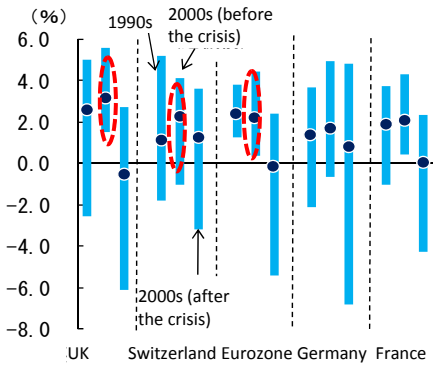
- After the Euro's introduction, the United Kingdom and Switzerland achieved better economic growth and employment performance than those of the Eurozone. The financial sector as a core industry has maintained its comparative superiority and its unshaken position as an international financial center. (Figs. 75 and 76)
- The two countries had raised funds from the Eurozone and lent them to non-Eurozone countries before financial flow was reversed due to the global financial crisis. Both before and after the crisis, the two countries' financial sector has increased its importance as a fund supply/demand contact between Eurozone and non-Eurozone countries. (Figs. 77 and 78)

Fig. 75 Each Country's Economic Performance

(1) Real Economic Growth



(2) Unemployment Rate

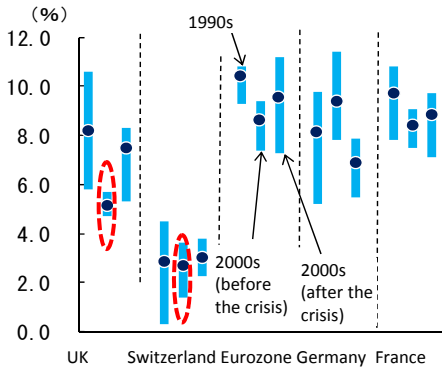
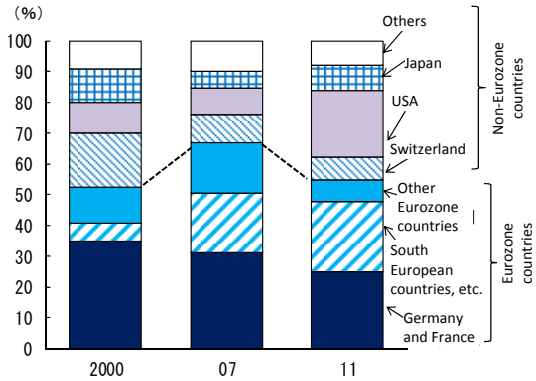


Fig. 77 UK's External Loans and Borrowings by Country

(Borrowings)



(Loans)

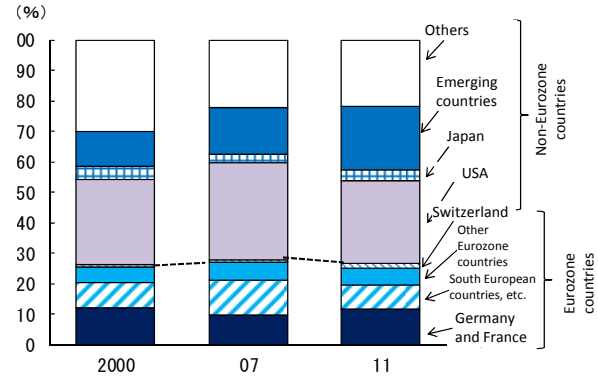
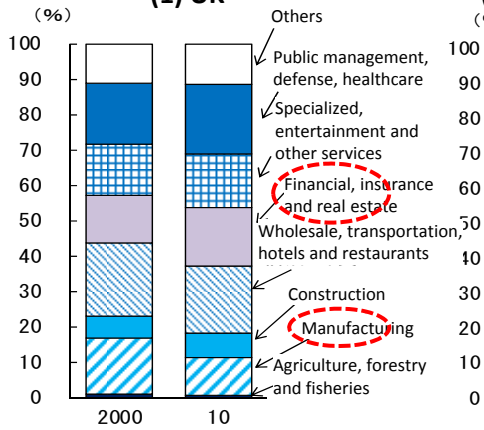


