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Recent developments
The Netherlands in the euro area

The international environment has deteriorated markedly in recent months. Initially, the deterioration was confined to the United States, but now the euro area economy is also slowing down. As a result, and owing to lower consumer demand, economic growth in the Netherlands has dropped materially. In July, the Dutch inflation rate was again the highest in the euro area. Although this is attributable in large measure to one-off factors, the high degree of capacity utilisation is also playing a significant role in this respect. Now that growth is slowing down, the degree to which wages will adjust will be crucial for the dynamics of inflation. Unduly slow adjustment may further impair competitiveness and may ultimately lead to higher unemployment.

Worsening international environment

World economic conditions have deteriorated over the past year, as reflected in a sharply decreased growth rate of world trade (Chart 1). Internationally, developments are dominated by the sharp growth deceleration in the United States. In the second quarter of this year, US GDP in volume terms was just 1.2% up on a year before (Table 1). The changed perception of the (profit) potential of the ‘new economy’ in particular is a major factor underlying the current state of stagnation. The unexpected drop in demand for notably computers and passenger cars led first of all to unduly high stock levels, causing corporations to embark on substantial production cutbacks. The resulting downturn was strengthened in the first six months of this year by a sharp decrease in investment, especially in the ICT sector. In the first half of the year ICT investment made a negative contribution to the US economic growth rate, against a positive contribution of 1 percentage point in the preceding period. The stock exchange climate plays an important role in this respect. The sharp price correction for equities of technological corporations in particular is complicating the financing of new invest-

Table 1  Economic growth in the United States
Per cent changes on previous corresponding period

<table>
<thead>
<tr>
<th></th>
<th></th>
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<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
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<td>GDP</td>
<td>4.1</td>
<td>4.1</td>
<td>5.2</td>
<td>4.4</td>
<td>2.8</td>
<td>2.5</td>
<td>1.2</td>
</tr>
<tr>
<td>Private consumption</td>
<td>5.0</td>
<td>4.8</td>
<td>4.9</td>
<td>4.9</td>
<td>4.2</td>
<td>3.5</td>
<td>3.2</td>
</tr>
<tr>
<td>Private investment</td>
<td>7.8</td>
<td>7.6</td>
<td>8.6</td>
<td>7.4</td>
<td>6.3</td>
<td>3.4</td>
<td>-1.4</td>
</tr>
<tr>
<td>of which ICT investment</td>
<td>17.9</td>
<td>20.4</td>
<td>20.8</td>
<td>19.4</td>
<td>19.8</td>
<td>8.2</td>
<td>-2.2</td>
</tr>
<tr>
<td>Government expenditure</td>
<td>3.3</td>
<td>2.7</td>
<td>4.0</td>
<td>2.4</td>
<td>1.2</td>
<td>2.8</td>
<td>3.0</td>
</tr>
<tr>
<td>Exports</td>
<td>3.2</td>
<td>9.5</td>
<td>11.1</td>
<td>11.3</td>
<td>7.0</td>
<td>4.4</td>
<td>-2.1</td>
</tr>
<tr>
<td>Imports</td>
<td>10.5</td>
<td>13.4</td>
<td>14.4</td>
<td>14.2</td>
<td>11.3</td>
<td>5.6</td>
<td>-0.4</td>
</tr>
</tbody>
</table>

Per cent changes on immediately preceding period, annualised

<table>
<thead>
<tr>
<th></th>
<th>1999</th>
<th>2000</th>
<th>2000</th>
<th>2001</th>
</tr>
</thead>
<tbody>
<tr>
<td>GDP</td>
<td>5.7</td>
<td>1.3</td>
<td>1.9</td>
<td>1.3</td>
</tr>
</tbody>
</table>

Contributions to GDP growth, percentage points

<table>
<thead>
<tr>
<th></th>
<th>1999</th>
<th>2000</th>
<th>2000</th>
<th>2001</th>
</tr>
</thead>
<tbody>
<tr>
<td>Private consumption</td>
<td>2.5</td>
<td>2.9</td>
<td>2.1</td>
<td>2.1</td>
</tr>
<tr>
<td>Private investment</td>
<td>1.5</td>
<td>0.4</td>
<td>0.1</td>
<td>0.3</td>
</tr>
<tr>
<td>of which ICT investment</td>
<td>1.3</td>
<td>0.9</td>
<td>0.9</td>
<td>-0.9</td>
</tr>
<tr>
<td>Government expenditure</td>
<td>0.8</td>
<td>-0.3</td>
<td>0.6</td>
<td>0.9</td>
</tr>
<tr>
<td>Stockbuilding</td>
<td>1.8</td>
<td>-1.0</td>
<td>-0.5</td>
<td>-2.6</td>
</tr>
<tr>
<td>Net exports</td>
<td>-0.8</td>
<td>-0.7</td>
<td>-0.4</td>
<td>0.6</td>
</tr>
</tbody>
</table>

Explanatory note: Contributions in percentage points; owing to statistical differences, the contributions do not add up to the GDP growth rate.
ment. Many budding ICT corporations used to rely on equity issues as a cheap source of funding. The current lower equity prices raise the cost of funding because larger equity packages must be issued in order to obtain the required amount of funds. This forces entrepreneurs, more so than in the past few years, to carefully weigh the costs of and the future returns on investment. All in all, owing to the correction which had already been expected for some time, the United States is to some extent, after years of exuberant growth, returning to more 'balanced' conditions.

The economic situation in Asia has also worsened in recent months. In the world’s second largest economy, Japan, which has shown little strength for a considerable period of time, growth has fallen to 0%. Signs for the near future do not suggest an improvement. Both domestic and foreign order inflows have decreased sharply, especially from North America. Korea, Singapore and Malaysia are also heavily affected by the US growth deceleration. As in Japan, technological products hold pride of place in these countries’ export mix.

Against the background of the changing economic dynamics, various national and international institutions have lowered their growth projections. Thus, for the current year, the oecd expects an average growth rate of no more than 2% for its members, half last year’s figure and the lowest rate since 1993.

**Domestic demand**

In the euro area, economic growth dropped to 2.5% in the first quarter of 2001 (Table 2). This was mainly due to the levelling-off of consumption growth, recently intensified by slowing investment growth. Although the global growth deceleration caused euro area exports to decline, imports fell even more sharply because of lower domestic expenditure. This explains the rising contribution of net exports to GDP growth and, hence, the relatively stable quarter-on-quarter movements. The simultaneity of the growth deceleration in the euro area and in the United States and Asia is, incidentally, no more than partially due to the contraction of trade flows. In Europe, an important role is presumable also

**Table 2 Economic growth in the euro area**

<table>
<thead>
<tr>
<th>1999</th>
<th>2000</th>
<th>2000</th>
<th>2001</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>I</td>
<td>II</td>
<td>III</td>
</tr>
</tbody>
</table>

Per cent changes on previous corresponding period

| GDP  | 2.5  | 3.4  | 3.5  | 3.8  | 3.3  | 2.9  | 2.5  |

**Gross contributions to GDP growth, percentage points**

| Consumption | 2.0  | 1.9  | 1.9  | 2.3  | 1.8  | 1.5  | 1.3  |
| Investment  | 1.1  | 0.9  | 1.2  | 1.0  | 0.9  | 0.7  | 0.3  |
| Net exports | -0.6 | 0.6  | 0.8  | 0.4  | 0.5  | 0.6  | 0.8  |

Per cent changes on immediately preceding

| GDP  | 0.9  | 0.8  | 0.6  | 0.6  | 0.5  |

---

**Chart 1 World trade and economic growth**

Per cent changes on previous corresponding period

![Chart](image-url)

played by lower consumer confidence and lower industrial confidence, both of which are highly sensitive to events in the United States and to the stock exchange climate.

In the Netherlands, growth dropped considerably more sharply than in the euro area as a whole. GDP volume growth slowed from 3.5% in 2000 to 1.5% in the first six months of this year (Table 3), the lowest rate recorded since the second half of 1993. The downward tendency set in last year when investment growth decelerated sharply. Initially, the decline was limited to investment in residential property and business premises, but in recent months corporations, prompted by a worsening profit outlook and heightened uncertainty about (international) cyclical movements, reduced investment across the board.

Early this year, the economic slowdown was intensified by lower consumer spending by households. The largest effects were evident in the first quarter, when consumption was below the level of the preceding quarter. In the second quarter, however, a low, positive quarter-on-quarter growth rate was recorded. None the less, a major proportion of the purchasing power improvement consequent on the tax reform has not yet been reflected in spending, resulting in a strong growth of household savings (Chart 2). This has caused the contribution of consumption to GDP volume growth to be halved to barely one percentage point. This levelling-off, which mainly focuses on consumer durables, may be explained in part from the VAT increase on 1 January last. The increase prompted consumers to advance their car purchases in particular. In the first quarter of this year, consumption of passenger cars in real terms was 20% lower than a year before. The 9% drop in the second quarter was already less pronounced. In addition, the abolition of the partial tax relief for interest paid on consumer credit may also have led to some

Table 3  Economic growth in the Netherlands
Per cent changes on previous corresponding period

<table>
<thead>
<tr>
<th></th>
<th>1999</th>
<th>2000</th>
<th>2000</th>
<th>2001</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>I</td>
<td>II</td>
<td>III</td>
<td>IV</td>
</tr>
<tr>
<td>GDP</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Private consumption</td>
<td>4.5</td>
<td>3.7</td>
<td>3.5</td>
<td>2.9</td>
</tr>
<tr>
<td>Business investment</td>
<td>7.8</td>
<td>3.1</td>
<td>7.0</td>
<td>2.7</td>
</tr>
<tr>
<td>Government expenditure</td>
<td>3.3</td>
<td>2.6</td>
<td>3.6</td>
<td>2.9</td>
</tr>
<tr>
<td>Exports</td>
<td>5.4</td>
<td>9.5</td>
<td>9.7</td>
<td>9.5</td>
</tr>
<tr>
<td>Imports</td>
<td>6.3</td>
<td>9.4</td>
<td>10.5</td>
<td>8.2</td>
</tr>
</tbody>
</table>

Gross contributions to GDP growth, percentage points

<table>
<thead>
<tr>
<th></th>
<th>1999</th>
<th>2000</th>
<th>2000</th>
<th>2001</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>I</td>
<td>II</td>
<td>III</td>
<td>IV</td>
</tr>
<tr>
<td>Private consumption</td>
<td>2.2</td>
<td>1.9</td>
<td>1.7</td>
<td>1.5</td>
</tr>
<tr>
<td>Business investment</td>
<td>1.4</td>
<td>0.6</td>
<td>1.4</td>
<td>0.5</td>
</tr>
<tr>
<td>Government expenditure</td>
<td>0.9</td>
<td>0.7</td>
<td>1.0</td>
<td>0.7</td>
</tr>
<tr>
<td>Stockbuilding</td>
<td>-0.6</td>
<td>-0.2</td>
<td>0.2</td>
<td>-0.5</td>
</tr>
<tr>
<td>Net exports</td>
<td>-0.2</td>
<td>0.6</td>
<td>0.0</td>
<td>1.3</td>
</tr>
</tbody>
</table>

Chart 2  Consumer credit and savings
Per cent changes on previous corresponding period

Explanatory note: Per cent changes have been calculated on the basis of debit balances (consumer credit) and balances on deposit accounts (savings) as the end of the period.

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*DNB / Quarterly Bulletin September 2001* 9
restraint among consumers where purchases of more expensive goods are concerned. This is suggested by the fact that the growth rate of consumer credit recently slowed down slightly, from over 10% in January to 7.5% in May (Chart 2). The high rate of inflation, which has wiped out part of the improvement in purchasing power, probably also exerts a dampening effect on consumer spending.

Although the decline in consumption growth was pronounced early this year, a downward tendency had already been in evidence for a number of quarters. This becomes clear when consumption growth is adjusted for car purchases and is thus partially adjusted for the anticipation effect in the fourth quarter of 2000 (Chart 3). In itself, declining consumption growth is not surprising given the strong growth of household income in the past few years. A plausible explanation for the timing of this downward tendency is provided by the lower influence of wealth effects. Not only has return on equity been low recently, but the rise in house prices has also levelled off. In the past, the sharp increases in house prices boosted consumer spending in and around homes. For 1999 the Bank estimated the relevant wealth effect to account for 0.6 to 0.7 percentage point of the \( \text{GDP} \) growth rate.¹ The less exuberant increase in house prices has already been reflected in a considerable decrease in mortgage renewals and second mortgages. Possibly as a result of this development, the first six months of this year saw an unchanged volume of sales of do-it-yourself products, while turnover at building stores declined slightly, following many years of strong growth.

