



Chart in focus

Euro on the rise despite the crisis

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The euro is going strong as a reserve currency: the chart shows the euro and US dollar shares in international foreign-exchange reserves and their annual percentage change.

It can be seen that the share of the euro has risen strongly since the currency was launched eleven years ago. By Q3 2009 it had grown to 27.7%, from 18.1%. This represents an increase of 53% in a growing environment, as total forex reserves have quintupled over the same period.

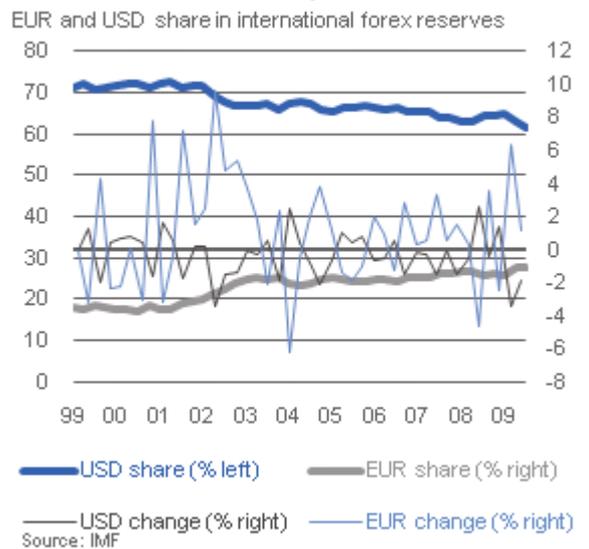
Nonetheless, Eurosceptics consider the euro's role as reserve currency to be in jeopardy at present. They fear that high government debt in some EMU countries could make the euro unattractive to international investors. This argument does not hold, however, as the lack of risk appetite is offset by higher risk premiums on government bonds in debtor countries. So it is no contradiction that the euro's share in global forex reserves reached its highest level since 2004 in Q1 2009, when risk premiums on Greek bonds hit a first record high.

What's in store for the future? On a medium-term horizon there are no alternatives to the euro and the dollar. To be sure, sterling could benefit for a short while from turbulence in the euro area. But Britain's expansionary monetary policy and inflationary tendencies make sterling an expensive alternative in the long run.

The euro will continue to gain in importance relative to the dollar – not only because of the confidence built by the ECB's conservative monetary policy over the past years. Another reason is the potential for diversification: only within EMU can investors choose from a wide range of government bonds issued in the country's home currency with different yield and risk classes without having to switch currencies.

Over the long term, the euro's significance will depend neither on the US nor on Europe but on China's willingness to liberalise its capital markets. With free movement of capital and freely floating exchange rates the yuan could become a serious alternative to the euro and the dollar as reserve currency.

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