England, we have been monitoring closely the entire changeover process. We predicted that it would be completed successfully. And I am delighted to report that it has been. That could by no means be taken for granted, because of the scale and complexity of the project. It involved the production of 52 billion euro coins, weighing 24 times as much as the Eiffel Tower; and an initial stock of 15 billion euro banknotes which, if placed end-to-end with the legacy banknotes they replace, would cover the distance from earth to the moon ten

times. It involved the prior distribution of over 10 million starter kits of euro coins to retailers, and over 160 million smaller kits for sale to the general public. It involved adapting some 190,000 machines for dispensing cash, 4 million point-of-sale terminals and 7 million vending machines. And it involved converting to euro perhaps 1 billion bank accounts.

Before the cash changeover could begin, the non-cash changeover had to be completed by the end of last year. This affected all aspects of economic activity where currency is involved: the conversion of bank accounts, payments, prices and invoices, and the redenomination of financial contracts. So far as we can tell, this non-cash changeover appears very largely to have been completed on schedule. But it has been interesting to us – as outside observers – that different countries had approached the non-cash changeover in different ways. In some countries, like France, banks were encouraged to convert bank accounts early, from last summer, because of the scale of the task, and to help familiarise the public with the euro. Yet in other countries, like Ireland, the banks agreed that the account changeover would be better at the very end of the year, and that this was technically feasible. Now that the process is over, we will be interested to assess the relative merits of these different approaches and to see if any could be judged more successful than others.

Two other points about the non-cash changeover are worth noting. First, special arrangements have had to be made to enable payments in legacy currency outstanding at the end of last year to continue to be settled this year, for a period which varies from country to country. Second, besides the changeover by the banks, businesses and public administrations also had to change over their own operations. Initially, there were fears that some small businesses and remote public administrations would not be able to complete the changeover in time. But there have not yet been reports of significant problems. At this stage, I think, no news is good news.

The cash changeover began at midnight on New Year's Day. Throughout the euro area, the aim has been to change legacy cash (Deutsche marks, French francs and so on) into euro as quickly as possible, to help minimise costs for banks and retailers, and confusion amongst the public. The changeover was preceded by a major information campaign, obviously concentrated in, but going beyond, the countries immediately affected, to explain the mechanics of the changeover and the features of the new euro banknotes and coin. This was organised by the European Central Bank, national central banks and their governments.

The specific target of governments in the euro area was to change the bulk of cash transactions into euro in just two weeks. In fact, an average proportion of over 50% was achieved by the end of the first week, though the proportion varied between different countries. It had reached an estimated 90% on average at the end of the second week. Almost all cash dispensing machines, which provide the route through which most banknotes enter general circulation, were converted by the end of the first week; and about half the number of vending machines. This is astonishingly quick, to the great credit of all the euro-area authorities, both the ECB and the ministries and other agencies involved.

One of the most encouraging aspects of the changeover has been the willingness of the general public in the euro area to convert their remaining holdings of legacy notes and coin into euro as speedily as possible. In general, this has been achieved without long queues or confusion among the public, though there have - naturally and inevitably - been some exceptions. And where there have been queues, the public has generally been calm and good-humoured.

To ensure that euro cash could be put into circulation on 1 January, sufficient euro banknotes and coin had to be frontloaded to banks and sub-frontloaded to retailers in advance. This was in itself a huge logistical exercise. Frontloading of the banks did not for the most part prove to be a logistical problem, partly because the financial burden on the banks was eased by the ECB delaying payment for the euro cash until this month. So there was a sufficient financial incentive for the banks to participate – and they recognised of course their social duty and central role in the cash changeover. But sub-frontloading to retailers proved more problematic, as the costs and risks of transport and of securing their premises, and the costs of insurance, left retailers with few incentives to receive euro cash until the last minute. In some cases, this left them short of euro cash to give in change early in the New Year, or with no euro at all for a few days.

As a way of helping to speed up the cash changeover, retailers have been encouraged to give change only in euro, whether customers pay for goods in euro or legacy currency. Supermarkets and other large retailers have been able to provide euro in change from the outset. But there has been a shortage of change in some smaller shops, particularly those that had not arranged adequate sub-frontloading. Some members of the public have hoarded euro coins rather than spent them. And despite a big increase in the production of low-denomination euro banknotes during the course of last year, stocks of low-denomination notes have appeared to be inadequate in places. Some have argued that the ECB should have agreed to the prior distribution to the public of starter kits, not just of euro coins, but of euro notes as well, though it is not clear how much difference this would have made in practice.