Fig. 76 Industrial Structure

(1) UK



(2) Switzerland

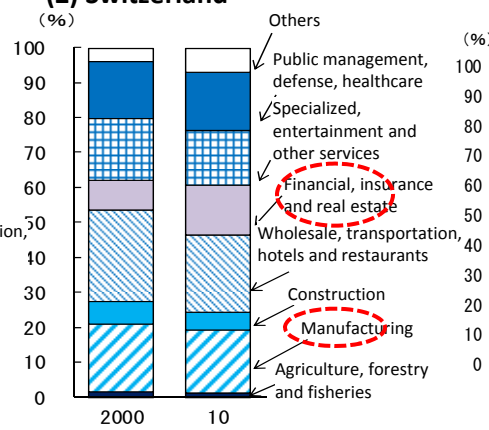
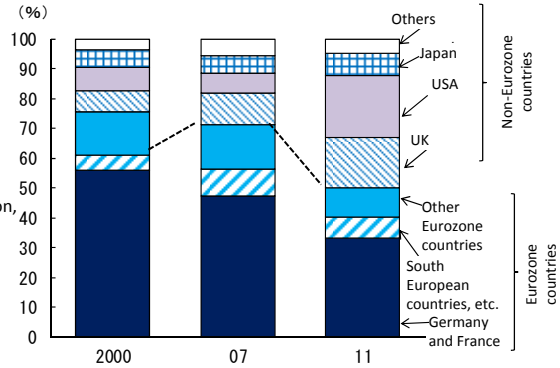
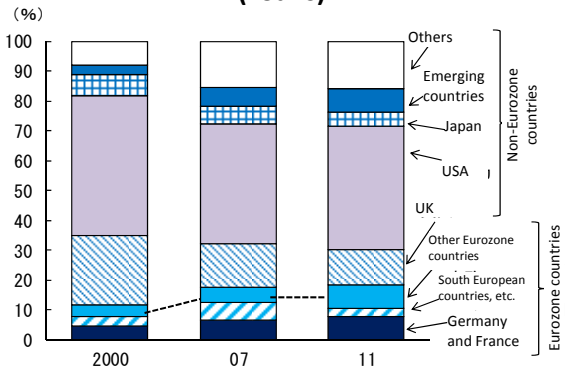


Fig. 78 Switzerland's External Loans and Borrowings by Country

(Borrowings)



(Loans)



- The United Kingdom and Switzerland have had close trade relations with the Eurozone. But changes in their real trade volumes with the Eurozone after the euro's introduction contrast. (Fig. 79)
- The difference in the trade volume changes might be attributable to a difference between their directions of foreign exchange rate changes just after the Euro's introduction and after the global financial crisis and a gap between their non-price competitive positions against the Eurozone. (Figs. 80 and 81)
- While the ECB cannot take monetary policies satisfying all the Eurozone countries due to their different economic conditions, the UK and Swiss central banks can take relatively flexible measures. (Fig. 82)
- But their respective currencies are more vulnerable to domestic and foreign economic shocks than the common currency of the Euro. (Fig. 83)

Fig. 79 Changes in Real Trade Volumes with Eurozone (Comparison of trade volumes before the euro's introduction, between the introduction and the financial crisis, and after the crisis)

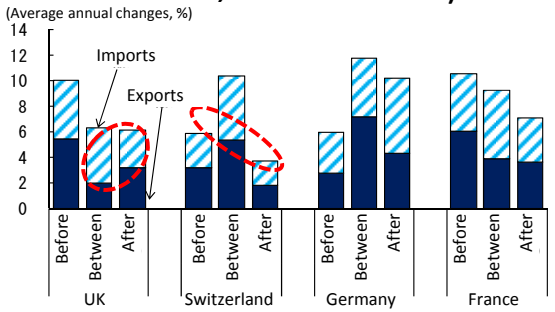


Fig. 80 Real Exchange Rates (against euro)

