American University of Central Asia

European Studies

The Economic impact of European Integration

By

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Abstract

Indeed, Europe nowadays not is that one that the history has known for ages. Split by strict territorial borders, nations that constitute eternal enemies, seeking to invade new territories, never ending wars. This Europe is gone into the past. In the new millennium, the history has encompassed one more astonishing and in some way inspiring reconstruction in the west of the Eurasian continent: creation of the first organization that consists of 27 member states with their difference in language, historical background, economic situation, social infrastructure, and…basically, in everything, the EU has proved herself to be inspiring example of integration that can be reached by common consent and efforts, put by each of the included member country.

Admittedly, as benefits of the common currency shared among 17 MS, European Commission points out low inflation rates, which in its turn promotes cheaper government borrowing and social cohesion within the country, improves healthiness of the country's economy before and after the entrance to the euro area, and the single currency makes the country's economy more resistant to external shocks by uniting economies into supranational level. Nevertheless, there is a certain euro skepticism on whether the adoption of the single currency increased economic welfare of the euro area MS. Hence arises question was that so-called deepening of integration beneficial? Have joined countries reached their targets? What kind of impact had joining the Eurozone has had on the economies of the MS?

This paper studies the change in economic situation in countries that are the MS of the euro area and whether they are affected by economic integration of Europe. The main goal is to analyze such economic indicators as Gross Domestic Product per capita, net Foreign Direct Investment, and current account balance of the MS of the Eurozone and evaluate influence of the adoption of the euro on these factors. Moreover, the countries will be divided to three

groups according to their income per capita in order to see whether the countries with low income benefited more or less than the high income group. This resulted in a hypothesis that is going to be tested: *European economic integration had a positive effect on the economies of the Eurozone Member States.*

As a result of the research in this paper, it can be deducted that the euro proved to be a good motivator of inward investment. Exceptionally high surge of foreign direct investment began shortly before EMU both in Eurozone as well as outside of the Eurozone. Inflows fell sharply afterwards though, still the increase in the period after EMU was considerable. Estimates of euro economies appear to support the euro hypothesis: the substantial rise in FDI after EMU that is post-EMU period to a moderate level above pre-EMU trend. These figures indicate that the offsets in current account deficit can be easily complemented by the FDI flows. As for the income growth, there was a radical change in the average GDP per capita growth after the adoption of the single currency.

As for the grouping the countries and connecting the benefits with the low/middle/high income economies, net flows of direct investment increased substantially after the EMU for all of the countries and for low-income countries in particular, though there were imbalances in the trend; the GDP per capita's average growth has increased significantly for all of the country categories, but for high income countries especially; and the current account balance has proved to be dispersed differently by virtue of its trend, but trade surplus is a main trend for the middle income countries during the period of the premonition of adoption of the euro in 1990s. Hence, the hypothesis of this paper that the economic integration of Europe has resulted in positive effect for the economies of the euro areas member states has been partially proved.

Abbreviations

CEEC	Central and Eastern European Country
EC	European Community
ECB	European Central Bank
ECSC	European Coal and Steel Community
Ecu	European currency unit
EMS	European Monetary System
EMU	Economic and Monetary Union
ERM	Exchange Rate Mechanism
ESCB	European System of Central Banks
EU	European Union
FDI	Foreign Direct Investment
GDP	Gross Domestic Product
IMF	International Monetary Fund
OECD	Organization for Economic Cooperation and Development
PPP	Purchasing Power Parity
PPS	Purchasing Power Standard
SEA	Single European Act
SEM	Single European Market
SGP	Stability and Growth Pact
TEU	Treaty on European Union
UNCTAD	United Nations Conference on Trade and Development
WB	World Bank
WEO	World Economic Outlook database

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1. Introduction

Today the power and the influence of any country depend first of all on its economic wellbeing, and after on politics and culture. Therefore such processes as globalization and integration are taking place in the world. At first sight these two processes are merely the same or even one is a part of another. However, globalization is considered as a process of national border elimination thereby creating one whole united world, while integration process is rather different or even contradictory. Regional integration is a process which targets the protection of internal markets, economic growth and high standards of living of members of this process, thereby dividing the world into various groups and regions. Especially, regional integration has gained popularity after the Second World War.

The best brains of Europe came together to build one community, one organization that would make impossible to new wars. Since France and Germany constantly clash with each other, it was efficient to start collaborating on the basis of their peace. Thus, with other four developed countries such as Italy, Belgium, Netherlands and Luxembourg jointly have created community with a supranational body which was to supervise the community. Year after year, the European Coal and Steel Community (ESCS) proved to be promising and prosperous that made other European nations to be eager to join it.

However, more and more the EU became like a big blanket with different pieces that is full of contradictions and divergence that were made up together. Keep on widening, in 2004 enlargement took place as a fourth wave of countries joining EU. Back then face of Europe changed significantly with former communist countries becoming members of EU. Enlargement after enlargement EC/EU grew in sizes and in authority as well. It became an economic giant, united block who plays a great role in international arena. The time for a deepening of the integration that would make the new Member States fully integrate into the EU came.

The Maastricht Treaty enforced appearance of the Economic and Monetary Union in Europe with Single European Market enabling intra EU zone trade. Further on, a single currency has been established. The Economic and Monetary Union is the political and economic base for the euro and supplement for EU single market. The euro is a single currency introduced by the economic integration on January 1st, 1999 as a final stage of the Economic and Monetary Union. It is shared among 17 EU member states, which together make up the euro area or the Eurozone. Protagonists hoped for enormous changes and benefits after adoption of the single currency: the euro would benefit all citizens, businessmen, the euro area member states and the European economy as a whole. In addition, according to the declaration of the Commission, single currency could stabilize exchange rate volatility, thus increase foreign direct investment in the zone. Moreover, as the euro was able to create concurrency to global currency - dollar, then it could increase flow of investment from extra EU zone as well.

Moreover, the euro is one of the “strongest tangible symbols of the common identity and shared values of Europe, European nations and Europeans themselves” as it moved the European integration even further. The main goals that lie behind the creation of the EMU and the euro after all are a better function of the European economies and prosperity of Europeans by creating a stable currency, lowering inflation and interest rates, eliminating currency exchange costs, creating price transparency, integrating financial markets, building a framework for sounder public finances, easing international trade greatly, and giving a stronger representation of the EU in the global economy.[1]

As pros of the single currency at the time of its introduction and promotion European Commission has indicated and continues to point out several benefits that the euro brought to the Europeans and the Eurozone member states. According to the EC, the European economy

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[1] *How the euro benefits us all.* European Commission publication. Nov. 2010. Web. <http://ec.europa.eu/economy_finance/publications/publication9869_en.pdf>

benefit from the euro in terms of deeper financial integration, which makes it possible for investment flow in the area where it is used most efficiently, the euro gives the EU a greater importance in the world arena as now it is the second world currency after the USD, and one currency among the area members supports international trade with least transaction costs as the businesses and deals pay and are paid in the euro.

As for the benefits for the Eurozone Member States, European Commission points out low inflation rates, which in its turn promotes cheaper government borrowing and social cohesion within the country, improves healthiness of the country's economy before and after the entrance to the euro area, and the single currency makes the country's economy more resistant to external shocks by uniting economies into supranational level.

