

Common Currency Areas and Currency Unions: An Analysis of the Issues

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Abstract

This paper discusses the conditions under which currency unions would be desirable and viable. We discuss and present new empirical evidence concerning the operation of existing currency unions in federal states and among regional country groupings. In particular, we examine the traditional criteria for optimal currency areas and present evidence concerning the shock-absorbing properties of federal fiscal systems and the discipline imposed on the public sector by financial markets. We also examine the implications of economic heterogeneity across a currency union, and whether or not convergence should be achieved before rather than after the union occurs. In addition, some issues relating to the possible transition towards monetary union in Europe are considered.

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