Production

During the past few months, industrial activity in the euro area has slowed down. In the first five months of this year, industrial output growth averaged a mere 2.5%, while May even recorded a decrease. However, the slowdown is still less pronounced and also of more recent date than that in the United States, where industrial output has been contracting since October 2000. The deceleration in the euro area is due to both domestic and foreign factors. The weakness of domestic spending affects the durables sector in particular, while the lower demand for exports is also depressing production in the capital goods and intermediate goods sectors. For the coming months leading indicators such as the purchasing managers’ index, confidence and the ifo indicator, point to a further decline in industrial output, even if various indicators showed a slight increase in July. The services sector is also experiencing a slowdown, but this is considerably less pronounced than that in industry. The value added in this sector, which accounts for 68% of \( \text{GDP} \), increased in the first quarter by 2.9%, against 3.5% in 2000.

In the Netherlands, too, production has shifted to a lower gear. Especially output growth in industry has declined markedly, even more markedly than in the euro area as a whole (Table 4). In the first half of the year, the volume growth of Dutch output of goods was almost nil. The fact that, in this respect, the Dutch performance is below the European average is due in part to the comparatively large share of extra-euro area exports in Dutch \( \text{GDP} \) (over 20% as against 15% for the euro area as a whole). In addition, however, the Netherlands is losing ground in terms of market share to other euro area countries owing to the relatively strong price rises of Dutch exports. Finally, the Dutch export mix exerts a negative influence considering the high shares of sectors which tend to lead the business cycle, such as chemicals, metals and metals manufactures, and electrical engineering. Owing to the large share of re-exports, combined with the lower consumption growth, import growth has also dropped sharply. For the coming months the outlook is considerably less favourable than it was a number of months ago. Several indicators, such as industrial confidence and the Bank’s leading indicator, do not suggest a speedy economic recovery, despite the increase in the industrial confidence indicator in July.

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¹ DNB/ Quarterly Bulletin September 2001
The levelling-off of economic activity is in evidence almost across the board. Apart from the international slowdown, one-off factors are also making themselves felt. For instance, through negative output growth in the food, drink and tobacco sector (slaughterhouses), the consequences of the foot and mouth crisis are gradually being reflected in the figures. The immediate negative effect of the crisis on agriculture and slaughterhouses is expected to depress GDP growth in the second quarter by about 0.3 percentage point. In addition, indirect output effects are making themselves felt in the haulage, fodder and tourism sectors as well as within disposal companies. The overall effect is comparatively considerable, since the Netherlands is the largest exporter of livestock in the euro area.

Table 4 Output in the Netherlands
Per cent changes on previous corresponding period

<table>
<thead>
<tr>
<th></th>
<th>1999</th>
<th>2000</th>
<th>2000</th>
<th>2001</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total output</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Goods</td>
<td>2.9</td>
<td>3.3</td>
<td>4.2</td>
<td>2.1</td>
</tr>
<tr>
<td>Food, drink and tobacco</td>
<td>2.5</td>
<td>2.0</td>
<td>4.0</td>
<td>0.4</td>
</tr>
<tr>
<td>Construction</td>
<td>5.4</td>
<td>2.7</td>
<td>5.4</td>
<td>0.6</td>
</tr>
<tr>
<td>Commercial services</td>
<td>5.2</td>
<td>4.5</td>
<td>5.5</td>
<td>4.9</td>
</tr>
<tr>
<td>Catering</td>
<td>3.1</td>
<td>3.1</td>
<td>3.5</td>
<td>3.5</td>
</tr>
<tr>
<td>Postal and telecommunications services</td>
<td>18.0</td>
<td>19.8</td>
<td>16.7</td>
<td>16.5</td>
</tr>
<tr>
<td>Financial intermediaries</td>
<td>4.6</td>
<td>3.4</td>
<td>8.9</td>
<td>7.7</td>
</tr>
<tr>
<td>Non-commercial services</td>
<td>1.7</td>
<td>1.3</td>
<td>2.4</td>
<td>2.6</td>
</tr>
</tbody>
</table>

Gross value added at basic prices.
Source: Statistics Netherlands.

The growth deceleration is not confined to industry. Since the third quarter of 2000, the growth of construction output has almost come to a standstill in volume terms, while the first half of the year even saw a slight decline. This was due not only to disappointing demand but also to supply side constraints. Only 4% of construction businesses cite insufficient demand as a reason for production constraints, no more than a marginal increase compared to a year earlier. In May, however, 14% cited supply side problems owing to staff shortages. Moreover, the supply of building plots still does not match demand, witness the decrease in the number of building permits in a period when the housing market may still be characterised as tight. There is some evidence, however, suggesting that the supply side problems are diminishing. In September 2000, as many as 35% of construction businesses had encountered production constraints owing to staff shortages. These problems account in part for the sharp growth deceleration of investment in real estate, the bulk of which is undertaken by the construction sector.

In commercial services, which had been the driving force behind the strong economic growth of recent years, the growth of value added has also shown a decline in volume terms, from over 4% in 2000 to 2.3% in the first six months of this year. This has been due mainly to the telecommunications and financial sectors. The financial sector experienced a marked growth deceleration, hit as it was by a sharp decrease in commission income from stock exchange issues and regular stock exchange trade combined with rising interest expenses on deposits. In line with the global weakness in the ICT sector and lower demand for mobile telephony, growth in the postal and telecommunications sector slowed down markedly, from nearly 20% in 2000 to 10% in the first quarter of this year.

The growth deceleration in the Netherlands raises the question to what extent it resembles that in the United States. There are marked differences. In the United States, the slowdown would mainly appear to be a reaction to a period of overinvestment, with demand for ICT products in particular showing a decrease. In the Netherlands, however, the lower growth of investment is due in part to labour supply problems. Moreover, a major proportion of the slowdown in the Netherlands
may be ascribed to consumer spending, which is the very factor that is still to some extent propping up US economic growth.

Inflation and wages

Over the past few months, the euro area inflation measure which is relevant for monetary policy, the increase in the Harmonised Index of Consumer Prices (HICP), was considerably above the upper limit of price stability. At 3.4%, the highest rate of increase was recorded in May. During subsequent months, the rate of price increase slowed down slightly, to 2.8% in July, mainly as a result of diminished effects of energy prices and of the euro exchange rate, both of which were roughly at the same level as a year before. In the earlier stages of production, inflationary pressures are gradually subsiding. Purchasing managers cite reduced pressure on prices, and the rate of increase of producer prices has been slowing down in recent months (Chart 4).

In recent months, the Netherlands has been the highest-inflation country in the euro area. Whereas initially HICP inflation had fallen to 5.0% in June, from 5.4% in May, in July it showed a renewed rise, to 5.2%. A similar tendency is discernible in the inflation rate measured on the basis of the national definition (CPI), which reached 4.6% in July (Table 5). CPI inflation mainly differs from HICP inflation in that rents are included in the CPI but not in the HICP. Because, at 2.7%, the annual rent increase in July of this year was considerably lower than the inflation rate, the price rise measured by the HICP exceeded that measured by the CPI. July is the month which sees not only the annual rent increase but also the annual adjustment of gas and electricity prices. During the month, both these prices were raised; however, as the increases were virtually the same as last year, the net effect on inflation was nil.

The direct effect of non-recurrent factors on inflation has been decreasing in recent months. Owing to the stabilisation of oil prices compared to the level a year earlier, the increase in energy prices slowed down to 6.6%, the lowest level since November 1999. The effects of the foot and mouth crisis are also wearing off to some extent. Thus, in June and July the annual rate of price increase for unprocessed food slowed down slightly.

These downward pressures are offset by an overall upward tendency. For a broad range of goods and services, price increases were measured in recent months which considerably exceeded the levels which could be explained from the increase in the VAT rate and the environmental tax. This is especially evident in underlying market inflation (CPI), which shows inflation excluding the effects of government measures and some volatile components, such as energy, vegetables and fruit prices. Since October of last year, this measure has been showing a practically uninterrupted upward tendency, culminating in a new record high of 4.1% in July.

Despite the growth deceleration, the Dutch economy is still operating at high levels of capacity utilisation. Under such conditions, notably domestically-oriented businesses will seek to improve their profit margins and to reflect cost increases in full in selling prices. Compared to other euro area countries, wage costs in the Netherlands are showing a rapid rise. At about 4.8%, the increase in compensation per employee would appear to exceed last year’s level by a considerable margin. As a result, Dutch competitiveness, measured in terms of unit labour costs, has deteriorated in the past few years (Chart 5). Recently, this tendency was strengthened by the comparatively sharp decline in output, causing the increase in labour productivity to slow down. To what extent the upward pressures on prices will persist will depend on the degree to which wages will adjust to the changing economic conditions.
Labour market

After a period in which decreases were recorded, the euro area unemployment rate stabilised at 8.3% in recent months. Because of Germany’s heavy weight, the movements in German unemployment are of major significance for the movements in the euro area as a whole. If, owing to slower economic growth, German unemployment were to show an increase in the months ahead, the lowest level of unemployment in the current business cycle would not be below that in previous boom periods. This would suggest that German unemployment includes a persistent structural component (Chart 6), with a large proportion of the working population unable to find a job even in times of relatively favourable economic conditions.

The Dutch labour market situation contrasts sharply with that in the euro area as a whole. Despite the economic growth deceleration in the first half of the year, the tight labour market conditions would not seem to have eased to any considerable degree. In the first quarter, employment growth was still well over 2 1/2%, and the unemployment rate declined slightly further, to 1.8% in the period May-July. Although the number of unfilled vacancies did not increase further in the first quarter, the private sector still has 200,000 unfilled vacancies on offer and the public sector (including education) 15,000. Furthermore, the percentage of industrial businesses reporting production constraints owing to staff shortages has barely shown any decrease (from 10% to 9%). Although this cannot be distilled from the various macro-economic data, there are indications that in some market segments the tight conditions are easing to some extent. This is true of the ICT

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Table 5  Inflation in the Netherlands
Per cent changes on previous corresponding period

<table>
<thead>
<tr>
<th></th>
<th>1999</th>
<th>2000</th>
<th>2000</th>
<th>2001</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total HICP</td>
<td>2.0</td>
<td>2.3</td>
<td>3.0</td>
<td>4.8</td>
</tr>
<tr>
<td>Goods</td>
<td>1.7</td>
<td>2.9</td>
<td>4.0</td>
<td>5.5</td>
</tr>
<tr>
<td>Processed food</td>
<td>1.4</td>
<td>1.7</td>
<td>2.6</td>
<td>4.7</td>
</tr>
<tr>
<td>Unprocessed food</td>
<td>2.3</td>
<td>0.3</td>
<td>3.6</td>
<td>7.4</td>
</tr>
<tr>
<td>Industrial goods, excluding energy</td>
<td>1.5</td>
<td>0.9</td>
<td>1.7</td>
<td>3.3</td>
</tr>
<tr>
<td>Energy</td>
<td>2.8</td>
<td>14.9</td>
<td>15.6</td>
<td>12.7</td>
</tr>
<tr>
<td>Services</td>
<td>2.6</td>
<td>1.5</td>
<td>1.4</td>
<td>3.6</td>
</tr>
<tr>
<td>HICP, underlying 1</td>
<td>1.9</td>
<td>1.3</td>
<td>1.7</td>
<td>3.7</td>
</tr>
<tr>
<td>CPI</td>
<td>2.2</td>
<td>2.6</td>
<td>3.0</td>
<td>4.4</td>
</tr>
<tr>
<td>Market inflation, underlying</td>
<td>1.4</td>
<td>1.7</td>
<td>2.4</td>
<td>3.1</td>
</tr>
<tr>
<td>Exclusive of tax changes, low income</td>
<td>1.7</td>
<td>2.1</td>
<td>2.7</td>
<td>3.4</td>
</tr>
</tbody>
</table>

Sources: Eurostat and Statistics Netherlands.