Admittedly, a common currency shared among 17 MS is beneficial to the Europeans as well. As a consumer, European gains in low and stable price, more choice, low inflation and interest rates. Moreover, they can travel easier and cheaper by sparing their budget that usually would go on the exchange costs. As businessmen, Europeans gain in terms of increasing investment, risk spreading, long term planning and bigger market for their products.[2]

Nevertheless, there is a certain euro skepticism on whether the adoption of the single currency increased economic welfare of the euro area MS. Hence arises question was that so-called deepening of integration beneficial? Have joined countries reached their targets? What kind of impact had joining the Eurozone has had on the economies of the MS?

This paper studies the change in economic situation in countries that are the MS of the euro area and whether they are affected by economic integration of Europe. The main goal is to analyze such economic indicators as Gross Domestic Product per capita, net Foreign Direct

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[2] *How the euro benefits us all.* European Commission publication. Nov. 2010. Web. <http://ec.europa.eu/economy_finance/publications/publication9869_en.pdf>

Investment, and current account balance of the MS of the Eurozone and evaluate influence of the adoption of the euro on these factors. Moreover, the countries will be divided to three groups according to their income per capita in order to see whether the countries with low income benefited more or less than the high income group. This resulted in a hypothesis that is going to be tested: *European economic integration had a positive effect on the economies of the Eurozone Member States.*

2. Literature review

After a seminal work of Rose the topic of the impact made by currency unions gained popularity. Mainly these works were about the trade impact of the single currency. Thus, the euro and its effect on the trade became a topic of interest for researches. This empirical literature achieved a conclusion that a creation of a single currency area has a positive impact on trade among the Member States of that area. According to Rose suggestion a currency union even might have increase trade by 200%. [3]

Moreover, such a growing interest made the researches go deeply and not only to reveal the effect of the common currency on FDI flows which in its turn have grown much faster than trade flows. Increasing economic and monetary integration that is the case with the euro affect positively on FDI flows by eliminating uncertainty and riskiness of the trade, promoting stable exchange rates and least transaction costs, which support the expansion of the business within the area. Thus, the currency union can increase trade and investment in the area as well as in the partner countries. Recent researches based on the impact of the single currency on the FDI inflows and outflows are numerous, as the euro gains more and more credibility.

[3] Baldwin, Richard et al. *Study on the Impact of the Euro on Trade and Foreign Direct Investment.* Apr. 2008 Web. <http://ec.europa.eu/economy_finance/publications> Economic Papers 321, May 2008

Wei and Choi examined the effect of a currency union or complete dollarization on US FDI and estimated it as high as 185%.[4] Moreover, Aristotelous estimated that the overall effect of EMU on US FDI inflows of the Eurozone using a panel of 15 EU countries and data for 1966-2003. His main conclusion that the effect of the EMU was positive and significant.[5] Schiavo investigated as well the overall impact of the EMU on FDI flows using data from 25 developed countries for the period 1980-2001. Despite the fact that his data covered only three years of the post-EMU period, generally he concurred that the effect of the EMU was positive.[6]

It was discussed in the research of Barry Eichengreen and Andrea Boltho, for instance, that thanks to the fact that single currency decreased exchange rate volatility it would encourage growth in trade and vice versa.[7] Another studies analyzed that on certain assumptions, the presence of volatile real rate even would increase investment. Nevertheless, a study by Byme and Davis found out that in the long run exchange rate and interest rate volatility negatively related to investment, thus concluding if the EMU would more or less stabilize it then probably investment will increase.

Moreover, if these studies reflect upon the effect of the euro on investment and trade, some studies concluded that a positive change in trade or investment can lead to an economic growth. There are some related questions about the role of the euro based on empirical approach. Henrekson, Thorstensson & Thorstensson examine the role of trade and institutional integration on economic growth, using a purely empirical approach and a crosssectional and pooled OLS study, their study finds that joining the EU or EFTA enhances growth.[8] Crespo-Cuaresma, Ritzberger-Grünwald, and Silgoner (2002) examine the impact of European integration on economic

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[4] Wei, S-J. and C. Choi, 2002, *Currency Blocks and Cross-border Investment*, Unpublished manuscript.
[5] Aristotelous, K., 2005, Do currency unions affect foreign direct investment? Evidence from US FDI flows into the European Union, *Economic Issues*, 10, 1-10.
[6] Schiavo S., 2007, "Common currencies and FDI flows", *Oxford Economic Papers,* 59: 536-560.
[7] Eichengreen, Barry, and Andrea Boltho. *The Economic impact of European integration.* Web. *Sept 20, 2007*
[8] Henrekson, M., J. Thorstensson, and R. Thorstensson. "Growth Effects of European Integration" *European Economic Review* 41, 1997; 1537-57.

growth of current EU members, using a panel regression. They find that the length of EU membership has a significant and positive effect on growth, and it is higher for poorer countries, suggesting an asymmetric impact of EU membership.[9] These studies solely focus on a regression analysis of the relation between membership and growth without providing an underlying theoretical framework or projections for the candidate economies.

This paper attempts to contribute to the literature by exploring the effect the euro has made on FDI flows, GDP per capita and trade balance represented by the current account balance in the context of the European Monetary Union (EMU). In order to prove the hypothesis that the economic integration of the EU, despite the myths had no negative effect on the Member States economy, it will examine what impact had the euro on the FDI flows, GDP per capita and current account balance of the Eurozone MS. There is no much of theoretical works done on this issue. However, there is a lot of empirical work that recently growing as long as the topic becomes more and more popular. The main points are that the positive effect of the euro as a common currency decrease transportation costs and exchange rate and increased price stability and increase trade among the Eurozone MS.

According to the results of the research conducted by Taylor, intra/extra-zone inflows of FDI in Euro-12 has risen gradually in 1980s and early 1990s and rushed forward in late 1990s and in 2000. However, fell back afterwards the next year. It can be related to the fact that the issue with EMU was affirmed and markets were already convinced. Therefore, around 1999 high flows of investment can be observed. Certainly, it fell back shortly after the adoption of euro, nonetheless, the level of FDI still was higher than it was before the euro. Similar situation is with outflows from the Euro-12 gradually augmentation until the late 1990s and upsurge around 1999-2000 and then fell back. High boost around 1999-2000 in both outflows and inflows of Euro-12 occurred. In order to make the euro hypothesis more

[9] Crespo-Cuaresma, J., D. Ritzberger-Grünwald, and M.A. Silgoner. *Growth, Convergence and EU Membership* National Bank of Austria Working Paper No. 62, 2002.

convincing he has focused on the situation before and after the shift to EMU and adoption of the euro. The main conclusions are that the intra-zone FDI nearly quadrupled in real terms between before and after the EMU period. However, the most part of the intra-zone flows happened to and from BLEU that is Belgium, Luxembourg and the European Union. So if we exclude BLEU from the overall result, increase in intra-zone is much smaller but still prevails, about 80%.[10]

The question with the current account balance occurs significantly in relation with again the exchange rate variability. While the early literature on the trade effects of the euro suggests that the abolition of nominal exchange rate volatility has promoted intra-euro area trade, the picture is complicated by the historically high propensity of euro area members to trade amongst each other. In fact, Berger and Nitsch argue that the common currency added little or nothing to the pre-existing trend of increasing trade intensity among euro area member countries.[11] In another set of papers, Ahearne, Schmitz and von Hagen and Schmitz and von Hagen find an increase in the heterogeneity of intra-euro area current account and trade balances since 1999. There is also evidence that the euro area members' bilateral trade balances with other member countries became more dispersed than their extra-area balances; these differences seem to have been on an upward trend already prior to the introduction of the euro.[12] For instance, the European Commission notes that current account dispersion has steadily increased since the early 1990s, reaching an "all-time high" in 2008. Schmitz and von Hagen, for instance, show that the integration of euro area financial markets reached a new level with the introduction of the common currency, paving the way for higher current account and trade imbalances and provide evidence that regulation affecting price and

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[10] Taylor, C. T. 2002. Foreign direct investment and the euro: the first five years. *Cambridge Journal of Economics* 2008, 32, 1–28 Web. <www.cje.oxfordjournals.org>

[11] Berger, Helge, and Volker Nitsch, 2008, "Zooming Out: The Trade Effect of the Euro in Historical Perspective," *Journal of International Money and Finance*, Vol. 28, Issue 8, pp.1244–1260.

