1. Introduction

This paper reviews the current state of affairs with European Monetary Union (EMU) and draws out some of the implications for trade in goods and services and foreign direct investment, both within Europe and outside of Europe, and with particular reference to Canadian interests. This first section lays out the background to EMU, the timetable for the process, the convergence criteria for EMU and possible scenarios for the European Union (EU) up to the beginning of the next millennium.

In the 1980s and 1990s a radical shift took place in Europe. The European Economic Community (the EEC) came into existence after the Intergovernmental conference (IGC) of 1957, and was based on the general framework for integration embodied in the Treaty of Rome of 1958. In the Treaty of Rome, the underlying premise was to foster closer economic and political associations between the signatories, principally because of latent fears that Germany could once again threaten the stability of Europe at some future time. The EEC countries, or "Member States" as they are now called, have, after years of stalling, particularly in the 1970s and early 1980s, forged ahead over the last decade and constructed an ambitious integration project that is unprecedented in its depth and scope. Much of the recent progress is due to the visionary leadership of Jacques Delors, who came to be either despised or admired by the political classes throughout Europe. The attempts at creating a single European market in goods, services, labour and capital were embedded into the Treaty of Rome, but there had never been the coincidence of interests to bring unanimity to achieve such an aim. The breakthrough came through the work of the Dooge Committee, which produced a blueprint for the Single European Act (SEA) - only when it was signed at the European summit in 1986 did the prospect of a single market look likely. After ratification of the SEA, with controversial referendums in both Denmark and Ireland, the European Commission began to propose directives for creating a single market, most of which have now been ratified by all Member State parliaments.

Following on from the success of the exchange rate mechanism (ERM) of the European Monetary System (EMS), an adjustable peg exchange rate regime that was put in place in March, 1979, it was conceivable that further attempts to introduce a common European currency might now be feasible (- a failed attempt had been initiated in 1971). The Delors committee of experts produced a report in 1989 that laid out a blueprint for achieving EMU which was then taken forward as the discussion document for the Intergovernmental negotiations of 1991 that culminated with the Maastricht Treaty.

While the original motivation for EMU was mostly economic (see Commission of the European Communities (1990) where the justification for EMU was as a logical extension to the single market), it is undoubtedly the case that since the incorporation of the EMU process into the Maastricht Treaty in 1991, the essential motivation is now political (see Sutherland (1997)). From an economic perspective, there was certainly some doubt about the gains to be made from adopting a single currency, apart from the obvious savings from eliminating the cost of converting currency between Member States. Many of the arguments for a single currency related to the single market, and indeed the main rationale still given by the European Commission is to entrench the economic gains from the single market and to improve on its operation by removing currency costs.

The Delors report of 1989 (Committee on the Study of Economic and Monetary Union (1989)) was the initial catalyst for the inclusion of the subject of EMU in the 1990 IGC. It had as its lynchpin, the ERM, which is officially centred around the European Currency Unit (ECU), a composite currency, but in reality the Deutschemark had become the *de facto* anchor for the system. The ERM had assisted in lowering volatility among European exchange rates (see Artis and Taylor (1994) and Crowley (1995)) and had helped to foster economic convergence among EU Member States. The credibility afforded to the ERM could apparently even compensate for large inflation differentials between Member States, so it was deemed that fixing of exchange rates and then adopting a single currency would not be inconsistent with the recent history of the ERM at that time. The Delors report suggested a three stage process for adopting a single currency, the European Currency Unit (ECU), and the creation of a European Central Bank (ECB) to conduct monetary policy for the single currency.