1 Excluding unprocessed food and energy.
sector in particular, but medium and small-sized business are also reporting a decrease in the number of unfilled vacancies.

Monetary and financial developments

On 30 August last the European Central Bank (ecb) lowered the interest rate for main refinancing operations by 25 basis points, so that the overall monetary easing since the beginning of the year has reached 50 basis points. The policy rate thus came out at 4.25%. In its pursuit of price stability, the ecb Governing Council assesses the inflationary risks in the euro area on the basis of its two-pillar strategy.

In July the three-month moving average growth rate of the broad monetary aggregate $M_3$ accelerated by 0.6 percentage point to 5.9%. In this regard, a number of comments are in order. First, this $M_3$ growth rate must be adjusted for non-resident holdings of money market paper and short-term debt instruments, which conceptually do not form part of $M_3$ but which cannot be eliminated from the relevant statistics. At present, this upward distortion is estimated at three-quarters of a percentage point. Furthermore, the growth of the broad monetary aggregate $M_3$ is related to the comparatively flat yield curve (difference between long and short-term interest rates) and to the stock market weakness. The fact is that both these conditions enhance the attractiveness of holding short-term, liquid and interest-bearing instruments, which form part of $M_3$. However, the inflationary risks attending these portfolio shifts are relatively small, since the shifts are primarily underlain by portfolio investment motives. Finally, it should be noted that lending to the private sector, which usually constitutes a financing source for expenditure, has been gradually slowing down for quite some time. All in all, the earlier assessment to the effect that the movements under the first pillar are consistent with favourable medium-term prospects for price stability is still in full force and effect.

Developments under the second pillar clearly signalled declining upward risks to price stability. In May, year-on-year €HICP inflation peaked at 3.4%, after which it fell to 2.8% in July. In addition, recent data on economic activity suggest that this year domestic demand will increase to a lesser extent than expected earlier, thus adding to the downward pressures on inflation.

At 8.4% year-on-year in July, the Dutch contribution to the growth of $M_3$ was again high. However, compared to the preceding months, money growth slowed down in July. During that month, the year-on-year growth rate of $M_1$ declined to −1.0%. Within $M_1$, the decline in currency in circulation continued in July (−12.7%), while the growth of overnight deposits slowed down (0.5%). The decrease in currency in circulation is due in part to the running-down of cash hoards in the Netherlands and to return flows of guilder banknotes from abroad, presumably in the context of the run-up to changeover to the cash euro. Return flows from abroad mainly consist of NG 1,000 notes. In the first six months of 2001, NG 1.2 billion worth of NG 1,000 notes was returned from abroad (Chart 7), 16.0% of the total number of NG 1,000 notes returned to the Bank.

In the Netherlands, lending to the private sector

Chart 7 NG 1,000 banknotes returned from abroad

Thousands

<table>
<thead>
<tr>
<th>Year</th>
<th>First half</th>
<th>Second half</th>
</tr>
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<tbody>
<tr>
<td>1999</td>
<td>0</td>
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<td>2000</td>
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<td>900</td>
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<tr>
<td>2001</td>
<td>1200</td>
<td>1200</td>
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expanded in July by 8.7% year-on-year, against 9.4% in the second quarter of 2001. Although the growth rate for July is clearly below the figures for the preceding months, the growth of lending to the private sector in the Netherlands is still above the level for the euro area as a whole (7.6%). However, the growth differential is narrowing. The growth of other (mainly corporate) lending, which largely accounted for the high growth rates of total lending to the private sector in 2000, slowed down in the second quarter of this year, to 8.2% year-on-year, compared with 12.9% a year before. Since the end of 1999, the growth of mortgage lending has also shown a declining tendency. After a brief revival in the first quarter of 2001, this decline continued in the second quarter of this year.

**Box The significance of securitisation for credit growth**

In the Netherlands the growth of lending to the private sector has been declining since 1998. In this respect, some remarks are appropriate. The fact is that bank lending is distorted downwards as a result of securitisation of loans. Securitisation is the sale of loans to a separate legal entity (a so-called special purpose vehicle), which finances such purchases by borrowing in the capital market. Generally, securitisation means that the loans are removed from a bank’s balance sheet and, hence, from the credit statistics of the Nederlandsche Bank. In addition to bank loans to corporations, consumer credit, mortgage loans on residential property and other collateralised loans can also be securitised. In the Netherlands the predominant form of securitisation is that of mortgage loans (see Chart 1). Chart 1 shows that securitisation has expanded strongly in the Netherlands over the past few years, a tendency which has also been in evidence in the euro area as a whole. Securitisation is increasing because it offers banks a new risk management tool, reducing the amount of capital that must be held against outstanding loans. Investors in turn benefit from the resulting wider opportunities for diversification, as well as from increased supply at the long-term end of the capital market (owing notably to securitisation of mortgage loans on residential property). The expansion of securitisation means that the data on the growth of bank lending are increasingly being distorted. In the Netherlands the downward distortion of the growth of bank lending in 2000 was 0.6 percentage point of the 12.9% growth rate (see Chart 2). The downward distortion of the growth of mortgage lending is even more pronounced: 1.2 percentage points of the 13.1% growth rate in 2000. Data on securitisation in the first half of 2001 – when only mortgage loans were securitised – indicate that the distortion has increased further this year. The downward distortion of credit growth may lead to underestimation of lending to the private sector and thus of private sector indebtedness. It is from that point of view, among others, that the securitisation operations of Dutch banks are closely monitored by the Nederlandsche Bank, while the Dutch data on securitisation are also used in the Eurosystem’s monetary analysis.

**Chart 1  Securitisation of bank loans**
*(with loans being removed from bank’s balance sheet)*

<table>
<thead>
<tr>
<th>Year</th>
<th>Total</th>
<th>Mortgage</th>
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<tr>
<td>97</td>
<td>1</td>
<td>1</td>
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<tr>
<td>98</td>
<td>1</td>
<td>1</td>
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<td>99</td>
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</tr>
<tr>
<td>01</td>
<td>4</td>
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</tr>
</tbody>
</table>

Explanatory note: The data for the year 2001 are based on the first six months.

**Chart 2  Bank lending to private sector**
*Per cent changes on previous corresponding period*

Explanatory note: The data for the year 2001 are based on the first six months and have been annualised.
In that quarter, the year-on-year growth rate of mortgage lending was 10.8%, against 16.1% a year earlier. It might be noted, incidentally, that the growth figures for lending to the private sector are to some extent distorted downwards by the effects of securitisation (see the Box).

The cooling down of the Dutch housing market, already touched upon in the previous Quarterly Bulletin, would appear to be continuing. In the second quarter of this year, the increase in house prices decelerated for the fifth quarter in succession, to about 11.5% year-on-year (chart 8). Compared to the first quarter of 2000, house prices rose in the second quarter by 3.6%, whereas the quarter-on-quarter growth rate during the first quarter had been a mere 0.2%. The movements in house prices are, however, strongly influenced by a seasonal pattern. At 2.6% in the first quarter and 2.0% in the second, the seasonally adjusted quarter-on-quarter growth rate of house prices would seem to suggest a measure of price stabilisation, at a lower level than in 2000. Another indication of the cooling down of the housing market is provided by the 4% decrease (year-on-year) in the number of new mortgages on dwellings in the second quarter, while the growth of the amount involved in such new mortgages kept pace with the increase in house prices. As noted earlier, the decrease in the number of new mortgages is related to a decrease in the number of dwellings sold as well as a decrease in the number of second mortgages and mortgage renewals. Furthermore, the average number of days during which dwellings were on sale in the second quarter of this year (51) has increased substantially compared to the same period of 2000 (44 days).

Latest developments in supervision

The international economic slowdown that set in at the start of this year is reflected in the Dutch banks’ deteriorating profits. Nonetheless, the risks arising from the cyclical development are manageable since, among other factors, the institutions have an acceptable solvency level. Solvency is hence a vital point of attention for supervisors; the revision of the international rules in this area, now the subject of intense consultations, has been prolonged by a year. On a national level, a Bill governing the issuance of electronic money is in preparation. In addition, the Bank was one of the first EU supervisors to conclude an agreement with the Swiss supervisory authority on the exchange of information and mutual cooperation. A solution was found for the restrictions imposed by the Swiss banking secrecy laws. Finally, this article expands on an investigation by the Financial Expertise Centre (FEC) into money transfer activities.

Developments in the financial sector

The international slowdown in economic growth is reflected in the profits posted by the Dutch banks over the past half-year (Table 1). Growth in total earnings came to a standstill. While traditional interest earnings rose steadily, commission income declined due to the adverse conditions in the financial markets.

The moderate growth in interest earnings arises from two opposing developments. On the one hand, credit expansion has been decelerating for some time (Chart 1). The growth in mortgage lending, for example, is falling in line with the cooling-off of the housing market and a decline in the number of mortgage replacements. And the increase in non-mortgage lending is under downward pressure too. This shows that banks have become more cautious in extending credit, and also that enterprises are less inclined to invest, resulting in lower borrowing requirements. On the other hand, these volume effects are offset by the rise in the spread between long-term and short-term interest rates, resulting in an overall increase in the banks’ interest margin.

A striking development is that, although income is stagnating, operating costs for Dutch banks continue to increase, implying that efforts to improve cost control are not sufficiently effective. Now that the economy is slowing down while international competition is expected to get tougher, adequate cost control deserves all the more attention. Moreover, banks are compelled by the worsening economic conditions to increase their provisions for credit losses (‘value adjustments to receivables’), albeit that these provisions were relatively

<table>
<thead>
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<th>2000</th>
<th>2001</th>
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<tr>
<td></td>
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<tr>
<td>Net interest earnings</td>
<td>15.2</td>
<td>6.3</td>
<td>6.7</td>
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<tr>
<td>Commission income</td>
<td>23.8</td>
<td>28.9</td>
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<tr>
<td>Total earnings</td>
<td>19.7</td>
<td>17.5</td>
<td>19.3</td>
<td>0.2</td>
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<tr>
<td>Operating costs</td>
<td>15.2</td>
<td>19.8</td>
<td>20.6</td>
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<td>Provisions</td>
<td>-24.3</td>
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<td>-19.4</td>
<td>44.9</td>
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<tr>
<td>Total costs</td>
<td>11.8</td>
<td>16.7</td>
<td>17.6</td>
<td>7.2</td>
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<tr>
<td>Post-tax operating profits</td>
<td>53.7</td>
<td>21.5</td>
<td>20.3</td>
<td>-16.0</td>
</tr>
</tbody>
</table>

Source: Nederlandsche Bank.

Chart 1  Bank lending to the private sector

Changes on the same period of the previous year; per cent

![Chart 1 Bank lending to the private sector](chart1)

DNB / Quarterly Bulletin September 2001
low. On balance, total costs have gone up by more than 7% and post-tax operating profits have dropped by almost 16% in the first half of this year.

The question emerges as to the extent of the bank’s vulnerability to a further economic downturn. The main risk factor is the development of the US economy. Research undertaken by the Banking Supervision Committee (bsc) of the ESCB shows however that the exposures of European banks to debtors in the United States do not form a direct threat to the European banking sector. Individual banks may obviously be in a different position. The influence of developments in the United States on banks and other financial institutions in Europe is more likely to be indirect, stemming from the spill-over effects on the international economy. In addition, market risks could increase if exchange rates or interest rates were to fluctuate more sharply.

The banks’ exposures to emerging economies and to companies in specific sectors, notably information technology, telecommunications and related branches, also present risks. However, measured as a fraction of the balance sheet total, the exposures of the Dutch banking sector to countries such as Argentina and Brazil are quite low, meaning that the aggregated financial risk is contained. Here too, the same may not necessarily apply to specific institutions. Moreover, it is possible that the financial difficulties of an emerging economy could worsen the climate in the international financial markets and spread contagion to other countries. In the case of telecom enterprises, share prices have now fallen considerably worldwide, whereas the margins on the international bond markets, a benchmark for credit risk, have gone up. Due to the poor stock exchange climate and the specific prospects for the telecom sector, banks are generally unable to reduce their exposures to these enterprises quickly. This issue thus remains a point for attention.

