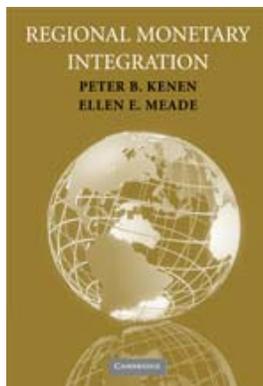


# COUNCIL ON FOREIGN RELATIONS

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## **Council on Foreign Relations Book** ***Regional Monetary Integration***

Teaching Notes

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*Regional Monetary Integration* surveys the prospects for monetary integration in various parts of the world. Beginning with a brief review of the theory of optimal currency areas, the book goes on to examine the structure and functioning of the European Monetary Union and then turns to the prospects for monetary integration elsewhere in the world—North America, South America, and East Asia. Such cooperation may take the form of full-fledged monetary unions or looser forms of monetary cooperation. The book emphasizes the economic and institutional requirements for successful monetary integration, including the need for a single central bank in the case of a full-fledged monetary union, and the corresponding need for multinational institutions to safeguard its independence and assure its accountability. The book concludes with a discussion of the implications of monetary integration for the United States and the U.S. dollar.

This book is suitable for the following types of courses:

- Courses on international money and finance
- Courses on European integration
- Courses on international economic relations
- Courses on comparative political economy

These teaching notes, discussion questions, and suggestions for further projects—including class debates, memoranda to the president, and role playing—may be useful for students in any of the courses listed above.

Instructors of specialized or advanced-level courses may wish to supplement with additional readings. The module and “Further Reading” section at the end of these notes are good places to start; additional publications and relevant websites are listed in the book.

## Discussion Questions

### **Courses on International Money and Finance**

1. To what extent does the European Union form an optimal currency area? Compare and contrast other regions of the world with Europe as to their suitability for adopting a single currency.
2. Why is it important to examine the effects of different exchange rate regimes using *de facto*, rather than *de jure*, measures of the regimes? What are the most important differences in macroeconomic outcomes associated with different exchange rate regimes?
3. Why might a group of countries forming a monetary union decide to peg the union's currency to a basket that includes the currencies of countries outside the group? What would an external basket peg imply for the monetary policy of the countries in the monetary union? What countries might favor this option?
4. What is the economic rationale behind each of the Maastricht Treaty's convergence criteria? Are these criteria important for judging whether a country is ready to join a monetary union? If so, why?

### **Courses on European Integration**

1. To what extent does the European Union form an optimal currency area? What are the main benefits to Europe from forming a monetary union and adopting the euro?
2. What are the main problems associated with the adoption of the euro by the accession countries in Eastern Europe? Would you expect the accession countries to enter the monetary union soon or to postpone entry to some later date?
3. What is the likely future development of the exchange rate between the euro and the U.S. dollar? In what ways has Europe's monetary union influenced the evolution of that exchange rate? Identify specific channels through which the monetary union has affected the bilateral exchange rate.
4. Compare the nineteenth century monetary unions with Europe's monetary union. In what ways is the European monetary union different? Did those earlier unions constitute "true" monetary integration? Why or why not?

### **Courses on International Economic Relations or Comparative Political Economy**

1. Why is institutional architecture important for a monetary union? Why is the monetary union in Europe more likely or viable than a monetary union among Asian countries?
2. To what extent has the European Central Bank been transparent about its monetary policy and accountable for its actions? Some claim that Europe's central bank is not democratically accountable. Why do they say this?
3. To what extent did the creation of Europe's monetary union reflect economic concerns and to what extent did it reflect politics? How do concerns about sovereignty figure into the answer?
4. What is the best forum in which to discuss the external value of a monetary union's currency? Should the union's exchange rate policy be handled by the single central bank or by the finance ministers of the union's members? How has Europe dealt with this issue?

## **Further Projects**

### **Debate**

Divide students into small teams and organize a debate on one or more of the issues raised in the book, for example:

- The pros and cons of having a single central bank set monetary policy for a group of countries
- The prospects for monetary integration in Asia, ranging from closer coordination to full monetary union
- The need for criteria to judge economic convergence for a group of countries wishing to form a monetary union
- The likelihood of the formation of new monetary unions outside of Europe

### **Memorandum to the President**

Assign students to write a memorandum to the President of the United States on the possibility of a U.S. monetary union with Canada and/or Mexico. The memorandum should provide reasons for expecting single currency to be beneficial for North America, and should discuss practical issues such as how the union's central bank should be organized, to what governmental bodies should it be accountable, and what the new currency should be called. In addition, the memorandum should address potential problems—such as income disparity and immigration—and how they might be dealt with. In the end, assess the pros and cons of full monetary integration, and recommend a course of action.

### **Role Playing**

In this task, groups of students would represent different regions of the world and argue the case for monetary union in each region at a mock board meeting of the International Monetary Fund. Divide students into small groups, each assigned to represent the views of a regional country group. The students must then argue from the perspective of that country group and make the case for monetary integration to other members of the IMF's board. After each group makes a presentation and takes questions from other IMF board members, the board should vote on whether the regional unions should be approved.

## **Further Reading**

- Barro, Robert J., "Currency Unions for the World," in Asian Development Bank, ed., *Monetary and Financial Integration in East Asia: The Way Ahead*, Vol. 2 (Basingstoke: Palgrave Macmillan, 2004).
- Berg, Andrew, and Eduardo R. Borensztein, "The Pros and Cons of Full Dollarization," in Salvatore, Dominick, James W. Dean, and Thomas D. Willett, eds., *The Dollarization Debate* (Oxford: Oxford University Press, 2003).
- Chinn, Menzie, and Jeffrey Frankel, "Will the Euro Eventually Surpass the Dollar as Leading International Reserve Currency?" in Clarida, Richard H., ed., *G7 Current Account Imbalances: Sustainability and Adjustment* (Chicago: University of Chicago Press, 2007).
- Ghosh, Atish R., Anne-Marie Gulde, and Holger Wolf, *Exchange Rate Regimes: Choices and Consequences* (Cambridge, MA: MIT Press, 2002).
- Kenen, Peter B., *Economic and Monetary Union in Europe: Moving Beyond Maastricht* (Cambridge: Cambridge University Press, 1995).

- Masson, Paul R., and Catherine Pattillo, *The Monetary Geography of Africa* (Washington, DC: Brookings Institution Press, 2005).
- Murray, John D., “Why Canada Needs a Flexible Exchange Rate,” in Salvatore, Dominick, James W. Dean, and Thomas D. Willett, eds., *The Dollarization Debate* (Oxford: Oxford University Press, 2003).

The Council on Foreign Relations (CFR) is a globalist international organization founded in 1921, which has long promoted the involvement of the United States in other nations and the protection of international business interests. The CFR seeks to influence American politics by inviting presidential candidates to speak at its events and by encouraging potentially influential businessmen, lawyers and government officials to join its organization or participate in its events. Many American presidents Here, at the Council on Foreign Relations, in the heart of the capital of the most powerful nation in the world, I do not have to stress the importance of international cooperation and strong international institutions. Everyone is aware of this, at least almost everyone. Let me put it this way: The future does not belong to those who deny reality and isolate themselves.