Introduction to the symposium

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The adoption of the euro is likely to be the most important and, probably, the most difficult economic policy decision the new EU member states will have to make this decade. It will be a decision that will have strong implications for economic policy formulation and will necessitate sizeable economic adjustments in the coming period. Although, according to the *acquis*, new member states will have to formulate their policies with the aim of adopting the euro, the decision on timing still remains mostly theirs. In making their decision, they will have to carefully weigh the size of the adjustment they will have to make to meet the Maastricht criteria for euro adoption. The first set of papers in this special issue concentrates on the issues that will have to be considered when the decision on the timing of euro adoption is made, while the second part analyses these issues from the viewpoint of the new member states.

The first set of papers focuses on the Balassa–Samuelson effect, and the issue of whether the new EU member states form an optimum currency area with the euro area. If the Balassa–Samuelson effect is large, the new member states are likely to experience difficulties meeting the Maastricht criteria for euro adoption in the near future. Although the two papers dealing with this issue test different (domestic and international) versions of the Balassa–Samuelson models, and thus arrive at different conclusions regarding the size of the Balassa–Samuelson effect, interestingly, both argue that the productivity differences underlying this effect are not likely to be a major factor that will hinder these countries' ability to meet the Maastricht criteria on inflation and exchange rate stability.

If the new EU member states are closely integrated with the euro area countries, in the sense that they are subject to similar economic shocks, joining the euro area quickly will not bring about significant welfare losses. The next two papers investigate this aspect of euro adoption. They focus on the correlation of supply and demand shocks between accession and euro area economies and the responses of the accession economies to shifts in Euro-area monetary policy. Both papers find that the front-runner countries are closely integrated with the euro area, suggesting that joining the euro area quickly will not create significant welfare losses. These economies, which are

sensitive to shifts in Euro-area monetary policy, are better off with a flexible exchange rate regime in the period until joining ERM2. An interesting finding is that Hungary, which has had an ERM2-type exchange rate band since October 2001, seems to belong to this group.

The second section includes papers discussing individual countries. These countries have different exchange rate arrangements, are in different cyclical positions, and pursue different macro-economic policies. Poland is the largest economy among the new members and the least open one. It has a freely floating currency and presently has a large fiscal problem. Estonia, on the other hand, is a small and very open economy. It has a fiscal surplus, hardly any public debt, and a currency board arrangement. While Poland is coming out of a long economic slowdown and has a relatively large output gap, Hungary is experiencing a slowdown after a long period of strong growth. The papers and discussions on euro adoption in these three new EU member states provide an excellent overview of why and how their strategies for euro adoption might differ.

The experience of Estonia is of particular interest to the other new member states with flexible exchange rate arrangements. By introducing a currency board, it gave up an independent monetary policy early in the transition. At that stage of its development, it clearly was not part of an optimum currency area with Germany (the original peg was to the Deutsche Mark). Nonetheless, real convergence was fast and the business cycle became more or less synchronised with the business cycle in the euro area, clearly suggesting that Estonia is now well placed to adopt the euro. On the other hand, even after a decade of a hard peg, nominal convergence is a major issue in Estonia and policymakers may still have to undertake *ad hoc* short-term measures to meet the inflation criterion.

Croatia hopes to join the EU in the second wave of enlargement at a time when some of the first-wave new members are expected to be in the final phase of euro adoption. This will create strong incentives for Croatia to speed up its policy and structural adjustments to meet the Maastricht criteria and aim for an early adoption of the euro. As Croatia is perhaps the most euroised economy outside the euro zone, early euro adoption seems a natural target for policymakers and can reduce the risks monetary policy faces in the interim period between accession and adoption of the euro. The experience of Croatia may also offer useful lessons for the other second-wave accession countries.

We hope that our readers—academics, policy makers, and market participants alike—will find these papers and discussions helpful in understanding the factors that will shape macro-economic policy making in the coming years and determine the timing of euro adoption in the new EU member states. A better understanding in this regard will no doubt promote

better policy decisions and more realistic market expectations about the true timing of euro adoption. Both would help to make the process smoother and avoid abrupt adjustments in financial markets. We would like to thank the authors and discussants of this special issue for their excellent contributions and outstanding cooperation throughout the production process.