[12] Ahearne, Alan, Birgit Schmitz, and Jürgen von Hagen, 2007, "Current Account Imbalances in the Euro Area," *Manuscript*.
Schmitz, Birgit, and Jürgen von Hagen, 2009, "Current Account Imbalances and Financial Integration in the Euro Area," *CEPR Discussion Paper*, No. 7262.

nominal wage flexibility and employment protection influence the adjustment of real exchange rates in the euro area.

3. Methodology

To develop the right research design is to point out the research approach you are using. According to Saunders, Lewis & Thornhill and Bryman & Bell, there are two of them – deductive and inductive.[13] As long as this paper discovers an impact of economic integration on economies of the member states it would be reasonable to conduct field research on it. However, paper is limited in the scope therefore this work examines the economic impact of European integration by testing the hypothesis, developing cause-effect relationship and analyzing the statistical data of relevant factors before and after adoption of the euro, it is preferable to use deductive approach.

Primarily, in order to enrich the knowledge of the subject and be able to elaborate on the core issues of the paper and in order to define the scale of the problem the desk-study method or literature review was used. In order to distinguish the researches that have been already done and to evaluate the relevance of this paper to the actual situation broad range of topics were studied. Moreover, literature review is important in delivering the message and in formulating hypothesis. Using primary and secondary sources of information improves the knowledge of the topic for readers and facilitates the understanding of the significance of the research.

Furthermore and mainly, the method of statistical data analysis was used. It is more relevant to this research for it gives the opportunity to clearly see the difference of the economic situations in the EA-12 countries before and after 1999. Dataset from certain online databases were retrieved and manually compiled by the author. In other words, the statistical

[13] Saunders, M., Lewis P., & Thornhill, A. (2007). *Research methods for business students*. 4th ed. Harlow: Financial Times/Prentice Hall

data, all of which is available online to everyone who has an access to the World Web, were downloaded and interpreted by the author. Note that all of the graphs are elaborated personally by the author using Microsoft Office Excel program.

4. Sampling

The sample period is 1980 till 2007 that is from the beginning of the process of deepening the European economic integration which has finished by introducing the euro to the beginning of the global economic and financial crisis. As the crisis was global and practically the countries throughout the whole world were involved, thus the period after 2007 is more or less unreliable in terms of the impact of the euro in particular. Moreover, the period is long term; for such long term period serves as a solid basis and makes the research more reliable.

Sample countries are those Euro Area-12 MS which has adopted euro in 1999 (plus Greece in 2001). The sample includes only 12 member states because five countries that joined the EA after the sample period that is from 2007. As three years are not sufficient to draw any significant conclusions they were excluded from the period and from the sample countries.

Moreover, in this paper the classification of the countries are based on the economic criteria introduced by the World Bank. Thus, we can differentiate between countries with high, low or middle income per capita. Hence, showing to what extent the benefits of euro are spread according to the level of GDP per capita of the countries.

According to the classification of the World Bank all its member countries can be grouped into four main categories – high income, upper middle income, middle income and low income countries. This classification is based on economic criteria evolved as a result of a new context when in the end of the 1980s bipolar world structure of East-West has changed into multipolar. The GDP per capita underlines the important difference between countries by the purchasing power, the theory stipulates the higher the purchasing power is, the more an economy is developed. However, all Eurozone MS are classified by the WB as high income countries.

Nevertheless, these high income countries had different levels of GDP per capita at the time when they accessed Eurozone. Therefore, in this paper they will be divided into three categories of high income, middle income and low income countries and all of the following steps will be based on this classification.

Incomes below $20000 in 1999 fall under low income economies. Incomes in the range of $20000 to $22000 in 1999 fall under middle income economies. The last group is incomes above $22000 which fall under high income economies. The following table illustrates the GDP per capita in 1999 of the countries based on the 2008 US$ PPP.

Table 1: Average GDP per capita calculated and sorted using Microsoft Excel. Source: the World Bank dataset.

Country Name	**Average GDP per capita during 1980-2007**
Portugal	9695,00
Greece	11397,34
Spain	13820,13
Italy	18569,24
Ireland	20891,12
France	21557,65
Belgium	21725,07
Germany	22365,30
Netherlands	22663,44
Austria	22730,20
Finland	22996,83
Luxembourg	41475,18

According to the classification worked out in this paper, Spain, Portugal, and Greece are considered to be low income per capita countries. Second group is Italy, France, Belgium and Ireland with middle income per capita. The last group of high income per capita economies consists of Finland, Germany, Netherlands, Luxembourg and Austria. Thus, the sample countries are divided into three groups. Significance is to find out whether the euro area was beneficial to countries differently depending on the level of GDP per capita.

5. Data

This paper is based on the official statistics retrieved mainly from the Eurostat – European Commission Statistical office and from different other sources while measuring the factors that the author took as indicators of the economy's growth: net inflows of investment, gross domestic product annual change, net exports' change and a change in their gross national income per capita to analyze the impact of the adoption of euro by member states of the EU. Ideally such statistical approach should be completed by a survey. However, this was out of the scope of the paper.

The data sources as already mentioned are Eurostat, the European Commission's statistical office on which the results for the euro economies are based. It is vital to distinguish flows within Euro-12 that joined the Eurozone simultaneously in 1999 that is intra-zone, from flows to and from the countries that are not a member of the Eurozone that is extra-zone. The definitions and key terms are based on the official Eurostat and IMF descriptions.

Another set of data used is the FDI database compiled by the OECD in which the importance is to view the effect of trade partners on the euro economies. This database generally is wider and much longer than the Eurostat's, nevertheless gaps such as data for

smaller EU countries remain. Moreover, the supplemental dataset is from UNCTAD's *World Investment Report* which is available online as well.

European Central Bank statistics was also used as a source of the dataset. This source was a basis for a calculation of a current account balance, for which the data has been given monthly since 1999. Another set of data on GDP and GNI per capita has been retrieved from the World Bank databank.

It is worth to note that though the data was downloaded from these sources, the author has grouped the euro economies out of them and graphed what was necessary using Microsoft Excel program.