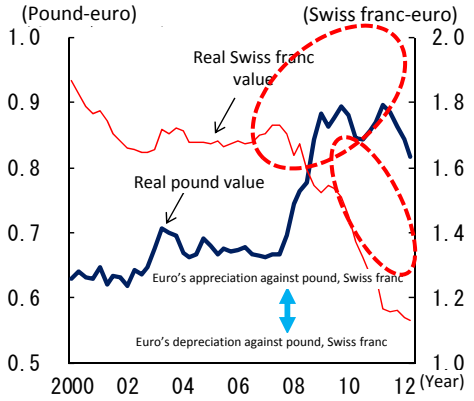


Fig. 81 Changes in Coefficients of Specialization in Trade with Eurozone

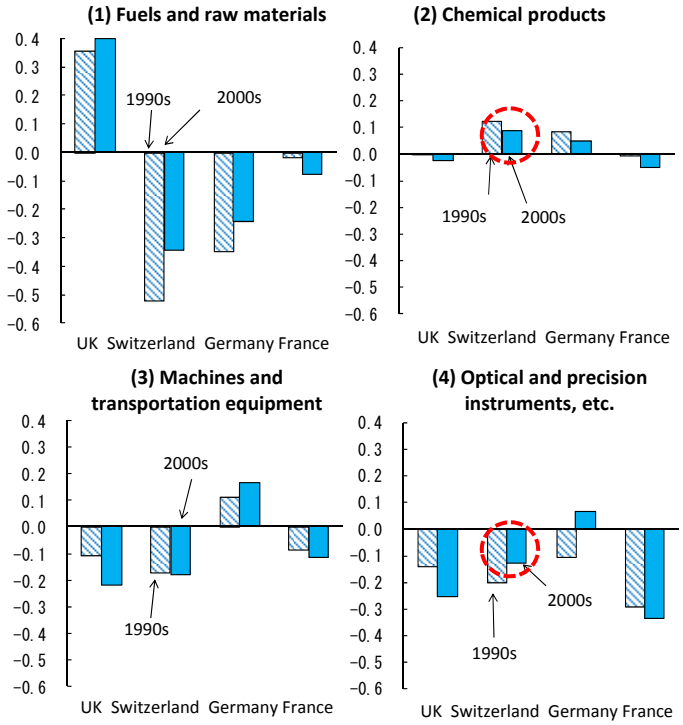


Fig. 82 Economic Trends upon Policy Interest Rate Changes

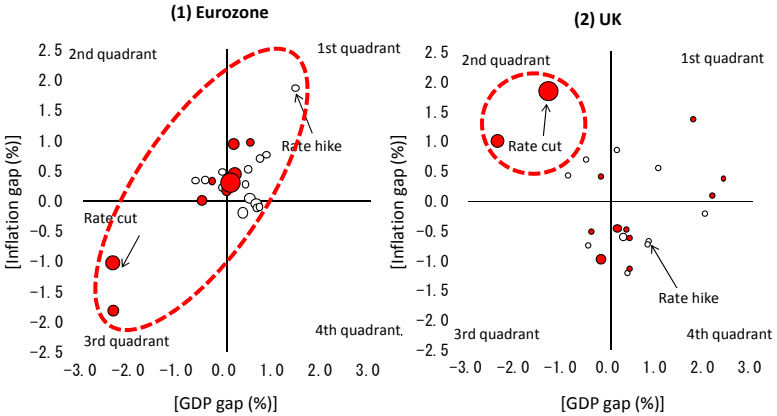
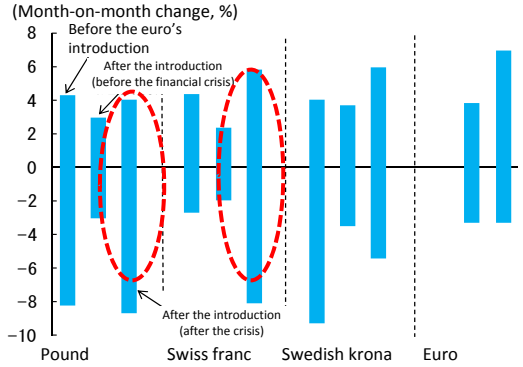