Particularly if the international economic slowdown continues, a further slide in the banks’ profitability should be taken into account, also in the Netherlands. In combination with deterioration in the quality of their exposures and rising provisions, that could make banks more selective in their credit operations. The Dutch banking sector has a strong starting position, however. In recent years, the banks’ profits have risen continuously while their capital position remained at an acceptable level. All in all, the risks to the Dutch banking sector arising from the worsening economic climate can be deemed manageable.

International and national regulations

Revision of Capital Accord postponed

One of the principal focal points of banking supervision is the solvency of individual institutions, for one because a bank’s capital adequacy determines its capacity to absorb losses. The international rules in this area, specifically the Basel Committee on Banking Supervision’s Capital Accord and the relevant EU directives, are now under revision. The timetable for the completion and implementation of the new Accord was recently modified. The Committee had initially aimed to conclude a new Accord at the end of this year. However, the Committee recently decided to release a third, complete and fully specified consultative paper (CR3) to the banking sector in early 2002, most likely in March. Plans are to present the finalised Capital Accord in the autumn of 2002 and to complete its implementation in 2005.

An important reason for the postponement is that the Committee wants to give due attention to the constructive comments on the second consultative paper (CR2) which was presented in January of this year. More than 250 banks and representative organisations worldwide submitted reactions. They agreed to the proposed structure of the new Accord, comprising three pillars: minimum capital requirements, supervisory review and market discipline. An essential objective of the revision, to improve the risk sensitivity of the capital requirements, also won support. Some complex components of the new Accord need to be worked out in more detail, however, forming another reason for postponement.

One of these issues is the solvency requirements for credit risk, particularly their effect on banks’ risk management practices. The Committee wants to give banks enough incentive, in the form of lower capital requirements, to switch from a standardised approach for determining regulatory capital to a more risk sensitive, so-called internal ratings-based (IRB) approach. However, the evidence obtained by the Committee thus far shows that the incentives are still insufficient. To boost these incentives, the Committee deems it expedient to reduce the capital requirements under the IRB approach, notably for retail and corporate loan portfolios. The matter is still being researched at a number of large international banks.

Another component that will be elaborated on is the capital requirement for operational risk, which was initially set at 20% of the total minimum capital requirements. Now that banks’ operational losses have turned out to be considerably lower than expected, this
requirement can be lowered. In addition, banks will be given more scope to use their own methods to measure the extent of this risk.

Lending to small and medium-sized enterprises (SMEs) is a third point. The concern arose in some countries that SMEs could run into difficulties due to the relatively high capital requirements. The Committee subsequently decided that this lending category should be treated separately, with lower capital requirements applying than proposed in CP2. This is not unreasonable since the loans involved are smaller and hence – given the same credit rating – less risky to banks than sizeable loans to large enterprises. Furthermore, in extending credit to SMEs, physical collateral and receivables have hitherto not been recognised as risk-mitigating factors. The extent to which such recognition is feasible will be explored.

The revision of the capital requirements for credit risk, and the planned reduction of the proposed capital requirements for loans to SMEs are undoubtedly important for the Netherlands. The proposed recognition of different internal methods for calculating operational risk is in line with Dutch practice, where the large banks appear to prefer different methods. The Bank is closely involved in the Basel consultations as a member of the Committee and via the chairmanship or membership of numerous working groups.

**Electronic money and Act on the Supervision of the Credit System 1992**

Electronic money (e-money) is now an integral part of modern life. Banks began to issue chip cards in the early 1990s, leading to mounting political calls in Europe for the regulation of e-money. Last year hence saw the significance of the form of money. Expectations are high that the options for granting exemptions will be widely used in the Netherlands.

The e-money directive allows Member States plenty of scope to grant exemptions and dispensations subject to certain conditions, e.g., that each electronic storage device has a maximum storage amount of not more than EUR 150. The underlying aim is to exempt small e-money products, of relatively little importance, from the supervisory regime. During consultations on the directive, the Netherlands consistently made a case for ample scope for exemptions so that the stringency of supervision could be kept in proportion to the relative importance of the form of money. Expectations are that the options for granting exemptions will be widely used in the Netherlands.

The Minister is expected to present the Bill to amend the ASCS 1992 in accordance with the Directive to the Second Chamber of Parliament in the autumn. Consequent on the change in legislation, the Bank will exercise supervision on issuers of e-money as of April 2002. Moreover, the Bank will monitor the periodic reports of those institutions with an exemption or dispensation from the Directive. In its consultations with the Minister, the Bank has stated its willingness to take on these new tasks.

**International cooperation**

The Bank recently reached agreement with the Swiss supervisory authority, the *Eidgenössische Banken-
kommission, to formally confirm via an ‘exchange of letters’ the cooperation and exchange of information which has developed in practice. The background to this agreement is that the Bank is responsible for the consolidated supervision of Dutch banks, including their Swiss offices. Conversely, the Swiss supervisory authority bears the same responsibility for the Dutch subsidiaries and branches of Swiss banks. In their statements, both parties promise each other to exchange supervisory information. They also give each other permission to carry out on-site examinations at the offices of banks in the host country. Furthermore, the agreement allows the host country supervisor to accompany the home country supervisor to examinations conducted in the host country. Under Swiss legislation, the retrieval of data that can be directly traced to individual customers is subject to a restriction in the context of bank secrecy. During its examinations in Switzerland, the Bank is therefore unable to obtain such information directly but must apply through the Bankenkommission.

The mutual statements formally confirm the existing smooth cooperation between the Bankenkommission and the Bank. Indeed, the Bank was the first foreign supervisory authority entitled to conduct examinations at banks in Switzerland under its supervision. The Netherlands is the second country, after the United Kingdom, to conclude an agreement with the Swiss supervisor. And it is the first time that the Bank has made a formal arrangement to cooperate and exchange information with a supervisory authority from a country outside the EU and the European Economic Area (Memoranda of Understanding have been agreed on with the supervisors in all EU Member States). As well as the talks with the Swiss, bilateral negotiations on cooperative agreements are being held with supervisory authorities from other countries where Dutch banks are particularly active such as the United States, Brazil and some Central European countries.

Supervision of money transfer activities

The Minister of Finance recently published a report by the Financial Expertise Centre (FEC) on money transfers. The Bank was closely involved in drafting the report, which signalled a number of shortcomings in the current legislation and made recommendations to resolve them. Some accounts published following the FEC report gave the mistaken impression that abuses were occurring at institutions under the Bank’s supervision. Money transfer is the receipt of funds with the intention of making them payable to a beneficiary elsewhere. It is an age-old method of making an amount of money available at another place. This service is still widely used, notably in and from/to Southeast Asia, Africa and South America. The method is simple, quick and cheap. Countries in these parts of the world often lack a regular banking system capable of competing with money transfer institutions. Moreover, many countries have foreign exchange restrictions that prevent or limit the transfer of (hard) currency. Emigrants have brought this practice to the West, establishing small ‘informal’ money transfer offices, often as a sideline to exotic goods stores, parcel services and travel agencies. Besides this informal channel, large, well-known organisations such as Western Union and MoneyGram arrange for money transfers in the Netherlands via reputable supervised institutions such as Grenswisselkantoren, Postbank, American Express or Thomas Cook.

Money transfer activities are covered by a prohibition under the asc 1992 against receiving funds repayable on demand from the public or acting as an intermediary, in whatever form, for such an activity. However, the Minister is entitled to grant a dispensation. In addition, all institutions that conduct money transfers have been obliged since August 1998 to report unusual transactions to the Unusual Transactions Reporting Office (MTr). It is also the intention to make money transfer activities subject to the Identification (Financial Services) Act 1993 before the end of this year. Under this Act, institutions are obliged to record some details of their clients. The informal money transfer offices do not always have the aforementioned ministerial dispensation, however. Moreover, the supervision of this category of institutions has not yet been provided for by law.

In early 1997, the National Criminal Intelligence Service (cNI) and the MTr conducted a limited investigation into money transfers and their use for criminal ends. It emerged that some of the payors and payees had a relevant record. The FEC subsequently launched a project to examine whether institutions, which were presumed to be carrying out money transfers, were complying with the statutory regulations. In the context of this project, the Economic Investigation Service (EED) set up inquiries in 1999; in 21 cases, money transfers were shown to have been carried out by institutions that did not have a dispensation. This did not provide grounds for concluding that money transfer institutions were transferring criminal funds, but a subsequent inventory by the CRI and MTr established that this was the case. All
in all, the FEC report concluded that it was plausible that money obtained through crime was being sent via money transfers. The money transfer business is open to abuse and the available legal framework is not broad enough to ensure adequate supervision of this sector. The FEC report hence recommends the rapid introduction of statutory supervision of money transfer offices.

The Ministry of Finance is now drawing up the Money Transfer Offices Act, designed to bring the entire money transfer sector – with the exception of banks supervised under the ASCS – under supervision. The main objective of this Act is to counter money laundering. The Money Transfer Offices Act is expected to come into force in 2002. From then on, the institutions concerned will be obliged to meet certain requirements in respect of their management and submit reports to the Bank; they will be subject to cash and accounts audits. This Act will also allow for swifter action against irregular conduct. It is expected that the Money Transfer Offices Act will contribute to a reform of the sector, as did the Exchange Offices Act. Experiences with the supervision of exchange offices has shown that close cooperation between supervisory authorities and investigative agencies helps to counter money laundering effectively. Since the strict secrecy provisions have often been an obstacle in this cooperation, it would be useful to have a smoother exchange of information – obviously with due procedural safeguards – during the introduction and implementation of the Money Transfer Offices Act.

1 See also the section on the significance of securitisation for credit growth elsewhere in this Quarterly Bulletin.
Current developments in payments and securities systems

In the run-up to e-day, the banknote circulation has declined further during the past few months. Preparations for the changeover operation have entered the operational stage, a matter discussed in detail by an article elsewhere in this Quarterly Bulletin. The banks and Interpay play an important part in the transition, which is why their preparations are monitored closely by the Bank. A milestone was the date of 1 July 2001, by which the banks were required to be technically ready for the conversion of the mass non-cash payment systems from guilder to euro, and to have finalised plans for their share in the cash changeover. On the whole, this deadline was met successfully.

In July, the Minister of Finance sent the Second Chamber of Parliament a memorandum about the market for non-cash means of payment, which concluded that payment systems in the Netherlands are on a high qualitative level. Through timely implementation of further adaptations and the utilisation of technological possibilities, our country can maintain its qualitative edge for the future. The transition to the euro in consumer payments reinforces the pressure to improve the cross-border payment of small amounts within the euro area. The banks have taken up the challenge, in cooperation with the Eurosystem. Bottlenecks to be removed include the differences between national systems and the small volume compared to domestic payments. The European Commission has decided not to await developments and has issued a draft regulation ordering the banks to level the costs of domestic and cross-border transactions in euro. This proposal ignores the complications mentioned above and the time needed to implement improvements.

Over the past months, the Bank, in its capacity of overseer of clearing and settlement systems and payment products, and the Securities Board of the Netherlands together assessed the settlement systems of Necigef, the Dutch securities settlement institute and depository with regard to, among other things, operational reliability and risk management. As a consequence of the formation of Euronext, Necigef is to merge into Euroclear, the international securities settlement and depository institute. This takeover will be reviewed by the central banks and securities commissions of the countries involved.

Developments in banknote and coin circulation

As the cash changeover is drawing closer, a decline in the circulation of banknotes is becoming more and more manifest. By the end of August 2001, the number of banknotes had declined by 6.6% compared to the corresponding month of the previous year; the value had come down by 14.2% to NLG 31.9 billion (EUR 14.5 billion); the circulation value had not been this low for fifteen years. In other euro area countries, the value of the banknote circulation decreased as well. By end-June 2001, the value of circulating banknotes in the euro area had come down by 3% compared to end-June 2000, to EUR 332 billion.

The most likely cause of the decline is the reduction of dormant cash holdings by the public: the decline of the circulation is most marked in the highest two denominations, which for the most part have been hoarded by the public. By end-August 2001, the number of NLG 1000 and NLG 250 notes had declined by 22.6% and 19.1%, respectively (Chart 1). The decline in the number of circulating NLG 100 and NLG 50 notes, by 8.0% and 9.1%, was also notable.