6. Economic integration of Europe

6. 1. The role of the Economic and Monetary Union

Instabilities in the currency exchange rates and huge losses in the 1970-80s had pushed the European governments engaged in political integration to move the integration forward. In other words, whenever there was a crisis Europeans became more and more integrated. This is not an implication of any kind of law, just an observation how far the European integration has moved facing challenging times. Nonetheless, united Europe is not only promising island of if not luxury then at least welfare for underdeveloped European countries and further development of rich ones, but also a tie which binds every EU member state to encounter challenges together and to overcome problems even if it's related only to one member of the Union.

The global economic and financial crisis of the last decade has shown the shortcomings of the European Union's monetary and fiscal policies. Therefore, the popularity of euro undergone drastically and the theme of whether the European integration brings welfare or misery for its members arose frequently everywhere in the world. According to the

statistics provided by Economists for alternative measures in Euro memorandum 2009/2010, the critical situation in Greece and Ireland provoked decrease in the overall accounts of the EU. Moreover, in 2010 there still might be excess in budget deficits over 5%.[14] Crisis in Greece is used to be associated with instability and weakness of the common currency of the Union. To put it in other way, the future of the Euro – the symbol of the successful European integration – was put under threat. Nevertheless, the EU in France and Germany heads affirmed their strong determination not only to facilitate the recovery of Greece and Ireland in such harsh times, but also to maintain the Euro as a single currency in the EU. They have declared their commitment to the integration progress as well.[15]

Coming back to the beginning why this integration was so successful, what factors helped in building such strong ties that bound so different countries into one, can this example recur in the world? Such questions and this is not the only questions that have arisen before researchers, professors, students and the whole world. Several ideas and numbers of explanation of the success of the European integration were published. However, though various stages of integration were explained, it comprised only a little part of the whole picture. In other words, there was always something left out. Theories of integration, and there are plenty of them, mostly were trying to explain, while following the integration in reality. That is, theoretic were trying to impose practice, that we can observe in reality, to the theory that have been afterwards written. They tried to interpret in their own way, based on their own ideological and political preferences.

However, that doesn't mean that theories do not require specific attention. Indeed, without theories and theoretic people would be unable to illustrate the steps and phases of the integration on their own, theories were different though. Moreover, various theories open wide perspectives in understanding the subject. By common efforts and analysis theories let to

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[14] *Europe in crisis*. Euromemorandum 2009/2010. Pp.8 Retrieved in 25.12.2010 <http://www2.euromemorandum.eu/uploads/en_euromemorandum_2009_2010.pdf>

[15] *Sarkozy. Franciya i Germaniya nikogda ne otkajutsya ot evro*. Retrieved in 28.12.2010 < http://www.dw-world.de/dw/article/0,,14799975,00.html>

clearly differentiate the basic points, a stone thrown into the water, and the rest, just a wave that it caused. The sources of 'inspiration' for theoretic were mainly their ideological beliefs and commitments.

According to the neo-functionalists, after the establishment of the single market based on the spillover effect the EMU can be shown as one of the necessities. As European Single Market has encompassed all the member states at the time it required stability in the exchange rates or at least little volatility, common monetary and fiscal policies of the EU-15 countries have to be coordinated so that there would be no transaction costs, high risk regarding exchange rate volatility, unexpected devaluations, and deficit in the balance of payments that would make nation states limit foreign trade, relative weakness of national currencies towards USD, and all of this put the necessity to build a mechanism which would even more facilitate free movement of goods, labor, capital and people. Moreover, it would deepen the integration economically, for the integration till that time was mostly about politics. In the end crisis of the systems-stabilizers the situation in the financial markets in aggregate drive the process to create the EMU.

The road to EMU was quite long, approximately four decades. Each decade corresponds to each phase towards the creation of the Economic and Monetary Union and the introduction of the Euro. Phase one from 1957 to 1970 includes the Treaty of Rome and the Werner Report. Second phase, from 1970 to 1979, moves further from the Werner Report to the European Monetary System. In the third phase from 1979 to 1991 or from the start of the EMS to Maastricht had been produced Delors Report. And the final phase, the fourth from 1991 to 2002, from Maastricht to the euro and the euro area.[16]

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[16] Europe. Glossary. *Economic and Monetary Union*. 20 Feb. 2009
<http://europa.eu/scadplus/glossary/economic_monetary_union_en.htm >

6.2. The road to the Economic and Monetary Union

Since the Treaty of Rome issues such as currency systems, volatility costs, etc. weren't covered. More or less one of the reasons was the reliability of the Bretton-Woods system and stability of USD attached to gold. All has started when Bretton-Woods system that was formed immediately after the Second World War faced challenges and USD proved to be weak. Taking into account this troubling background the high-level group led by the Prime Minister of Luxembourg at the time, Pierre Werner were empowered to report on how EMU could be achieved by 1980. Werner plan was to be achieved in three stages in ten years. However, the wave of the oil crisis changed the political direction of the EU. They decided to postpone the Report and concentrate on the problem with the currency fluctuations. In order to cope with them following system of 'snake' was created. 'Snake' was the relative volatility of currencies of European states through 'tunnel' – dollar. Still, it couldn't improve situation as it was weak as the dollar at the time. New phase in development was in 1979, when despite any crisis the European Monetary System had been found. The EMS excelled in coordinating the monetary policies between member states and served stable for more than a decade. Soon after discussions it was determined to launch a new plan. European Commission President at the time Jacques Delors with the group of the bank governors from the members set up "Delors Report". During the period of 1990 to 1999 the grounds were to be prepared for the Euro area and the Euro launched. Thus, the goal was to be achieved in three stages:

I. First stage (July 1st, 1990 – December 31st, 1993): completing the internal market through free movement of capital, closer coordination of economic policies and closer cooperation between central banks

II. Second stage (January 1st, 1994 – December 31st, 1998): establishment of the European Monetary Institute, achievement of the economic convergence, and in 1998 establishment of the European Central Bank

III. Third stage (from January 1st, 1999): fixing exchange rates and launching the single currency, and in 2002 introduction of euro coins and banknotes. [17]

6.3. Convergence criteria and the Stability and Growth Pact

One of the main consequences of the EMU was the establishment of the Stability and Growth Pact (SGP). Its main purpose is to enforce in the countries that have entered the EMU and especially those that have adopted the euro, a clear set of economic measures to prevent their governments from maintaining loose fiscal policies at the expense of other euro-area countries. The SGP should be respected by all EMU countries, but the main addressees are the countries that have adopted the euro.[18]

The SGP promotes healthy economical environment in the countries complying with it. The requirements of the Pact are: an annual government deficit no higher than 3% of GDP and a gross government debt to GDP lower than 60%.[19] Those countries which fulfill these requirements are able in the case of negative shock easily and quickly respond to it. However, one of the main criticisms of the SGP was that it was insufficiently flexible. Especially, it proved to be that way with such countries as France and Germany, who were the main pro-SGP countries at the time. Therefore the EU Council loosened the fiscal rules, in order to make the pact more enforceable and flexible.[20]

Basic points concerning the EMU was fully covered in Maastricht Treaty, where legal framework for creation and functioning of EMU, institutional framework of the union, stages of the EMU, four convergence criteria were formed, priorities for common monetary and fiscal policies were set. Those criteria were introduced with the purpose of sustaining the

[17] Europa. Glossary. *Economic and Monetary Union*. 20 Feb. 2009 <http://europa.eu/scadplus/glossary/economic_monetary_union_en.htm >