All countries in the euro area tried to reduce the changeover task during the cash exchange period by encouraging the public to return hoarded legacy coin and high-denomination legacy banknotes early, before the end of last year. These schemes had some success. But many people have kept most of their legacy notes and coin to exchange during the cash exchange period. In particular, some customers have used their remaining holdings of high-denomination legacy banknotes to pay for goods in shops, putting further pressure on shops short of euro change. In addition, some small shopkeepers and waiters not surprisingly have found it hard to calculate change in euro when they have received payment in legacy currency, given the odd and inconvenient conversion rates involved, and the need to serve customers fast to avoid queues. So initially, small shopkeepers and bar-tenders seem to have provided change in the currency in which payment was tendered, whether euro or legacy currency, and operated a two-till policy, rather than giving all change in euro, so as to avoid making mistakes and to conserve their supplies. This is unlikely to have had any material impact on the overall changeover. But retailers have quickly been able to replenish their stocks of cash from the banks, and most had sufficient supplies of euro change in time for the first weekend of shopping and the winter sales.

Another way in which the authorities had hoped to reduce the changeover task during the cash exchange period was to encourage the public to make payments by credit or debit card rather than cash, though – perhaps surprisingly – this was not a prominent feature of the information campaign in most countries. In the event, it appears that cash usage has actually increased since 1 January, because the public has been spending its remaining holdings of legacy banknotes. As a result, in a number of countries, the projected increase in electronic payment transactions does not yet appear to have occurred.

It was always recognised that the cash changeover would involve a number of risks, which the authorities in the euro area have done their best to minimise through careful preparation and

contingency planning. The cash distribution process, which involved transporting and storing securely very large amounts of cash, worked well. The incidence of thefts of cash has in fact been lower than normal, contrary to some fears; and where thefts have occurred, they have generally taken the form of burglaries rather than armed robberies. For a short time, some bank workers took industrial action in France and Italy. But this was not significant enough to disrupt the changeover. Nor was bad weather, despite the first snow over New Year on the Acropolis in Athens for 38 years!

One of the authorities' biggest concerns is the greater than normal risk of criminal activity in the form of counterfeiting and money laundering, given the public's unfamiliarity with euro banknotes and the large amount of cash to be exchanged over a short period. A few faulty €500 notes have been discovered, but these have been the fault of printers (having failed to attach the hologram!) rather than counterfeiters. But, although there is virtually no evidence of euro counterfeits coming to light to date, it is very early days and it would be wrong to be complacent. The public, inside and outside the euro area, must remain vigilant.

The overall judgment must be that none of the teething problems during the cash exchange period detracts from the considerable technical success of the changeover, which is already now very far advanced.

A remaining concern among the public in the euro area is that the changeover will lead to a rise in prices. The ECB and national central banks have done everything they can to allay public concern and, with the appropriate statistical agencies, they are monitoring the situation closely. Although there have been some well documented increases in specific individual prices, the Commission gave a comforting message on 9 January that: "At the moment, there are no signals of generalised price increases which would have a significant or permanent impact on inflation." Indeed, by enhancing competition, the introduction of the euro in cash form should, in the medium term, help to keep prices down. A number of central bank studies certainly suggest that, while there may be temporary upward pressure on prices, in the longer term there should be downward pressure on prices, owing to price transparency and increased competition.

**The UK and EMU**

The changeover in the first wave is significant in the UK in two senses. First of all, we want to learn any lessons from the changeover in the first wave, in case the UK decides to join EMU at a later stage. This is one of the reasons why we in the Bank of England have been monitoring the completion of the changeover closely, and reporting on it in our publication, *Practical Issues Arising From the Euro.* The most recent edition, published last December and available on the Bank's website, discusses the completion of the changeover in the euro area in detail. And in our next edition in the spring, we will assess how the changeover has gone, and identify any lessons which those involved may have learnt for themselves, as well as trying to apply these as far as possible to the UK context.

The other reason why the completion of the changeover in the euro area is important in the UK is because it may have an effect on public opinion. It is clear that, if the changeover had gone badly, this would have had a negative effect on public opinion in the UK, at least in the short term. Instead, the changeover has gone well, but it is still too early to give a considered view of what impact it will have on public opinion. The UK public will increasingly come into contact with the euro during the course of the year. According to some estimates, UK citizens

are expected to make as many as 40 million journeys this year to the Continent of Europe; there is also considerable travel to the UK from the euro area. And businesses in the UK are dealing with the euro all the time, as over half of the UK's external trade is with the euro area.