As the circulation of banknotes falls off, the flow of guilder notes from abroad has swelled. Most guilders returning from across the border come from other euro area central banks, which under Section 52 of the ecb/escb Statute are required to exchange banknotes spent elsewhere in the euro area at the official conversion rules. The majority of these 'Section 52 guilder notes' (86%) arrive from Germany, where commercial banks and foreign exchange offices may exchange foreign currency from the euro area at any of the 135 Bundesbank branch offices.

If a strong decline in the issue of the NLG 1000 has been going on for many months (12.2% down by end-August on the same date of the previous year), the issue...
of NLG 50 notes has also begun to decrease. Total issues and returns, however, continue to grow: ever larger flows of banknotes pass through the Bank because the banks increasingly return the notes they receive to the Bank through their regional banknote sorting centres instead of recirculating them.

A decline in the coin circulation has now also set in. For the first time in a decade, the number of coins in circulation has fallen off, by 0.9% against the corresponding period last year. Equally without precedent in the past several years, the value of the coin circulation decreased by 4.2% compared to end-August 2000, as a result of a decline in demand for the highest two denominations. Of the NLG 5 and NLG 2.50 denominations, respectively, 8.4% and 6.9% fewer coins were in circulation by the end of August than by the same date of the previous year.

Preparations for the introduction of the euro

Preparations by the financial core infrastructure
For the largest ten banks and Interpay, which together with the Bank constitute the financial core infrastructure for payments in the Netherlands, 1 July was a major milestone on the road to the introduction of the euro. It was the date by which these institutions were required to be ‘technically ready’ for the changeover in the mass non-cash payment system and for the introduction of euro notes and coins. In practice, this meant that all computer hardware and software and all peripheral appliances and equipment had to have been adapted for the euro; in the case of conversions which by their nature had to take place by a later date, such as the changeover weekend, preparations had to be fully completed before 1 July. That same date was also the deadline by which plans for the cash changeover had to be finalised, such as schedules for activities at branch offices around E-day and arrangements with cash-in-transit services about the supply of bank branches and the stocking of ATMs with euros.

The Bank has been closely monitoring the preparations. Both the consultations which the Bank held in July 2001 with the institutions involved and the written information it received, showed that the financial core infrastructure was all but technically ready by the required date. Only limited adaptations and some testing activities remained to be finished, which happened soon after 1 July. Plans and schedules for the cash changeover, which were finished in outline, still had to be elaborated in more detail. The delay was owing to the fact that some decisions about the cash changeover scenario, such as the distribution of consumer starter kits and the compensation for the extra cost of cash transportation, had to wait until a fairly late point in time. The cash changeover is described in detail elsewhere in this Quarterly Bulletin. Complicating the logistical planning of the cash changeover is the fact that it concurs with branch network reorganisation and/or downscaling projects undertaken by some of the largest banks. This issue deserves extra attention and the Bank will put it on the agenda for the next round of consultation.

From the preparatory stage we are now moving into the operational stage. From 1 September 2001, the front-loading of euro notes and coins to banks and businesses has been allowed, and as the year runs out, the mass conversion of accounts and customer contracts will gain momentum. The transition is marked by a drive to identify the risks involved in the operational stage and with formulating measures to deal with any operational problems that may arise. Also, milestones are set along the time path running from 1 December 2001 to mid-February 2002 by which the Bank may monitor the progress of the euro changeover. A communication and coordination framework is being set up for this purpose.

Preparations in the business world
Like the banks, the rest of the business world (and the government) must also prepare for the euro changeover. Elsewhere in this Quarterly Bulletin, the results of the Euro Survey are presented, picturing the rate at which preparations are progressing. One of the issues is the adaptation of EFT-POS terminals, which are to play an important role during the changeover period, because the use of EFT-POS terminals by consumers will reduce the amount of cash at points of sale. Also, the terminals in shops may, occasionally and locally, act as fallback alternative if a shortage of cash should occur.

The number of orders for EFT-POS terminal adaptations has again gone up. By mid-August, measured by the number of PIN transactions handled by the terminals involved, the percentage of terminals for which orders had been placed was approximately 95. Between end-May and mid-August, the number of euro-ready EFT-POS terminals (both debit card and combined debit card/prepaid) increased from 83,000 to 123,000 (Chart 2), or from 50% to 79% of the total number. Medium-sized and small businesses, too, have by now had most of their EFT-POS terminals converted, despite complaints from this sector about, in some cases, steep conversion
costs. The broader issue of tariff structures for electronic retail payments is at the moment being investigated by a Working Group on Tariff Structures and Payments Infrastructure. If suppliers keep up their present effort, the terminals for which orders have now been placed will still be converted in time. Unconverted terminals will cease to function on 1 January 2002. In most cases, these are terminals which either have already been in disuse or will no longer be needed in 2002.

Other preparations include the switch to euro-compatible file formats for electronic payment systems. Banks and Interpay have made every effort to persuade customers using electronic payment delivery forms to make the switch in time, but the business community has been slow in responding. The probable cause is that most of the businesses involved prefer the switch to coincide with the introduction in December of the euro inpayment transfer forms in their invoicing systems. Yet few distributors of euro inpayment forms have used the opportunity offered by Interpay to test these forms. This means that any shortcomings in either means of payment will be late in manifesting themselves, which constitutes a risk to the success of the euro changeover in mass non-cash payments. The Bank will therefore pay extra attention to these matters in the coming months.

In some cases it will be either difficult or highly expensive to provide, in early January, payment data in euro generated on the basis of this year’s guilder-denominated financial administrations. Therefore arrangements have been agreed within the framework of the National Forum for the Introduction of the Euro where certain types of payment orders may be presented in guilders until 28 January 2002. Starting that date, doing so will require special exemption by the Minister of Finance.

**Domestic retail payments**

Mid-July, the Minister of Finance sent a memorandum Betalingsverkeer: de markt voor girale betaalmiddelen (‘Payments: the non-cash market’) to Parliament. This memorandum discusses the issue of whether the non-cash payments market is producing the desired outcome. To this end, three policy objectives are formulated regarding safety, efficiency and consumer benefit. The main conclusion is that, generally speaking, the objectives are being satisfied and that therefore the market mechanism is functioning adequately. The memorandum finds that prices for holding a checking account in the Netherlands are relatively low; that non-cash payment processing is highly efficient; and that the utilisation rate of these efficient means of payment in the Netherlands is relatively high. In recent times, further improvements have been initiated. The Bank
and the Ministry of Finance have come to agreements with the banks about payment order processing times and stating value dates on account statements. Also, a covenant was agreed guaranteeing access to checking accounts, in particular for the homeless. Remaining room for improvement, as identified by the memorandum, is in research into tariff structures and infrastructure, payment market dynamics, the accessibility of the payment market to new players, possibilities for consumers to move between banks while retaining their account number and payments via the Internet.

Besides the issues mentioned by the memorandum, the cost effectiveness of payment systems should also be a matter of concern in the coming period, if the continuation of the present level of service is to be guaranteed.

As regards the accessibility of the payments market, the memorandum announces an investigation to be held into the possibilities for and effects of opening up the payment products market to non-bank players such as insurance and telecom companies. The investigation should reveal whether increased accessibility of the payments market will enhance market dynamics. It will also include safety aspects. If the outcome is positive, a discussion about opening the market should be initiated at the European level. As a further comment it should be remarked that while enhanced accessibility may encourage competition, it must in all cases serve the ultimate objective of safety and efficiency in payment systems.

The basic ideas underlying the decision to investigate the possibilities of opening up the payments market are also expressed in a CM Finance report, commissioned by the Ministry of Economic Affairs and published in early 2001, ‘Nederland in de grote dynamiek van elektronisch betalingsverkeer’ (‘The Netherlands in the larger dynamics of electronic payment systems’). This report is important because it is the first comparative study of the Netherlands’ electronic payment systems in an international setting.

The report is centred around the question how well the Dutch financial sector is performing internationally when it comes to electronic payments, both between banks and from the banks to private and corporate customers v.v.. The Netherlands is found to be positioned favourably in a group of adequate but medium performers.

This comes as something of a surprise, because in some respects, the Netherlands is performing very well in an international comparative context. The main factors positioning the Netherlands lower down in its league than expected are the dynamism and adaptability of the payments sector – factors which are hard to quantify objectively. The Netherlands has traditionally been a ‘giro country’. Over the past few decades, large amounts have been invested in the payment systems’ infrastructure, which is now highly efficient, especially in an international context. The Netherlands is in the forefront, for instance, where the transition of paper to electronic payments and the automation of payment processing and of clearing and settlement systems is concerned. While the report does discuss this matter, it is not translated into a balanced assessment. The decisive criterion by which the sector’s dynamism is measured, for instance, is the number of recent initiatives to improve the payment system. This approach favours countries that work hard to eliminate relative disadvantages, such as the United States, where (paper) cheques are used on a massive scale.

It is also good to remember that there is no single best way to organise a payment system. Countries may differ in many respects including the initial situation, competitive relationships, the level of technological development, or the level of government interference. While such differences are touched upon by the report, they do not affect its final conclusions. An interesting point in the report is the importance it attaches to standardisation. The desirability of uniform standards is endorsed by the Bank. A uniform infrastructure is a network whose usefulness increases with the number of users. Service providers may compete in the sphere of the products and terms they offer to consumers. The Netherlands’ poor performance in the report is owing to a lack of standards, especially in the ‘front office’. An important recommendation the report makes is that the government and the sector should make every effort to establish common standards. This has also been one of the Bank’s key policy issues. It should be borne in mind, however, that introducing a standard is possible only if a (clear) majority of market players is convinced of its adequacy and effectiveness, and insofar as standardisation agreements do not run afoul of antitrust legislation. The central bank may play a stimulating role in the process.

The cost of cross-border payments in Europe

With the introduction, on 1 January 1999, of the euro as the common currency of countries participating in the Economic and Monetary Union, the elimination of exchange rate fluctuations fulfilled one precondition necessary to facilitate cross-border payments in the euro area and to make them less expensive. For large-value
payments, such as those initiated by financial institutions, cross-border settlement systems providing rapid and inexpensive settling of cross-border payments have indeed been created. For retail payments (up to EUR 50,000), however, this is not yet the case. This is the outcome of a survey carried out in March 2001 by order of the European Commission, following on an earlier, similar survey carried out in 1999. The report presents the results of 352 transactions in each of which EUR 100 was transferred between banks in the euro area countries (with the exception of Greece). The survey also extended to the cost of using debit and credit cards abroad and the cost of withdrawing money from ATMs in other countries than one’s own. Of the survey’s results, those relating to the cost of credit transfers attracted the most attention, because they showed that transferring sums of money had actually become more expensive than it had been two years ago (Chart 3). The average charge for the transfer of EUR 100 to another euro area country was EUR 17.36 (in 1999: EUR 17.10). Dutch banks charged EUR 11.45 on average (1999: EUR 10.00), which is relatively inexpensive in comparison to banks in other countries. The survey also found that in some cases, the processing time was longer than the six working days allowed by EU regulations.

Although the survey was limited in scope, the number of transactions being so low that only tentative conclusions could be drawn, the findings prompted an initiative by the European Commission to improve the situation at short notice. It proposed a draft regulation to the effect that no difference in cost may exist between domestic payments in euro and cross-border payments up to EUR 50,000. For payments by debit or credit card (POS payments or ATM withdrawals), the regulation is to become effective on 1 January 2002; for transfers on 1 January 2003. The process leading up to the adoption of the regulation has by this time been launched.

The European banking community has firmly rejected the draft regulation, if only because forced pricing would conflict with the principle of free competition in an open market economy. Moreover, it will create different points of departure for banks in each country because in countries where banks charge their private customers for domestic payments, they will be able to do so for cross-border payments, too; whereas in countries where domestic payments are free, such as the Netherlands, cross-border payments will also have to be offered free of charge. Therefore it cannot be ruled out that as a result of this regulation, fees will be charged on domestic payments in our country as well.