[18] European Commission for Economic and Monetary affairs. *The Stability and Growth Pact.* http://europa.eu.int/comm/economy_finance/about/activities/sgp/sgp_en.htm

[19] Ibid. *The Stability and Growth Pact.*

[20] Katinka Barysch. *A Pact for Stability and Growth.* The CER Website. October 2003. The Centre for European Reforms. 6 October 2005. http://www.cer.org.uk/pdf/policybrief_stabilityandgrowth_oct03.pdf

stability even taking into account the "fresh" members, and to maintain the convergence among them. They are:

1. Inflation rate should be no more than 1.5 percentage points higher than the three lowest inflation rates in the European Union.
2. The ratio of the government deficit to gross domestic product must not exceed 3% and the ratio of government debt to gross domestic product must not exceed 60%. Even if it cannot be made due to some specific reasons it should closer to these numbers.
3. Country should join the exchange rate mechanism under the European Monetary System and should not devaluate its currency during the two consecutive years.
4. The nominal long term interest rate should be no more than two percentage points higher than in the three lowest inflation member states. [21]

Basically, these are four criteria so called "the convergence criteria" that are to be met by the country who wish to be a part of the Euro area and adopt the euro. Further on, priorities set were fighting inflation and maintaining price stability. Only on the condition of approaching to the inflation level, long-term interest rates, healthy state finances, lowering budget deficit and decreasing state debt it would be possible to keep common monetary-fiscal system stable.

Being a member of common monetary system means to give up on some issues of monetary and fiscal policies to the institution that is in charge: the European Central Bank. In turn, ECB is the head of the European System of Central Banks that are the national banks of member states. As for the MS who joined, since the very creation 11 member states automatically withdrew from their national currencies towards the euro, later Greece was to join as soon as it met convergence criteria. Three eligible countries decided to opt out: UK,

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[21] Europa. Glossary. *Convergence criteria*. 20 Feb. 2009 <http://europa.eu/scadplus/glossary/convergence_criteria_en.htm>

Denmark and Sweden, thus the rest made up the Eurozone. Those countries formed so-called "euro area".

7. The Euro area

7.1. What is the Eurozone?

"Eurozone is a geographic and economic region that consists of all the European Union countries that have fully incorporated the euro as their national currency; also referred to as "euroland"."[22] In other words, it is the area with European Union member countries who share single currency. 368.2 million EU citizens accept euro as their own *national* currency. As this an enormous quantity it is a huge process to regulate, thus convergence criteria are the tools that facilitate the supervision and maintenance of the stability in the area. It is over 10 years that euro has been adopted. Since the creation in 1999, the Eurozone enlarged and now it is already 17 MS: 1999, Austria, Belgium, Finland, France, Germany, Ireland, Italy, Luxembourg, The Netherlands, Portugal and Spain adopt the euro as their official currency. In 2001 Greece has joined, following years after the fifth enlargement in 2007 Slovenia becomes the 13th member of the Eurozone. In 2008 Cyprus and Malta join the area. In 2009 Slovakia and in 2011 Estonia adopted the euro.[23]

Since the Maastricht treaty was ratified, it is compulsory to become a member of the Eurozone in order to join the EU. Namely at the Maastricht treaty, that the Convergence criteria are indicated. According to the rules of the accession into the Eurozone, the MS that is to join the area should at least 2 years work on the framework of the EU mechanism and address the problems arisen because of inflation, exchange rate volatility and discount rates, till its economy is ready to adhere to the Eurozone. Furthermore, the MS should pay attention

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[22]Eurozone Definition. *Investopedia.* < http://www.investopedia.com/terms/e/eurozone.asp>
[23] Euro Timeline 1990-2011. *The German Way and More: Language and Culture in Germany, Austria and Switzerland.* Web. <http://www.german-way.com/euro-timeline_2.html>

to the criteria mentioned above: budget deficit shouldn't exceed 3% of GDP; government debt should be minimum 60% of GDP. In the case, the MS has fulfilled all the above-mentioned requirements; it is capable to join the area without distorting its stability.

Principally all EU countries have committed to adopt the euro except Sweden, Denmark and the United Kingdom, which have opt-outs. As for the new MS they are already on the path to the euro, four are already members of the Eurozone: Slovenia, Cyprus, Malta and Slovakia, while others expected to join in the next few years. The countries of the last enlargement are still fighting with inflation rates in order to fulfill the compulsory conditions to join the euro area.

7.2. Present situation of the Eurozone

As for the countries that accessed with the first wave, for instance, Ireland due to the size of its economy crisis times hurt it badly. However, Ireland has greatly improved since the accession to the European Union. In far 1950s during the post war period the economy of Ireland was devastating, unemployment had so high levels that the citizens had to move away in order to at least find a job, emigration has grown and the population was 2.8 million. The only country where or in other words put it only market where they could trade was UK. Even though the other spheres of the economy were quite developed one of the main sources of money making was the sphere of the agriculture. The country was firmly planning to transform its market to free market economy and to apply for the European Economic Community which was performing mainly well. At last in 1973 Ireland along with UK and Denmark became a member of the EEC. EEC membership brought them a Common Agricultural Policy with its market opening to 8 countries. The opening of continental markets enabled Ireland to develop further its economy, not only in terms of agricultural products but industrially produced as well. Such an economic growth made the citizens who left their country in search of job return, immigration of Irish workers boosted.

As abovementioned Ireland was still very dependent economically and politically on the UK in 1970s until it became a part of the EEC. Actually, it was really linked to British sterling. Thus, when British currency was experiencing high inflation and price instability it was a real threat for Irish economy. Hence, the Irish membership in the European Monetary System meant to establish more or less certainty in the economic issues. Even though the creation of the EMS was followed by currency instability crisis, thanks to the membership in the EMS Ireland was able to recover afterwards. Inflation fell below 5% in the mid 1980s and short-term interest rates fell lower than in the UK. In the late 1980s full Economic and Monetary Union was to be completed, to be supplemented by new treaty though. According to the poll results the Treaty of Maastricht had support of almost 70% Irish voters.[24] Now Ireland along with 16 EU countries involved in the Eurozone enjoy single currency. In its turn this single currency, as this paper examines, influence significantly on investment flows in the euro area.

7.3. Future prospects of the Eurozone

Creation of the Eurozone plays an important role in the international arena, as the population living in the area makes 5% of the world population, just for comparison, population of the USA comprises 4.6%. But the share of the world GDP in the area is 23,4%, while the USA has 26.9%.[25] Moreover, as the economy is more open than that of the USA the share of it in the world trade relatively surpass that of the USA. In future the countries of the last enlargement are preparing to join the euro area, thus even more increasing the international role of the Eurozone.

Lithuania, one of the ten 2004-enlargement countries had been planning to join Eurozone. However, it wasn't accepted by EU because of its inflation rate which was above

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[24] European Commission.: The EU in Ireland. *Impact of EU membership on Ireland.* Nov. 2010. Web. <http://ec.europa.eu/ireland/ireland_in_the_eu/impact_of_membership_on_ireland/index1_en.htm>

[25] European Commission. *Economic Portrait of the European Union* 2001. – Luxembourg, 2001

0.1%. Neither do Poland, Hungary and Czech Republic, who had problems with high level inflation. The level of inflation in Czech Republic, Hungary and Poland is increasing: 2.3%, 2.9%, and 2.4% respectively.[26] Poland stand as one of the euro “outs” and basically is very anxious about the situation with euro. Simply those MS didn’t pass the criteria. Slovenia as well faced a failure with a stable inflation, though it did access the Eurozone. It had problems with inflation rate which was three times higher than that of acceptable level. Eventually, Slovakia is one of the last countries which have been accepted to Eurozone, as it met the requirements.