Public opinion in the UK will play a crucial role, because there will be a Referendum of the British people, if the Government decides to recommend EMU entry. The British Government has already taken the decision in favour of joining, in principle. But in practice, it has made equally clear that entry must be clearly and unambiguously in the UK national economic interest. To enable the Government to reach a decision, the Treasury is committed to making an assessment, by June 2003, of its famous five economic tests. These are: whether there is sustainable economic convergence between the UK and the euro area; whether the UK economy would have sufficient flexibility to adapt; what the impact of UK entry would be on foreign investment; on financial services; and more generally on growth and jobs. These tests are, of course, quite distinct from the Maastricht convergence criteria, which the UK would also have to meet, and would be confident of meeting as well as any first-wave country did in the spring of 1998.

The economics of EMU are not straightforward. There are both considerable potential benefits and equally considerable risks. One of the undoubted benefits of EMU is that the euro helps to establish deeper and more liquid financial markets in Europe. Previously, these were segmented by national currency. Now, instead of 12 different currencies, there is only one single currency; a much bigger financial market-place is being established and, when fully developed and integrated, this will be of benefit to investors and borrowers alike. In the process, Europe's capital markets will become more efficient and the euro more widely used. Perhaps surprisingly to some, the City of London is playing a key role in helping to achieve that goal. Let me come back to this shortly.

There is another – even more fundamental – benefit from EMU. For participants, the introduction of the euro removes nominal exchange rate uncertainty, indefinitely into the future and across a wide economic area. This is a much more important point than the elimination of foreign exchange transaction costs. Nominal exchange rate certainty is naturally attractive to those exporting elsewhere within the euro area, so long as the exchange rate at which their currency has been locked to the euro is appropriate, in the sense of being a broadly sustainable rate. As companies can trade and invest across a wide area without any nominal exchange rate risk, prices become more transparent, transaction costs are lowered, competition is greater and economic resources are allocated more efficiently. Once consumers become familiar with euro notes and coin, and all prices are in the same currency, this effect should become more powerful, including across the internet. So, for example, the prices of BMWs should become broadly the same. There are, of course, limits to this process, as a result of transport costs and differing national regulations, standards, cultures and even the weather (for example, washing machines in the hot, dry countries of southern Europe have much lower spin speeds than in the cold, wet countries of northern Europe). But no-one should be in any doubt that the benefits are very real, and that if they are fully realised a much more dynamic euro-area economy could result.

However, against the benefits of obtaining nominal exchange rate certainty on at least half of the UK's external trade would have to be set the risk of the 'one-size-fits-all' short-term interest rate throughout the euro area. The risk is that this single interest rate may not in practice suit all the participants in EMU all the time: indeed, at any particular point in time, it may not precisely suit any of the participants. They may be at different stages of the economic

cycle, or have divergent fiscal positions; or they may be affected in different ways by 'asymmetric external shocks' – shocks from outside which affect different countries to a different extent, and may require potentially differentiated policy responses.

The Maastricht convergence criteria try to help reduce these risks, by addressing sustainable economic convergence. Divergent regional needs already exist within countries, as well as between them, as we in the UK know only too well. But alternative adjustment mechanisms, like fiscal transfers between rich and poor regions, are better developed within countries than across the euro area as a whole, and – as I mentioned - no-one is arguing to raise the small European Union budget to allow significantly greater transfers. This leads to the, by now conventional, wisdom that, for EMU to work well, the participating economies – current and prospective – need to be made as flexible as possible; and that the highest priority should as a result be attached to supply-side policies to improve the functioning of markets, particularly the labour market. A key time for assessing how well structural reform is going to work across the EU as a whole will be the Barcelona European Summit on 15 and 16 March. For the time being, the jury remains out.

In the UK case, it is virtually indisputable that the balance of these economic arguments came out strongly against participation in EMU at the outset, and that is why the Government stood side from participating in EMU in the first wave. The Government has said that it will make the next assessment by June 2003. Far be it from me, or my colleagues in the Bank, to second-guess what this assessment will conclude. But let me say just two things. First, the economic conditions are obviously important, if the UK is to live comfortably with the 'one-size-fits-all' monetary policy of the euro area: this means genuine sustainable convergence, which is extremely complex to assess and inevitably will involve difficult judgments.

Second, the sterling exchange rate is clearly overvalued, at least against the euro, which helps to explain the great difficulties our internationally exposed, and particularly manufacturing, sectors are facing and the consequential difficulties for monetary policy setting now. Virtually everyone suggests that a lower exchange rate against the euro would be required for entry – indeed this is one of those very few things that almost all economists appear to agree on, even if there is plenty of room for reasonable men (if one can describe economists in this way!) to disagree on the precise margin of overvaluation. Yet if the sterling exchange rate were to fall, or be artificially lowered, through a generalised depreciation in the sterling effective exchange rate, this would be bound to put strong upward pressure on UK inflation, and carry potential implications for UK monetary policy. By contrast, if the euro were to strengthen generally, so that sterling fell back bilaterally against the euro but was unchanged, or even stronger, against the dollar and other currencies, this would have considerably less potential impact on UK inflation. Regrettably, however, any such benign outcome seems to be in the lap of the gods rather than policy makers, in the UK or elsewhere.