The Bank also has its reservations about the way the regulation has been formulated and the timing of its implementation. When in 1999, in accordance with European Commission’s findings, it had been recognised at the ECB level that cross-border payments were processed in a considerably less efficient manner, and were therefore more expensive, than domestic payments, the ECB was quick to launch consultations with European banks. The resulting dialogue should lead to considerable improvements in 2002. The ECB is aware, however, that the volume of cross-border retail payments is only a tiny fraction (about 0.5%) of that of domestic payments, whereas the payment systems in

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**Chart 3  Costs of cross-border money transfer**

In euro

![Chart 3 Costs of cross-border money transfer](image)

Note: European Commission survey results, based on a limited number of EUR 100 payments.
different countries are built to various automation standards, leading to structurally higher cross-border settlement costs. Making improvements will inevitably take time. One issue taken in hand is the introduction of an International Bank Account Number (IBAN), allowing the automatic and therefore less expensive processing of payments. For the IBAN to be successful, however, the business community will have to cooperate and, for instance, print IBANs on invoices et cetera. All in all, such a market oriented approach seems preferable to the regulation favoured by the European Commission. The Dutch banks have already begun to issue IBANs to their customers. Customers who so wish, may apply for an IBAN via the Internet.

**Oversight of payment and settlement systems**

*Securities settlement systems*
In the period under review, the Bank’s oversight of the Dutch stock exchange’s clearing and settlement systems concentrated on the systems processing the final transfer of securities and money, called settlement. In cooperation with the Dutch Securities Board, STE, a comprehensive assessment was performed on the settlement systems of Necigef, the Dutch securities depository. The assessment was based on the criteria formulated in the Oversight Framework Clearing & Settlement Euronext. Items included in the assessment were the systems’ operational reliability, the contractual relationships between Necigef and the institutions affiliated with it, and the risk management observed by Necigef. The outcome of the assessment was that Necigef had to make some improvements to the systems.

In late July, Euronext, the shareholder of Necigef, arranged with Euroclear SA to sell Necigef to that Belgium-based international settlement organisation. This share transfer brings the further integration of the Belgian, French and Dutch settlement systems a step closer. For the Dutch securities market, the sale of the Dutch depository will be a major step. The Bank and STE therefore are to perform a thorough assessment of the institutional and operational consequences, involving the Ministry of Finance as well.

The sale will also be examined by the overseers in Belgium and France. Since a coordination of efforts is desirable, the Bank and STE have taken a joint initiative to conduct a coordinated assessment, together with their foreign counterparts, in all three countries. As a part of the assessment it will be determined what shape the oversight of settlement systems in the three countries should take after the sale, and what cooperative agreements between overseers and supervisors will be required. The assessment is scheduled to be completed before the end of October 2001.

**Oversight framework of payment systems and payment products**
For the oversight of interbank retail payment systems and payment products, a separate Oversight Framework has been formulated, delineating the assessment by the Bank of payment systems and products. The methodology adopted by the Framework conforms to international standards and resembles closely the Oversight Framework Clearing & Settlement Euronext formulated for the clearing and settlement systems used by the Dutch stock exchange. It is, moreover, in line with the intended structure of the Act on the Oversight of Clearing and Settlement Systems (Wta) now being prepared.

The Framework opens with a general explanation of the Bank’s oversight tasks regarding interbank retail payment systems and products, after which it proceeds to detail the oversight of Interpay, the principal manager and operator of these systems and products. Subsequently, the technical and operational procedures are explained, in particular the performance of risk analyses and assessments and the analysis of documentation and of the periodic reports sent to the Bank. Also included in the Framework are general assessment criteria for the oversight on Interpay’s payment systems and products. Primarily, these are criteria applying to particular systems or products. But some are criteria applying to the manager of such a system or product, or even to its participants or users.

**Assessment of payment products**
Developments in the field of new electronic payment products move at a fast pace and in a highly competitive market place. The overseer, in carrying out its primary task of ensuring the adequate operation of a safe and reliable payment system, must monitor relevant market developments and assess new relevant initiatives with regard to payment products, before they appear on the market. In doing so, the Bank aims to ensure that the prospective supplier of a new product takes adequate measures to manage the risks attaching to it. These may be risks posed to the supplier itself, to the consumer or to the payment system as a whole. Whether initiatives will be assessed within the framework of oversight is determined by, among other criteria, the expected size of a new product’s market, the proportion of its inherent risk and its innovative qualities.
Articles
A closer look at European economic policy coordination

The well-functioning of the Economic and Monetary Union (EMU) is conditional upon an appropriate process of policy coordination. During the 1991 negotiations on the Maastricht Treaty, this was a constant focus of attention, the central question being: How can we ensure that EMU, with a centralised monetary policy conducted by the European Central Bank (ECB) and decentralised fiscal, social and economic policies, will generate satisfactory macroeconomic results? This article discusses how the framework for policy coordination works out in practice, presents an assessment of that framework and suggests possible improvements. It also looks at several recently launched ideas for stepping up economic cooperation in Europe.
Introduction

On 1 January 2002, the introduction of euro banknotes and coins will be the final step in the process of monetary union of the euro area. By comparison with monetary union, the ultimate goal of economic union is less well-defined. On the one hand, there is the clear objective of creating a single market for labour, goods, capital and services, while on the other, economic union also means increasing cooperation with regard to fiscal, structural and employment policies. For the time being, policy decisions in these areas will continue to be national responsibilities. In other words, the 'e' in theEMU has not yet taken the shape of the centralisation and harmonisation which marks monetary policy and the completion of the single market. Instead, a wide range of procedures has been created over the past few years with the aim of reconciling economic policies; this process is known as economic policy coordination. This subject will be the main focus of the present article, which will deal with questions such as how economic coordination works in practice and what needs to be improved. It will also take a brief look at communications between the monetary and the budgetary authorities.

Why coordinate economic policies in Europe?

There are three reasons for coordinating economic policies in Europe. The first is the necessity to provide the Monetary Union with a sound foundation. Take, for instance, the necessary limitation of national policy discretion in respect of fiscal policy. Within theEMU, a rising government deficit in one Member State, attended as it would be by inflationary pressure, could negatively impact the entire euro area because it would make interest rates go up, and hence make it more difficult for theECB to conduct its monetary policy.

Policy coordination can also compensate for the negative spill-over effects of economic integration. The Member States of theEMU are being increasingly confronted with the cross-border effects of their partners’ economic policies. Such interaction can have both positive and negative spill-over effects. On the one hand, healthy policy competition stimulates a continuous improvement of Member States’ policies, because policy errors are corrected by competitive forces. Harmful policy competition, on the other hand, can undermine policy across the board. Healthy tax competition is, for instance, in evidence when a low-tax country produces more efficient or fewer facilities than one with higher tax rates. There is unhealthy tax competition when countries do not compete on the basis of their real economic fundamentals, but aim their policies notably at tapping each other’s tax flows. By reconciling economic policies only where absolutely necessary, countries can make optimum use of the advantages of policy competition; moreover, the potentially negative spin-offs of economic integration are thus kept to a minimum.

The last rationale for coordination is the increasing realisation that Member States can benefit from exchanging information about their respective policies and performances. The heterogeneity of theEMU Member States and the ensuing diversity of their policy decisions offer opportunities to learn from each other’s successes and failures.

What does policy coordination in Europe actually entail?

The European Central Bank (ECB), the Finance Ministers and the European Commission meet regularly to discuss monetary and fiscal policy. The objective of these meetings is to exchange information with a view to optimising decision-making doing full justice to the Treaty-based responsibilities of all concerned; this means, for instance, that because of theECB’s independence, theECB and the budgetary authorities cannot be forced to make policy commitments in advance.

Economic policy coordination within theEMU notably takes the form of consultations between the European Council of heads of state or of government, theEU Ministers of Finance (theECOFIN Council) and the informal meeting of the Ministers of Finance of the euro area (Eurogroup). The Ministers keep each other abreast of their policies, discuss international developments and work out a balanced policy mix in respect of fiscal policy, structural reforms and a sound development for wage costs. On a recommendation of the European Commission, the resulting European policy intentions are subsequently laid down every year by theECOFIN Council in the Broad Economic Policy Guidelines (BEFGs). The details of these guidelines are worked out in four underlying coordination procedures:

- To begin with, the Stability and Growth Pact. Under this Pact, the Member States are held to strive for a budgetary position in the medium term which is close to balance or in surplus. Over the business cycle, the budget can move flexibly in tune with economic develop-
ments. This is known as automatic stabilisation. Building up a budget surplus when economic conditions are favourable creates scope for a rise in government spending (notably unemployment benefits) when the tide turns and for the option not to compensate for tax setbacks, even when this means a small budget deficit. The upper limit for a government deficit is formed by the norm provided for in the Maastricht Treaty, a deficit of at most 3% of GDP within the framework of the excessive-deficit procedure. The Member States have also agreed to make allowance in their current fiscal policies for developments which will be making themselves felt in the longer term, such as population ageing. The Member States report recent budgetary developments and present their plans for the near future in a Stability Programme, published annually.

• The process of Luxembourg: This procedure concerns the implementation of the European employment strategy. In this context, every Member State must draw up a National Employment Action Plan annually, setting out the efforts made by the various national agents (including the social partners) with regard to employment, the labour market and training.

• The process of Cardiff is intended to encourage structural reforms of capital and product markets. These reforms, which must be presented in a progress report, cover a broad spectrum ranging from competition policy to reform of the tax system and access to risk capital.

• The process of Cologne relates to the macroeconomic dialogue between the European Ministers of Finance and Social Affairs, the European Commission and the ECB, on the one hand, and the European employers’ organisations and trade unions, on the other. The dialogue is intended to be a proper exchange of information on fiscal policy, wage movements and price-stability-oriented monetary policy.

In Lisbon in the spring of 2000, the European Council furthermore decided to create a concrete plan aimed at improving the competitiveness of the European economy, partly in reaction to the American ICT performances of the past few years. This plan relates mainly to structural policy; structural indicators have been drawn up to facilitate comparison of the EU Member States.

The survey shows that economic policy coordination is mostly an intergovernmental affair. The ultimate decisions on most components of social and economic policy are taken by the Member States. It should be noted, however, that the European Commission plays a major initiating and supporting role in all procedures. It often sets the tone by assessing and publishing the Stability Programmes. It also draws up the draft pro-
posals for the conclusions eventually adopted by the ecofin Council, a procedure intended to guarantee the consistency of the ultimate policy recommendations.

How compelling are the various coordination mechanisms?

The policy coordination framework for emu was intended to strike a balance between the pros of policy coordination and the cons attending some loss of national sovereignty. The resulting system encompasses different forms of policy coordination for different policy areas. The greater the need for policy coordination, the more compelling the procedures and the more powerful the sanctions. The heaviest sanctions apply to fiscal policy (under the excessive-deficit procedure). A Member State with a deficit which threatens to exceed the 3% limit may be given a recommendation by the ecofin Council to adjust its policy. If the Member States fail to take action, it may eventually have to pay a penalty in the form of a non-interest-bearing deposit held with the ecb. Recommendations pertaining to the other coordination procedures are less strict and should be seen as incentives rather than sanctions. They are more a form of peer pressure. A Member State whose economic policy is not in the general interests of emu may be pressurised by the other countries to adjust its policy. The peer pressure method is currently being applied in the process of Luxembourg and the broad guidelines. The instrument of a country-specific recommendation given in the framework of the broad guidelines was applied for the first time this year, when in the spring the ecofin Council censured Ireland for conducting a pro-cyclical fiscal policy.

The processes of Cardiff and Cologne do not provide for sanctions, and are hence less compelling. Here successful policy measures are identified with the aid of benchmarking – an instrument also used in the other procedures – of each other’s performances and the selection of best practices.

How successful is the current coordination model?

The current European coordination mechanism has so far generated fairly successful outcomes. To begin with, the monetary and budgetary authorities keep in close touch by attending each other’s meetings. It is important that their communications to the outside world be characterised by uniformity. The macroeconomic dia-

logue in which the social partners take part contributes to greater understanding between the various players in Europe. Open and informal consultations give policymakers the opportunity to vent their ideas, to learn from national experiences and to explain their intentions. Where the coordination of economic policies within the framework of the broad guidelines is concerned, cautious optimism is in order, thanks especially to the independence demonstrated by the European Commission. Its objective assessment ensures that all Member States threatening to damage the common interest are actually criticised. Also, an increasing level of consensus has gradually arisen among the Member States about the importance of structural reform.