Initially part of Czechoslovakia, Slovakia had been separated from it in 1993. In order to recover quickly government implemented market reforms and in 1998 it already had well working market economy. In 2004 Slovakia became a member of the European Union, not long after in 2007 it entered into Schengen agreement and eventually the Euro area. Country was quite successful thanks to it well organized taxation politics, liberalization of financial mechanisms, reforms in trade and health systems. Having high growth rates and relatively low government debt Slovakia successfully kept the level of inflation under 3.2%. In 2007 Slovakia was second in growth rates after Luxembourg. In 2008 GDP growth was 10% which is one of the highest in Europe. The GDP of Slovakia grew four times since the beginning of the decade: from 4 thousand dollars in 2001 to 18.5 thousand dollars in 2008.[27]

It is yet early to talk about the adhesion of the countries of the last enlargement in the sooner future. However, attempts are being made and basically, they are catching other MS easily and quickly. Moreover, these countries have great incentives to join the area as it implies about the market of a greater size, and as the euro is already one of the leading international currencies in the world after the USD.

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[26] *Slovatskij Oazis.* Chastnyi Korrespondent. Feb. 2011. Web. <http://www.chaskor.ru/article/slovatskij_oazis_9203>

[27] *Stat’i.* Mar. 2011. Web. <http://veuropu.ru/index.php?id_menu=6&PHPSESSID=685dc9b322f2966f4b9b228776c26f28>

8. The major findings: The euro's impact

So far, the precedent chapters of the paper have presented historical background, meaning, and timing of Economic Monetary Union have revealed the direct and indirect advantages, risks and disadvantages, the convergence criteria, the Stability and Growth Pact, the institutions that are in charge of setting the interest and exchange rates. However, the question still remains open how the euro impact the economies of the MS of the Eurozone.

In order to analyze the impact of the euro it is necessary to look at the prospect of whether the euro is weak or strong, stable or unstable and whether it can overtake the supremacy of the US dollar as the economic growth of the country depends on the strength of the currency.[28] When the euro depreciates relative to, let's say, US dollar the Eurozone members' export increases. It is even possible that the Euro area cheap products exported to non-Eurozone countries will tend to price out other producers. However, if the euro depreciates too much, this will create inflation within the Eurozone and thus destabilizing economic environment.

Alternatively, if the euro appreciates relative to other currencies becoming strong, Eurozone imports from other countries increase thus spurring production of the region's main trading partners. In order to know whether the euro is weak or strong relative to the other currencies specific factors are determined. These include stable economic and political environment, the current account balance, inflation and interest rates and the euro's use as an international reserve currency.

As monetary and fiscal policies are both conducted by the European Central Bank it makes it possible to fight inflation effectively. Moreover, in fact not the countries but the

[28] Helmut Frisch, The Euro and Its Consequences: What Makes a Currency Strong?, *Atlantic Economic Journal*, Vol.31, No. 1, (March 03).

ECB set exchange rates and interest rates that should be compatible for all. Since the establishment of the euro in January 1999, ECB keeps the interest rates relatively low, thus adhering to the policy of low interest rates, low inflation.

Stable economic environment lead to the high rates of investments, as the fear of the budgetary problems, political discord or high level of unemployment (19% in Spain, 13% in Finland, 12% in Italy and 11% in the Eurozone as a whole) brings uncertainty and leakages or stoppage of foreign investments. However, the early years of the existence of the monetary union have conceived the long term stability and reliability of the Eurozone.

Another determinant of the weakness and strength of the single currency is current account balance. If the country consumes more than it producers, in other words if it imports more than its export the country runs into the current account deficit. This in its turn pushes the country to borrow from other countries, and creates long-term instability.

8.1. Euro's impact on net FDI flows and stocks

Theoretically, with the creation of the single currency among MS of the Euro area, the costs such as the exchange rate cost and transaction costs ceased to zero in intra Eurozone region. In measuring whether the euro impacted positively on the economy first of all we should look at the factors that have changed after the adoption of the single currency. One of such factor is foreign direct investment, according to the definition given by the International Monetary Fund: "Foreign direct investment (FDI) is the category of international investment made by an entity resident in one economy (direct investor) to acquire a lasting interest in an enterprise operating in another economy (direct investment enterprise). The lasting interest is deemed to exist if the direct investor acquires at least 10% of the voting power of the direct investment enterprise."[29] In other words, FDI is a situation when a firm creates, acquires or

[29] IMF, 1993; OECD, 2008

extends a controlling interest in a foreign firm, whether a subsidiary, branch or associated company.

The FDI effects of the euro are much less researched as the euro's effect on trade. It can be possible explained by underdevelopment of the data and empirical methodology. FDI can be distinguished and defined by two main key elements. First, FDI is an investment made by a citizen of one country, in other words a representative of one economy makes an investment in another economy. Moreover, it is of a lasting interest, meaning that this is a long-term nature investment. Second, *direct investor* has a significant degree of influence on the management of the enterprise. For operational purposes it is stipulated that it should be 10 percent of the voting shares thus keeping an investment interest.[30] This 10 percent is here to serve as limit in order to improve international comparability.

According to Reddaway, FDI is beneficial to both sides for host as well as for investing party. Even though the later studies argued that it was too optimistic, there still two motivators due to which investors are interested in making FDI. Ownership and location advantages make it profitable to investors put their money in particular zone. Ownership advantages is more profitable as specific assets are costly to produce rather than just transfer across a national borders, such as know-how, brand names, etc. Location advantages mean factors that make it less costly to produce abroad rather than in home country, such as transportation costs, lower foreign labor force, size of the markets, etc. In other words, the main benefits that create impetus to invest is the advantages of internationalizing the company by not only producing for export but producing in host country that would ease transportation costs and keep technical know-how from selling to another firm.[31]

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[30] IMF, 1993, paragraph 362; OECD, 2008, paragraph 117

[31] Reddaway, W. B., Perkins, J. O. N., Potter, S. J. and Taylor, C. T. 1968. *Effects of UK Direct Investment Overseas: Final Report,* University of Cambridge Department of Applied Economics, Occasional Paper 15, Cambridge, Cambridge University Press