Fig. 83 Monthly Changes of Each Currency (effective rate)



- Some Asian countries had pegged their currencies to the US dollar until before the currency crisis. The inflow of short-term funds into these countries expanded as deregulation was coupled with high interest rates. Pressure continued on their currencies to appreciate against the dollar. Their short-term external liabilities far exceeded their foreign currency reserves. (Figs. 84-86)
- Funds flowing from abroad contributed to domestic capital investment growth. Foreign funds also flew into housing markets, overheating such markets in some countries. (Figs. 87 and 88)
- Total factor productivity (TFP) growth followed a downtrend before the currency crisis, indicating that funds flowing from abroad did not necessarily contribute to improving growth potential. (Fig. 89)
- Asian currencies other than the Indonesian one have generally been less volatile since the International Monetary Fund's support responding to the currency crisis. (Fig. 90)

Fig. 84 Capital Account Balance (Thailand)

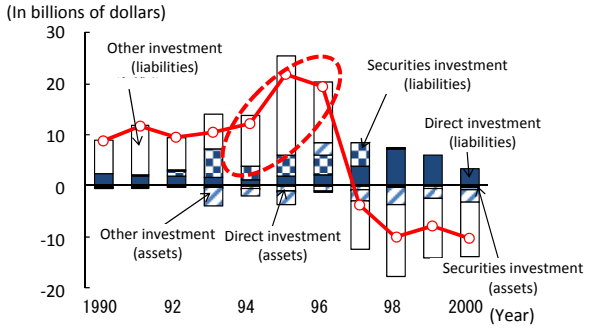


Fig. 86 Short-term External Liabilities' Ratios to Foreign Currency Reserves

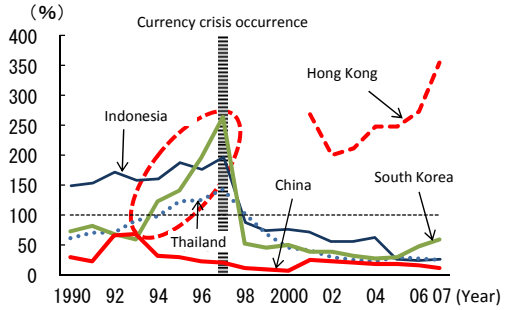


Fig. 89 TFP's Contribution to Real Economic Growth Rate

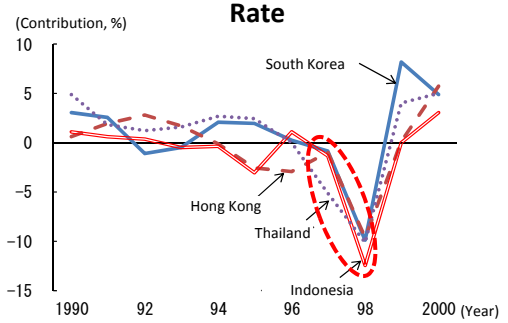


Fig. 85 Exchange Rate Trends

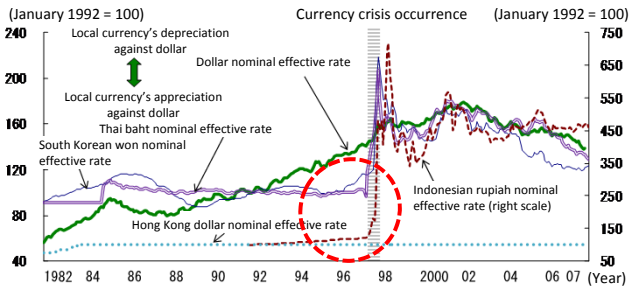


Fig. 87 Housing Prices

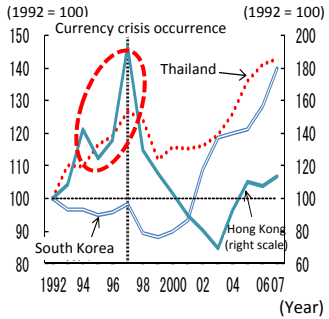


Fig. 88 Gross Fixed Capital Formation

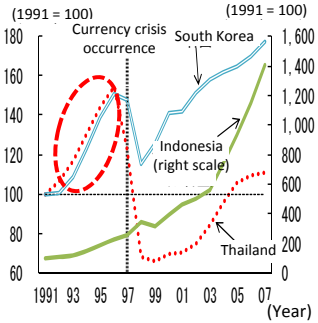
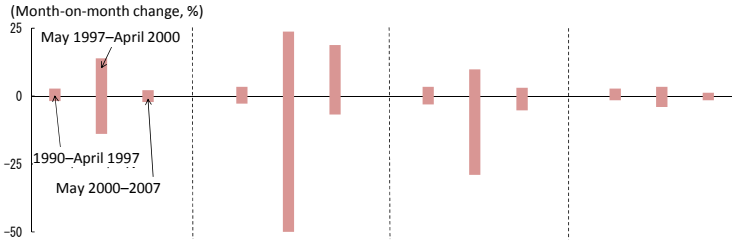


Fig. 90 Monthly Changes of Each Currency (effective rate)
(1) Thailand (2) Indonesia (3) South Korea (4) Hong Kong



- China has adopted a managed float system to strictly control exchange rate fluctuations and imposed strict restrictions on moves of international short-term funds, allowing its renminbi (RMB) to remain stable even after the currency crisis. (Fig. 91)
- As fund inflow after China's accession to the World Trade Organization in 2001 increased pressure on the RMB to appreciate against other currencies, the authorities repeated foreign exchange market interventions, leading to increases in foreign currency reserves. (Fig. 92)
- Investment from abroad has focused on direct investment under strict capital regulations. Both capital and current account balances have been in surplus. (Figs. 93 and 94)
- The RMB's gradual internationalization is going on through trade settlements and Hong Kong's offshore market. (Figs. 95 and 96)