So far the results in terms of budgetary outcomes can be considered positive. At the time of the negotiations leading up the Maastricht Treaty, uncertainty abounded on whether the Member States would be able to meet the convergence criterion of a budget deficit not exceeding 3% of gdp. In the meantime, many Member States have succeeded in attaining a budget surplus, while the government debts of all eu countries are undergoing a structural decline (Chart 1). In other words, the single monetary policy has not been thwarted by the ‘e’ in emu. Continued consistent and strict compliance with the requirements of the Stability and Growth Pact is, however, a sine qua non. Over the past few years, the coordination framework benefited from favourable overall economic conditions. In this respect, the monitoring of recent fiscal developments and the assessments of the
stability programmes of the large EU countries in particular – which will take place in the course of this year – will prove an important litmus test. The quest for and realisation of a budgetary position close to balance or in surplus continues to be of major importance if automatic stabilisation is to operate freely.

Where the other economic policies, and especially the structural reform of labour and product markets are concerned, much remains to be done in Europe. This has been noted before, by both international organisations and central banks. To the question whether the current coordination framework – with a central role for the broad guidelines – suffices, the answer is ‘yes’. The current model rightly places the responsibility for the implementation of policy with the Member States. Given the structural differences between the Member States and the fact that adjustment mechanisms which are successful in the United States (such as labour mobility) cannot be deployed in the EU, social and economic policy is best conducted at the national level. Here, coordination consists mainly of comparison, with the aim of identifying best practices. Further harmonisation seems unnecessary. The introduction of minimum social standards (minimum wages, social security) and the centralisation of structural policy – for instance, in the context of a level playing field or social cohesion – would only introduce elements of inflexibility. This does not mean, however, that the qualitative minimum standards agreed in Europe should be abandoned. It is gratifying that all Member States have minimum wages and social security, but harmonisation of their levels would be detrimental to economic dynamics and would not be in the interests of Europe.

Here a problem arises: coordination may not be an excuse for failing to take action. As a small, open economy, the Netherlands only stands to benefit from the well-functioning of other countries’ labour and product markets. The current, mild forms of coordination make allowance for the different institutional structures and the responsibilities of national governments and social partners. It is imperative, however, that the proposed measures are actually carried out. Peer pressure is called for because countries feel the consequences of structural problems elsewhere. But countries can also learn from each other via the best-practices method. There is much to be said for the current system of policy coordination, the motto being: policy competition where possible, policy coordination where necessary.

Any judgment on just how well the current coordination methods work must take into account that the model is still under development. On the basis of the experiences of the past few years, several adjustments have already been made. As described in the previous section, the policy recommendations have increasingly come to focus on structural policy, with a concrete plan to improve Europe’s competitiveness. In addition, the broad guidelines are increasingly addressed directly to the Member States. We know from experience that the milder coordination mechanisms are not powerless.

Take the official reprimand given to the Irish government by the Ecofin Council under the broad guidelines in the spring of this year. This is a good example of peer pressure; although the results will become visible only in the longer term, a major step was taken in that a country was reprimanded for conducting a policy which is not in the interests of the Union as a whole. The procedure has thus been given more clout. This will prompt the other Member States to try to avoid a public reprimand. The efficacy of the coordination process on the basis of peer pressure will have to prove its worth over the next few years. It is essential that the system be sufficiently sound to guarantee equal treatment of all Member States, the large ones included.

Can the system be improved?

In addition to the above remarks, there are various issues in terms of both procedure and substance which need to be addressed in the context of the further development of the coordination framework. The framework’s transparency is a case in point. As a result of the adoption of the ‘Lisbon agenda’, some policy areas are now doubly coordinated, a development which does not enhance the clarity of the procedures as a whole. It has therefore become extra important that commitments and intentions be properly evaluated: do the Member States really adhere to their commitments? So far consistency is guaranteed by the high quality of the assessments made by the European Commission, and the fact that the Commission does not hesitate to publish them. However, the number of procedures and the complexity of policy coordination must not increase further. The various procedures must not cause segmentation, but should help to deepen the joint policy intentions set out in the broad guidelines. Continued attention will have to be paid to the reconciliation of the new ‘Lisbon’ action plan providing for structural indicators and the existing coordination process for structural policy (the process of Cardiff).

Care must furthermore be taken to ensure that the
increased number of coordination procedures does not distract attention from the policy issues themselves and the priorities set. Structural reforms of the labour market must continue to figure prominently on the agenda. At this juncture, policy efforts within the EU (including those made in the context of the process of Luxembourg) are mostly aimed at boosting the number of jobs, whereas the labour market would be better served by a greater focus on the supply side. Reduction of the mismatch between labour market supply and demand, and stimulation of labour mobility have so far figured relatively insignificantly in the EU countries’ labour market policies.

Finally, it should be stressed once again that, apart from a sufficient degree of national economic flexibility, the Monetary Union is best served by the completion of the single market, the result being a well-functioning market economy spanning the entire euro area. This element tends to be overlooked in the discussion about the future of Europe and the need for a ‘new policy’. Regrettably, the single market has not yet been completed. Originally, the project was to have been finished before EMU set off. Where the next few years are concerned, it is essential that recent proposals – such as the Lamfalussy plan and the European Commission’s Financial Services Action Plan aimed at boosting capital market integration – be carried out promptly.

Developments in the longer term?

In Europe, the future of the EU is the subject of much debate, prompted by the growing interwovenness of the EU countries, the planned enlargement of the EU with mainly central European countries and the lack of affinity with Europe felt by many individuals. In brief, the debate centres on two issues, viz. form (what institutional structure should the future enlarged EU have?) and substance (with what policy areas should the centre in Brussels be involved?). It is important to keep in mind the interrelationship between the form and substance of the future integration of Europe. Although the national standpoints in this debate have not yet fully crystallized, a divide seems to be emerging. Some countries, including Germany, are in favour of an institutional leap forwards which should eventually lead to a ‘European core group’ with a full-fledged government and parliament. However, they wish to limit the European policy agenda to those core areas (foreign policy, criminality, the environment) which usually belong to the mandate of a federation’s centre, while the Member States or other regional authorities remain responsible for all other policy areas. The other countries, which include France, do not desire unduly large institutional shifts, but do advocate intensified cooperation in a large number of policy areas, with the Member States retaining their powers of decision.

Consequent on the broader discussion of the future of ‘Europe’, the French Prime Minister, Mr Jospin, the Commission’s Chairman, Mr Prodi and the Belgian Minister of Finance, Mr Reynders, and others, have commented on the desirability of greater economic policy coordination. However, they did not explain in detail what the objective should be and how it should be attained. As yet there are no concrete and detailed plans for reform of economic policy coordination. However, the comments had several elements in common. Two of these – the call for an economic government and the creation of an economic stabilisation fund to support Member States confronted by an asymmetrical shock – are discussed below.

A closer look at the call for the creation of a European economic government with far-reaching competences reveals up widely diverging views on the shape of such a government. The French hold that an economic government should not entail an institutional transfer of decision-making powers (no federation), but maintenance of the Member States’ powers preferably within the intergovernmental framework of the euro group. Mr Prodi is in favour of a far-reaching concentration of economic powers (federation), with the European Commission fulfilling the role of ‘government’. In order to be able to make policy, such a government would have to have tax revenues at its disposal; the Commission therefore advocates the introduction of a euro tax. A European tax would furthermore narrow the distance between the EU and its citizens.

The views of those who favour a marked increase in economic cooperation, albeit within the existing institutional framework, harbour a tension. This tension is most apparent in the threat to the position of the small Member States posed by expansion of economic policy coordination within the current institutional structure. If the common element in decision-making is not reinforced, an unduly large amount of power could be concentrated in the large Member States. Unless Member States are actually prepared to transfer competences to the supranational level, economic cooperation will remain more or less as it is. Should the EU countries really wish to create common competences with regard to social and economic policy, then they would have to accept a competence structure at com-
munity level, with a truly European government and a full-fledged parliament.

The second element which regularly emerges in discussions on stronger economic cooperation is that of a macroeconomic stabilisation fund. The call for such a fund seems ill-advised, for three reasons. First of all, its economic necessity may be disputed. Those in favour of such a fund question the options open to European governments to react adequately to economic shocks. Here a parallel can be drawn with the United States. The differences in adjustment mechanisms between the EU and the United States have been extensively discussed in the economic literature; it appears that the system of automatic stabilisation in the European Stability and Growth Pact has a stabilising impact similar to that of the United States’ federal budget policy. This means that in order to stabilise the economy a monetary union does not need to have a federal centre with a relatively large budget. In a recent ECB Monthly Bulletin it is furthermore noted that ‘The current fiscal rules in the EU provide the appropriate framework for preserving sound and stability-oriented public finances.’ To this end, however, the European governments will have to persist in their quest for a budgetary position close to balance or in surplus in the medium term, where automatic stabilisation can operate freely. Whatever happens, the unfavourable cyclical conditions which may lie ahead should not prompt the creation of a stabilisation fund.

The second argument against an economic stabilisation fund is underlain by experiences with such a mechanism in the United States. Formally, the American Administration has the power to actively stabilise the economy of some part of the country which is suffering from an asymmetrical shock with the aid of specific federal funds transfers. So far the Administration has made hardly any use of this instrument, in part because the need for a fiscal stabilisation mechanism rarely arises, but also because of the major practical drawbacks attending effective use of this instrument. The first and most important federal stabilisation experiment was set up to absorb the regional impact of the recession of 1974-75. The main problem turned out to be how to time the payments. When the first transfers were actually made, the recession was in fact already over, and the payments subsequently had an undesirable pro-cyclical effect. It furthermore proved difficult to measure, define and time the need for aid, and not to thwart incentive structures. In the worst-case scenario, local authorities anticipating a possible federal transfer will be stimulated to cut down on their spending and conduct a pro-cyclical policy.

The third objection to a stabilisation fund in the EU is that it would undermine the foundation of the no-bail-out clause contained in the Stability and Growth Pact. The creation of a support fund for EU Member States facing heavy economic weather would thwart the incentives provided for by the Pact to strive for budgetary discipline, if a Member State with a budget deficit in excess of 3% would qualify for support rather than a penalty.

**Conclusion**

*This article discusses the functioning of the European system of policy coordination on the basis of two key questions: does it suffice and how could it be improved?*

Where the first question is concerned, the current economic coordination framework, anchored in the Stability and Growth Pact, has so far yielded fairly satisfactory results, notably in terms of public finances. The ‘e’ in EMU has not thwarted the single monetary policy. It is noted, however, that the framework is fairly complicated and that improvements are called for when it comes to evaluating policy and safeguarding priorities. It is furthermore essential that the possibility to impose sanctions provided for by the framework will be consistently deployed in the coming period – which may see more economic adversity than the past few years. This goes for both the Stability and Growth Pact, insofar as a number of larger Member States have not yet met the requirement to achieve a budgetary position close to balance or in surplus, and for the broad guidelines, insofar that, if necessary, all Member States be treated in the same way as Ireland.

Without undue large institutional changes, social and economic policy in Europe should be aimed especially at continuation of the policy aimed at structural reforms. It is pointed out in this article that the flexibility of EMU is best served when the responsibility for such policies rests with the national authorities. The priorities for structural policy, drawn up by the European heads of state or of government in Lisbon (in the spring of 2000) and Stockholm (in the spring of 2001), offer good starting positions, especially for the improvement of labour market conditions. Improvement can be achieved notably through actual implementation of the measures envisaged, a matter which deserves greater attention in the annual evaluation of the broad guidelines.
1 The latter is the so-called intergovernmental method, providing not so much for a transfer of competences to the supranational level, as for decision-making on common policy issues by the Member States (i.e. the Council of Ministers) without an initiating role for the European Commission. The community method, on the other hand, entails a transfer of competences in respect of specific policy areas to the supranational level, with the European Commission initiating legislation and acting as the executive body.