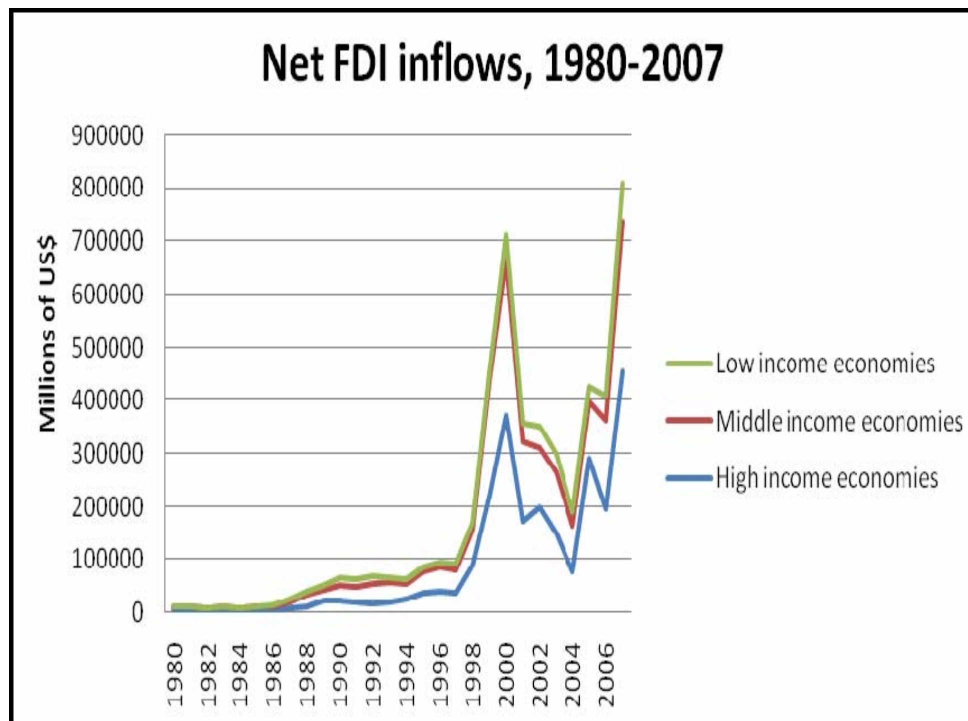

Figure 1: Net inflows of foreign direct investment of the Euro-12 during 1980-2007
Note: The data used for this graph was provided by the World Bank (www.data.worldbank.org) and graphed by the author using Microsoft Excel

As the Figure 1 presents from 1980 to 1988 net FDI flows are relatively low which is unique for all three categories of countries. Beginning from early 1990s there is a gradual tendency of augment. Eventually in 1999 there is a high upsurge with a peak in 2000. However, after there is a fall for several points which continued till 2004 and then again boost forward. Nevertheless, after-EMU trend is pretty much higher than it was pre-EMU. In particular, figure represents a trend that a group of countries as are classified in this paper as low-income economies has gained more than that of high-income economies. This can be explained by the fact that the high-income countries not only receivers of the investment, but also huge investors in their turn. As for the low-income economies they more get than give, thus the whole situation results in high net FDI in low-income countries in particular.

According to the data retrieved from Eurostat FDI flows into the Eurozone significantly increased after the creation of the EMU. This can be traced back to the economic benefits of the EMU. Lynch, P. et al note that the euro will abolish the exchange rate uncertainty thus improving intra-EU trade and investment. Except this the reduction in the transaction costs on cross-border trade and the last but not the least, the greater price transparency along with the stable and low inflation will inevitably influence on the trade between the member countries of the area.[32]

Moreover, this increase in FDI inflows can result in the expansion of trade. As the increase in integration can lead to a dissemination of technology, Pelkmans believes that FDI serves as an important channel for the transfer of know-how and resources which is economically beneficial for less developed regions. [33] Thus, FDI can increase organizational expertise, fuel product innovation, and in general can serve as a catalyst of organizational improvements. In addition to FDI, multinational enterprises (MNEs) play an important role in developing and transferring technological progress among countries. As a result we can say that indirectly low income economies enjoy positive spillover effects from an increase in net FDI inflows.

8.2. Current account balance of the MS of the Euro area 1980-2007

One interpretation of the evolution of current account balances under EMU is that the increased dispersion of current account positions has been driven by trade flows that reflect shifts in relative competitiveness within the euro area.[34] To a considerable extent, the current account balance is strongly related to the FDI flows as the current account deficits can be financed by foreign direct investment. However, current account deficits of more than 8

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[32] Lynch, P., Neuwahl, N., and Wyn Rees, G. *Reforming the European Union - from Maastricht to Amsterdam.* L.: Pearson Education limited, 2000. Print.

[33] Pelkmans, J. (2006). *European integration: methods and economic analysis*. 3rd ed. Financial Times: Prentice Hall

[34] Blanchard, Olivier, and Francesco Giavazzi (2002), "Current Account Deficits in the Euro Area: The End of the Feldstein-Horioka Puzzle?" *Brookings Papers on Economic Activity* 2002:2, 147-186

percent of GDP accumulate to the net international investment position. Thus, net external liabilities can soar the GDP growth.

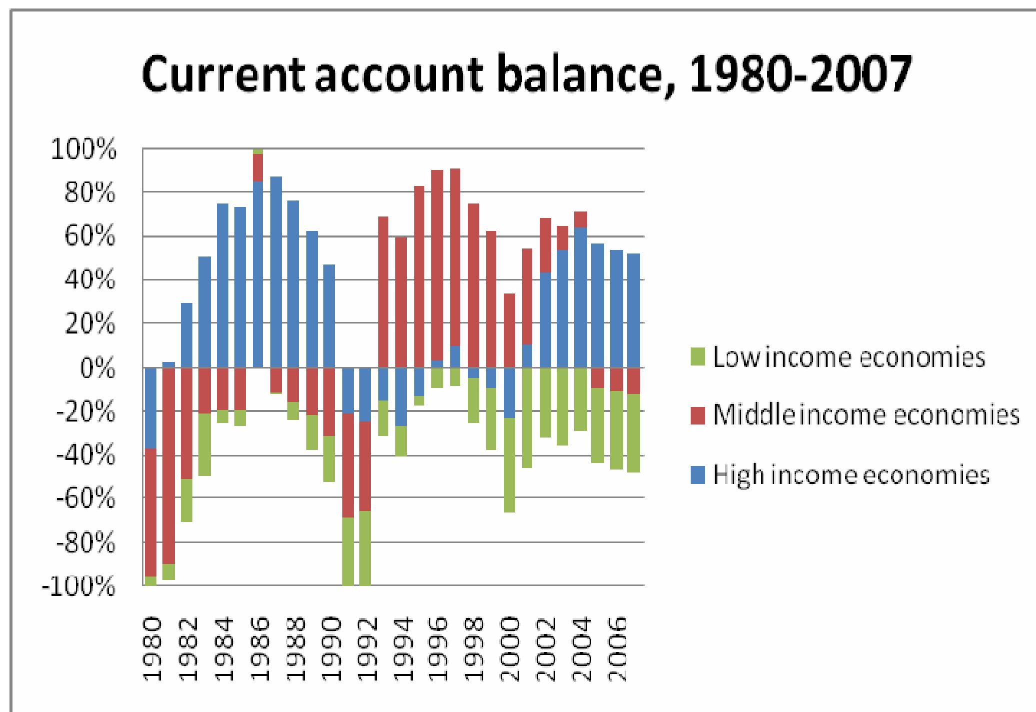

Figure 2: Current account balance of the Euro-12 during 1980-2007 as a % of GDP
Note: The data used for this graph was provided by the International Monetary Fund, World Economic Outlook Database and graphed by the author using Microsoft Excel

Figure 2 shows the evolution of current account balances before and after the adoption of the euro. The group of high income countries consisting of Austria, Luxembourg, Finland, the Netherlands, and Germany, that consistently ran surpluses during the period before the creation of EMU and during the period from 2001 till 2007. Germany registered small current account deficits averaging about 1 percent of GDP during most of the 1990s. The German balance swung into surplus in 2002 and the surplus has widened steadily over recent years as German exports have outpaced imports.

