

## **Many a slip - some forthcoming euro problems**

We are all familiar with the notion of something being fine in theory, but deficient in practice. The euro is likely to bring this notion home in devastating form to many organisations, and maybe even countries.

If we consider just the example of international banking - which I still consider to be the leading industry in this matter - a group calling itself the Heathrow group recently published a document on the possibilities of widespread settlement failure (which is just about equivalent to market failure). They suggest that if market participants include *full* information on settlements, including the medium (TARGET, EBA, CAHPS-euro etc.) then the number of fails will increase catastrophically.

Their solution - a sensible one - is for market participants to leave decisions on movement of funds to their agents.

But the origin of this problem is an interesting one. It is caused by two circumstances which have been given too little consideration and may creep up and bite this whole project.

The first is that it is an externally imposed market change without a single regulator responsible to whom reference can be made to ascertain the answer to complex and detailed problems. The second is that the market will not have time to adapt itself to the changes over a period of months or years - it will all have to work perfectly, first time.

So what will happen if market participants do not have the same view of market procedures? Well, it's quite simple. Payments and delivery of securities will simply grind to a halt. Probably by the end of the second or third day of trading.

This is just one of the dangers which businesses face as a result of the introduction of the euro. Let us look at some of the others:

Introduction of cash. This will affect the entire range of retail services, from supermarkets to banks. So far, few of the national authorities are believed to have considered the implications of *either* a long or a short replacement of cash. Both options have significant problems. Distribution of vast quantities of metal and paper, and their distribution to a public which will have difficulty telling the real from the forged, will be a major challenge. Conversely, running two separate sets of physical cash will be immensely expensive for retailers and banks.

Take-up within supply chains. Some supply chains will convert early, some late, and some will run two currencies in parallel for a long time. Participants must be prepared to handle a significant proportion of transactions in each currency. An organisation which fails to determine the take up within its market faces the risk of not being able to process all of its transactions without a major increase in manual workarounds.

Wrong assumptions. In some cases entire markets have made inaccurate assumptions as to the market of the future. In a case which appears to have been rectified, the Dutch banks have had to reconsider their view that few commercial and retail customers would need euro accounts during the transition period. The cost of this reconsideration has, we would expect, been higher than getting it right the first time. If it had been discovered a

few months later, the Dutch banks might have found themselves seriously embarrassed by incomers able to offer the desired service.

There will be