Fig. 91 RMB's Real Effective Exchange Rate

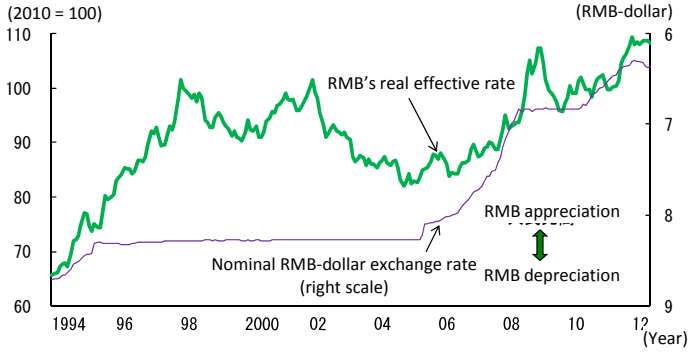


Fig. 93 Capital Account Balance

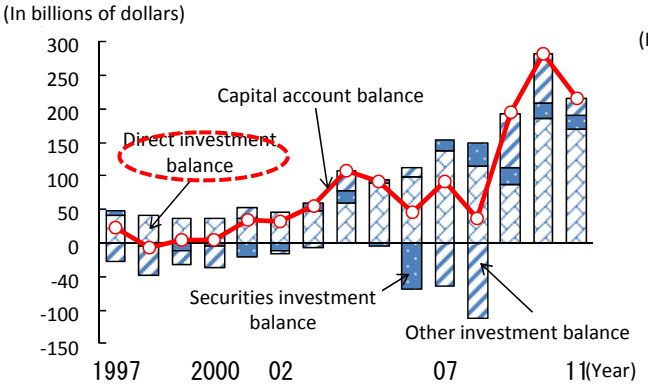


Fig. 95 Changes in RMB-denominated Deposits in Hong Kong

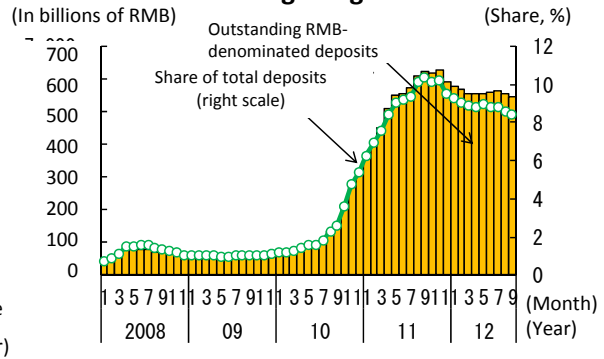
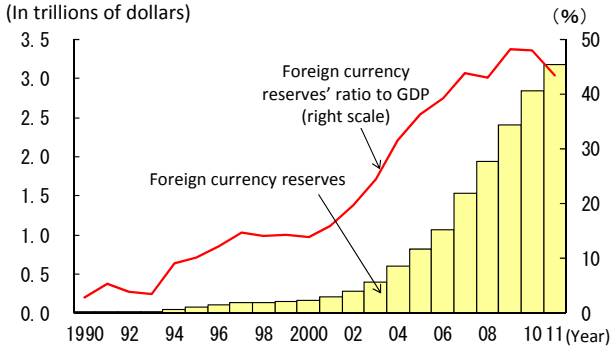


Fig. 92 Changes in Foreign Currency Reserves



Note: Prepared from data from the People's Bank of China

Fig. 94 Current Account Balance

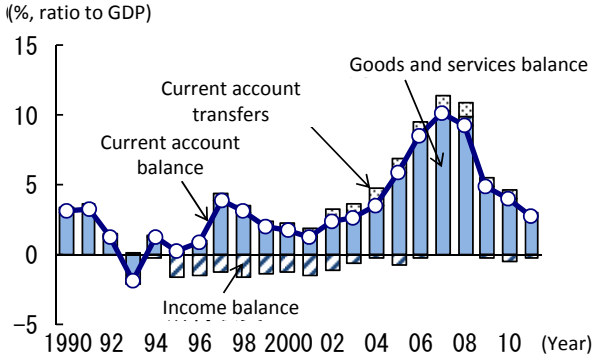
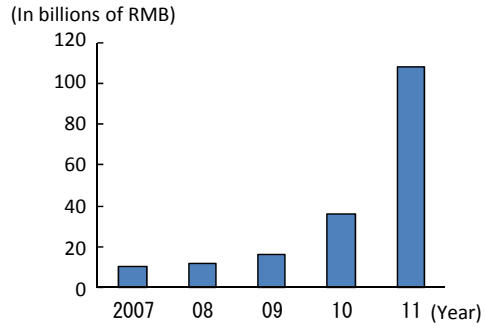


Fig. 96 New RMB-denominated Debt Issues



- Limited Advantages of Fixed Monetary System
  - The adoption of any fixed monetary system is not a necessary condition for invigorating trade and investment. Such invigoration can be achieved through the accession to free trade blocs like the European Union.
  - Small countries expect to stabilize prices with fixed monetary systems. However, some are still inflationary (including Greece). Meanwhile, non-Eurozone countries can control inflation depending on policies.
  - A common currency improves individual currencies' stability. However, all common currency zones have great effects on and responsibilities for neighboring countries

- Market Confidence and Safety Net Development Required for Maintaining Fixed Monetary Systems
  - In the absence of foreign exchange risks, there is a risk that massive short-term fund inflow from abroad could lead to speculative housing investment and loose fiscal policy.

  ⇒ Safety net development and structural reforms before or after any crisis should be implemented to increase resistance to internal shocks.

- Conditions That Must Be Reaffirmed for An Optimal Currency Zone
  - According to the optimal currency zone theory, a common currency can be introduced even under asymmetric shocks if conditions such as the mobility of production factors and the flexibility of prices are secured.

    ⇒ Actually, the Eurozone includes certain countries plagued with frequent asymmetric shocks and features rigid labor mobility and wage adjustment.
  - Imbalances can be corrected if fiscal funds are transferred. Given public opposition to fiscal fund transfers, however, the feasibility of any fiscal union is uncertain.
  - The willingness to reaffirm conditions for an optimal currency zone and establish a solid monetary system internally and externally is put into question.