The British Government's policy in the meantime is to <u>prepare</u>, in case the UK decides to join. The UK outline National Changeover Plan, published in its second edition, assumes that it would take about four months from a Government decision to organise a Referendum, and in the event of a positive Referendum result, there would then be a period of between 24 and 30 months before the introduction of UK euro cash to replace sterling.

Practical preparations in the UK for possible UK entry have been going on for some time. The Bank of England's own role is to co-ordinate preparations across the financial sector, to the extent that co-ordination is required. Whatever the entry date, the critical point for the City is

how long in advance the preparations would need to start. Wholesale preparations would need to be fully complete and ready for operation by the date of entry. We reckon that, in general, a lead-time of no more than twelve months would be required to implement these preparations, assuming prior planning and market consultation.

It is generally accepted that preparations for the full range of retail financial services in the UK would take longer, and so would not be complete by the entry date. Arguably, this may not matter in practice. The prevailing market view, reflecting experience in the first wave of EMU entrants, is that the retail customer base of financial institutions would probably in any event want to continue to operate in sterling until close to the introduction of UK euro notes and coin. So a phased approach to the changeover is planned, in which financial markets would change to euro immediately on entry, but full provision of retail financial services in euro would be delayed for a period beyond entry.

**The City of London as a euro centre**

The euro has, of course, been widely used in the City of London since its launch three years ago. The City has been in a good position to play a leading role in the development of the euro markets, because it is by a long way the biggest international financial centre in the European time zone. Arguably, this is the biggest contribution we can make to the success of the euro on the ‘outside’.

Let me briefly illustrate the structural developments in capital markets in Europe that have been taking place since the launch of the euro. These are not of course confined to the euro area, but are relevant to all EU countries, and indeed beyond.

First, market trading in the euro has been increasingly integrated across borders, though not yet fully in all market sectors. Overall, the euro market is more liquid and spreads between borrowing and lending rates are generally narrower than before (including as I say in London, so it would be wrong to think of the euro market as synonymous with the euro area).

Second, there has been substantial growth in corporate bond issuance, which had traditionally been much lower in Europe than in the US. Moreover, and there have been some signs of a growing equity culture, and this seems likely to remain intact, despite market volatility experienced in the last two years.

Third, international fund managers have begun to diversify their bond and equity portfolios away from national markets across the euro area as a whole – and even in some cases across the EU – though there may be further to go.

Fourth, from the outset, the plumbing supporting the euro financial markets has worked well, particularly the wholesale payments system, which efficiently links all 15 national systems. But clearing and settlement is much more of a jigsaw puzzle, and further consolidation is required. Whilst the authorities can encourage this process, it is right to leave to the marketplace how it actually occurs.

And finally, regulation. The regulatory environment across the Single European Market needs to keep pace with developments in the euro markets themselves. A great deal has already been achieved. But a number of barriers in the securities markets still need to be removed. Last year, a Committee of Wise Men proposed a process for doing so, and a set of legislative

priorities. We hope that the work of the Wise Men will be followed through quickly. It is an important, but by no means a straightforward, task.

As a result of the positive and constructive contribution that the City of London has made to the development of the euro markets, all the evidence (both data and anecdotal) continues to indicate that, since the launch of the euro, London's position as the dominant international financial centre in the European time zone has remained unchallenged.

One of the reasons that London has continued to thrive as an international financial centre is because of its openness, and the level playing field and balanced regulation we provide for financial institutions of every nationality and foreign investors. Like Wimbledon, we provide the venue, but foreign players often win the tournament. The most recent demonstration of this was the friendly takeover of LIFFE (the London futures exchange) by Euronext, based in Paris, in preference to the London Stock Exchange. No favouritism there! The City of London will act as Euronext's derivatives centre, and LIFFE will continue to be subject to UK regulation. The partnership between LIFFE and Euronext helps both to cement the relationship between the City of London and the euro area, and to bring about the consolidation in Europe's financial infrastructure that is needed to increase its efficiency.

**Conclusion**

So in summary, the introduction of the euro this month in physical, as well as virtual, form has been a considerable technical success, and a great credit to all involved across the euro area. We have been monitoring the changeover very closely in the UK, as we are keen to learn lessons from the experience of the first wave, in case the UK subsequently joins EMU. But the euro also has wider significance in macroeconomic and market terms. The City of London has played a leading role in the structural development of the euro markets. Arguably, that is the most positive and constructive contribution that the UK can make at present on the 'outside'.

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