At the other end of the spectrum, Greece, Portugal, and Spain have consistently run current account deficits in the past years, and their deficits have widened significantly under EMU and during the period in the run-up to EMU. All three countries had current account positions close to balance around the mid-1990s. Recent years have seen an especially sharp

decline in Spain's current account balance from roughly 3½ percent of GDP in 2003 to an estimated 8¼ percent of GDP in 2006. Current account deficits of the magnitudes seen in Greece, Portugal, and Spain at present are unprecedented among euro area countries, with the exception of Ireland in the mid-1980s and Portugal in the 1970s.[35]

8.3. Euro's impact on GDP per capita of the MS of the Euro area

As it was mentioned before, economic integration of the MS generates number of benefits for its member countries. According to theories presented in the paper economically integrated countries (especially less developed ones) enjoy positive spillover effects from other members. One of these effects is increased income growth. In this connection, analysis based on the economic performance of the euro area countries over the period from 1980 to 2007 has revealed that even though some of the results are not significant, in general data shows that European Union countries tend to grow fast.

According to the definition of the Eurostat office, "Gross domestic product (GDP) is a measure for the economic activity. It is defined as the value of all goods and services produced less the value of any goods or services used in their creation."[36] The volume index of GDP per capita in Purchasing Power Standards (PPS) is expressed in relation to the European Union (EU-27) average set to equal 100. Basic figures are expressed in PPS, i.e. a common currency that eliminates the differences in price levels between countries allowing meaningful volume comparisons of GDP between countries. The index, calculated from PPS figures and expressed with respect to EU27 = 100, is intended for cross-country comparisons rather than for temporal comparisons.

[35] European Commission (2006) *Quarterly Report on the Euro Area* DGECFIN, IV/2006.
[36] GDP per capita in PPS. <http://epp.eurostat.ec.europa.eu/portal/page/portal/help/user_support>

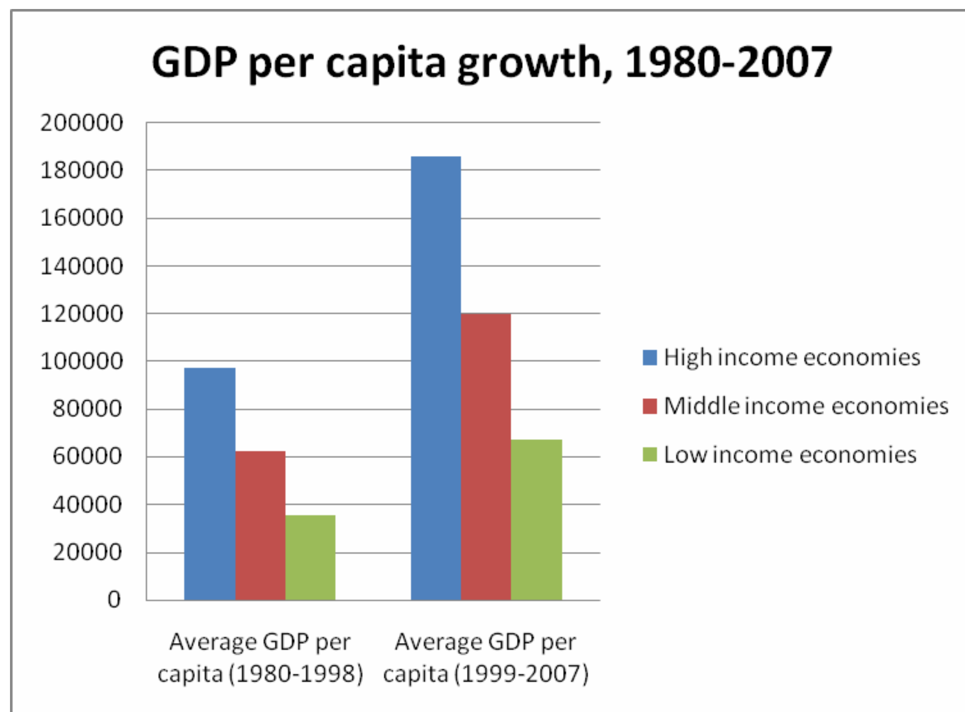

Figure 3: Average GDP per capita growth in 1980-2007 in Euro-12 divided into three categories
Note: The data was retrieved from IMF WEO 2009

As Figure 3 shows that average GPD per capita growth of the Euro-12 countries has increased significantly after they have entered Eurozone in 1999. From figure 3 it is reasonable to argue that the adhesion to the Eurozone has been at least one of the factors that have contributed to economic growth of low income countries after 1999. One of the reasons for the increased economic growth of Euro-12 countries related to their entry into the Eurozone is inflow of foreign investment. As Schadler et al. state that capital has provided a substantial contribution to economic growth of Central and Eastern European countries since among them the range of investment has been large: "foreign savings have played a key role in several countries".[37] This is applicable not only to the CEE countries but also, as we can draw an invisible line between the level of growth of FDI and the income growth.

[37] Schadler, S., Mody, A., Abiad, A., & Leigh, D. (2006). *Growth in the Central and Eastern European Countries of the European Union*. International Monetary Fund

9. Conclusion

EMU represents a great success story of the European integration. Even though it is best described as one of the major steps towards deeper integration, it is best understood as one of the components that were necessary in order to push forward the political integration across the European Union. The euro as a project undermined by creation EMU has four core economic benefits that are direct and uncontentious: reduction of transaction costs, elimination of exchange rate risk, increased price transparency, and creation of deep financial markets.[38] Other indirect benefits include macroeconomic stability, lower interest rates, fundamental structural reform, the creation of a new global reserve currency, and increase economic growth. These benefits result in increase of the net flow of investment, income growth and current account imbalances.

As a result of the research in this paper, it can be deducted that the euro proved to be a good motivator of inward investment. Exceptionally high surge of foreign direct investment began shortly before EMU both in Eurozone as well as outside of the Eurozone. Inflows fell sharply afterwards though, still the increase in the period after EMU was considerable. Estimates of euro economies appear to support the euro hypothesis: the substantial rise in FDI after EMU that is post-EMU period to a moderate level above pre-EMU trend. These figures indicate that the offsets in current account deficit can be easily complemented by the FDI flows. As for the income growth, there was a radical change in the average GDP per capita growth after the adoption of the single currency.

As for the grouping the countries and connecting the benefits with the low/middle/high income economies, net flows of direct investment increased substantially after the EMU for all of the countries and for low-income countries in particular, though there were imbalances

[38] Chabot, Christian N. *Understanding the Euro: The Clear and Concise Guide to the New Trans-European Economy.* NY: McGraw-Hill. 1999. Print.

in the trend; the GDP per capita's average growth has increased significantly for all of the country categories, but for high income countries especially; and the current account balance has proved to be dispersed differently by virtue of its trend, but trade surplus is a main trend for the middle income countries during the period of the premonition of adoption of the euro in 1990s.

Hence, the hypothesis of this paper that the economic integration of Europe has resulted in positive effect for the economies of the euro areas member states has been partially proved.

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