On 30 August, the euro banknotes were disclosed to the public eye, and on 3 September, the distribution of euro notes and coins to the Dutch banks has begun. We have entered the final stage on the road to \( \text{euro}\)-day, 1 January 2002. This article presents an overview of the current state of affairs with regard to the preparations for the cash changeover. It concludes that the prolonged periods, in many cases years, of preparations, are now almost completed. If the changeover operation is to run smoothly, it is important that retailing businesses order their initial supply of euro change by 1 October 2001. Some retailers still need to look more closely to their own internal preparations for the changeover. With the preparations all set, a key role will have to be played by the public in early January. The transition to the euro is, of course, a momentous change for everyone. The new prices and the new money will take some getting used to. The public will be asked to bank dormant holdings of coins and notes in time and to size down cash holdings toward the end of the year; to buy a starter kit of euro coins in December; and to begin paying in euros right from the start on 1 January. That way, we will all make things easier for ourselves and generally help to make the changeover as smooth a process as possible.
Introduction

On 30 August, the security features of the euro banknotes were made public by the ECB. It was the moment when, after years of preparation, the euro notes and coins were first shown to the public eye. It was also the moment that marked the beginning of the final stage on the road to Euro day, or e-day for short: 1 January 2002 (Box 1). In this stage, the focus will be on supplying banks and retailers with euro notes and coins, culminating in the mass distribution of euro coins in the final days of the year, after Christmas, through the so-called ‘microdistribution’ network. This article summarises the preparations for the cash changeover as they are made by or in co-operation with the Bank. On another track, various levels of government, the business community and other organisations prepare for the final switch to the euro. The state of affairs on that score is highlighted in Box 2 on page 47.

The euro coins and notes

The euro coins

In the entire euro area, 50.6 billion euro coins will have been minted in the runup to e-day. The Netherlands, for its part, will produced 2.8 billion Dutch euro coins. By the end of August, 2.5 billion coins, i.e. 75% or more

Box 1 Heading for e-day: the schedule

1 September 2001
• Retailers* receive a flyleaf from their banks detailing the ordering of euro coins and notes
• Euro notes and coins become available from banks for training purposes
30 September 2001
• Last day retailers* may order initial supplies of euro coins and notes
15 October 2001
• Banks begin their ‘Savings weeks’ campaign to encourage the public to deposit hoarded guilder coins and notes into their bank accounts
1 December 2001
• Large-scale delivery of euro coins and notes to banks and larger retailers
• Call centre made operational for questions, complaints and information about microdistribution
14 December 2001, from 09:00 hours
• Vouchers mailed to every resident over 6 years of age may be exchanged for ‘eurokits’ at: CombiFoto, Shell filling stations, Hema, ABN AMRO, ING Bank, Postbank and Fortis Bank/GWK
• Starter kits of euro coins worth NLG 25 (= EUR 11.35) may be bought from banks and retailers
17 December 2001
• First day retailers* may collect pre-ordered euro banknotes from their banks
27, 28 and 29 December 2001
• TPG deliver orders of euro coins to retailers*
31 December 2001
• First day retailers* may order extra euro coins to be delivered and guilder coins to be collected, by calling the call centre (0800-6040) or surfing to www.euro-fijndistributie.nl

1 January 2002
• The euro is legal tender; euro banknotes may be issued to the public
• Consumers to pay in euro whenever possible
• From 00:00 hours all EFT-POS (PIN and prepaid) payments are made in euro
• ATMs dispense only euro notes
• Retailers give change in euro
27 January 2002
• Last day the guilder is legal tender
• Last day retailers* may reorder euro coins
11 February 2002
• Last day retailers* may order guilder coins to be collected
31 March 2002
• Last day consumers may deposit guilders into their bank accounts free of charge
• Last day the will banks accept national banknotes from other euro countries
31 December 2002
• Last day banks will accept guilder coins and notes from their customers
1 January 2007
• From this day, guilder coins may no longer be changed at DNB
1 January 2032
• From this day, guilder notes may no longer be changed at DNB

* Applies only to retailers using the microdistribution service.
of every denomination, had duly arrived at the Bank’s Storage and Distribution Centre (SDC) in Lelystad. The remaining coins will be minted before the end of November. Part of the coins are to be packaged into various standard kits to facilitate the changeover operation (Table 1). This packaging process, contracted out to the firm of Budelpack, has almost been completed as well. In early October, the packaging equipment, now providing work for some 60 people, will have to make way for the installations required for the mass physical issue of euro coins and take-in of guilder coins.

In order to prepare the coin slot machines for the euro, manufacturers of coin testers for coin-operated (vending) machines were enabled, over the past year, to do tests with the euro coins. For this purpose, six testing centres had been set up throughout the euro area, of which one was at the Royal Dutch Mint in Utrecht. Although the businesses which used the facilities were satisfied, some market parties remain apprehensive about the use of the various euro coins in coin-operated machines. Since the euro coins have been produced to specifications with narrower tolerance limits than had been usual in the individual euro countries, there is no reason to presume that practical experience with the new coins will be different than it was with the national coinages.

**Table 1 Coin packages distributed in connection with the cash changeover**

<table>
<thead>
<tr>
<th>Contents</th>
<th>Value (EUR)</th>
<th>Weight (kg)</th>
<th>Volume (litre)</th>
<th>Number (millions)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Per package</strong></td>
<td><strong>Per package</strong></td>
<td><strong>Per package</strong></td>
<td><strong>Per package</strong></td>
<td></td>
</tr>
<tr>
<td>Microdistribution</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>'5-plus' package</td>
<td>440 euro coins:</td>
<td>219.00</td>
<td>3</td>
<td>1.4</td>
</tr>
<tr>
<td></td>
<td>2 rolls of 50 0.05 coins</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>2 rolls of 40 0.10 coins</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>2 rolls of 40 0.20 coins</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>2 rolls of 40 0.50 coins</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>2 rolls of 25 1.00 coins</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>2 rolls of 25 2.00 coins</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cents package</td>
<td>1000 euromunten:</td>
<td>15.00</td>
<td>3</td>
<td>0.7</td>
</tr>
<tr>
<td></td>
<td>10 rolls of 50 0.01 coins</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>10 rolls of 50 0.02 coins</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Starter kit</td>
<td>32 euro coins</td>
<td>11.35</td>
<td>Flat transparent bag</td>
<td>8.8-9.8</td>
</tr>
<tr>
<td>Eurokit</td>
<td>8 euro coins (one of each denomination)</td>
<td>3.88</td>
<td>The 8 coins sealed on a square of carton</td>
<td>16.3</td>
</tr>
</tbody>
</table>

**Euro banknote production**

The number of euro banknotes ordered by the central banks in the Eurosystem increased slightly in 2001, to 14.6 billion. The Bank had 655 million banknotes printed, the bulk of which is to be produced by Joh. Enschedé en Zonen Bankbiljetendrukkerij at Haarlem. Orders for the remainder were placed abroad. Conversely, Joh. Enschedé also produces notes for other euro area central banks. On 1 September, all notes ordered by the Bank had been printed, 430 million of which had also passed the final quality check by the Bank and were all ready to be issued. This number already far exceeds the number required to replace the present guilder banknote circulation. By end-September 2001, the total supply of 655 million banknotes will be in readiness at the Bank. Some of the 5, 10 and 20 euro notes have been packaged specially for the introduction, into sealed packages of 20 notes each, to facilitate the over-the-counter issue of the notes to the retail sector (i.e. retailing merchants, the catering industry and other businesses and institutions involved in receiving cash payments).

During the past few months, the central banks in the euro area have continued offering testing facilities to manufacturers and importers of ATMs and other banknote accepting/dispensing machines, where these could be tested on euro banknotes of all denominations and...
produced by different printers. Of the approximately 60 companies which participated in the testing, under strict security, ten did so in the Netherlands. The results of the tests with the euro banknotes were positive.

**Euro banknotes’ security features**

Like the guilder notes, the euro notes have two types of security features: those that are primarily brought to the notice of the public and those that are primarily meant for cashiers and checkout operators of banks and retail businesses (Table 2). The euro notes also have additional features which facilitate recognition by banknote sorting machines, including some special features which enable the central banks of the Eurosystem to check the authenticity of banknotes returning from circulation. The public media campaign will emphasise three security features: the hologram, the watermark and the security thread lining the notes. All denominations, moreover, show a conspicuous iridescent stripe or a spot, where the colour of the ink changes with the light incidence on the banknote. Like the guilder notes, the euro notes also feature palpably raised (‘intaglio’) print, diminutive lettering (mini and micro lettering) and a see-through register. In all, the euro notes contain as many as 37 security features, as opposed to 20 in the current guilder notes.

**Banknote publicity campaign**

The first steps in the protection of banknotes are technical quality and recognisability, in particular of the security features described in Table 2. It is, in fact, largely owing to these security features that the euro notes are even better protected against counterfeiting than the current national notes within the EU. The next step is to ensure broad public knowledge about what to look for when accepting banknotes in payment. Because of the unique situation, with all denominations being replaced at once with new banknotes differing in many respects from the notes people have been used to, the Eurosyste has planned an intense publicity campaign to be held throughout and even beyond the euro area, with the Bank as one of the participants.

On behalf of the police, banking staff and retailing personnel, all of whom need to acquire an adequate knowledge of the euro notes’ security features, the Bank is to make available educational materials developed by the Eurosystem. These materials include a small but

<table>
<thead>
<tr>
<th>Feature</th>
<th>= Public</th>
<th>Explanation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Hologram</td>
<td>●</td>
<td>Silvery foil. Different images appear in the foil seen from different angles.</td>
</tr>
<tr>
<td>Watermark</td>
<td>●</td>
<td>Light en dark hues in the paper. Clearly visible against the light.</td>
</tr>
<tr>
<td>Security thread</td>
<td>●</td>
<td>1.2 mm wide synthetic fibre thread in the paper. Visible against the light</td>
</tr>
<tr>
<td>Iridescent stripe (5, 10, 20)</td>
<td>●</td>
<td>Tilting reveals a golden-coloured, shiny stripe. Reverse side.</td>
</tr>
<tr>
<td>Colour-shifting ink (50, 100, 200, 500)</td>
<td>●</td>
<td>Depending on the viewing angle, the colour changes from purple to olive green.</td>
</tr>
<tr>
<td>See-through register</td>
<td>○</td>
<td>Seen against the light, front and reverse side fit each other exactly.</td>
</tr>
<tr>
<td>Tactile print</td>
<td>○</td>
<td>Tactile print layer on the front side.</td>
</tr>
<tr>
<td>Micro lettering</td>
<td>○</td>
<td>Small lettering, height 0.2-0.4 mm. Legible under a magnifying glass.</td>
</tr>
<tr>
<td>Mini lettering</td>
<td>○</td>
<td>Height 0.8 mm. Barely legible to the naked eye.</td>
</tr>
<tr>
<td>uv-reflection</td>
<td>○</td>
<td>Under uv light, several fibres become visible in the paper, in three colours:</td>
</tr>
</tbody>
</table>
comprehensive information brochure, of which 400,000 copies are to be distributed, a CD-ROM which may be used for personal training and a videotape which may be shown during training sessions. The national retailers’ association Hoofdbedrijfschap Detailhandel alone has made 12,000 copies for the purpose of training retailing staff throughout the country. Many organisations have also applied to become ‘Europartners’. They will receive instruction material which they may use in their own publications or commercial activities. Especially for front office banking staff, the National Forum for the Introduction of the Euro (NFE) has published an ‘EMU checker’ with information both on all the national banknotes taken out of circulation from 1 January and on all euro notes and coins.

The broad public awareness campaign will be concentrating on the weeks surrounding e-day. In early December, everybody over six years of age in the Netherlands will receive an information sheet about the euro banknotes. This part of the campaign is backed up by means of public television broadcasts and newspaper advertisements.

All in all, the publicity campaign that will be launched on the introduction of the new banknotes will be unprecedented in its kind.

Distribution of euro banknotes and coins prior to e-day

Supplying banks and retailers
In view of the cash-in-transit services’ limited capabilities, the ECB has allowed the national central banks to start supplying banks in the euro area with euro notes and coins from 1 September 2001. The banks, in turn, have been given permission to re-supply other entities whose usual line of business requires them to stock the euros, starting 1 January 2002. Re-delivery to banks outside the euro area will be permitted from 1 December 2001.

Special conditions have been set for the supply operation until 1 January 2002. The central conditions were imposed by the ECB and are applied by all national central banks. In this connection, the Bank has made a so-called frontloading agreement with the individual banks. This agreement states that banks must in their turn bind third parties to some of the terms in the frontloading agreement. One important condition is that an entity which is supplied with euros prior to e-day must take good care that these are kept safely and are prevented from entering circulation. Central banks may impose fines in case of non-compliance. In the Netherlands, moreover, circulating euro notes and coins before 1 January 2002 is a punishable offence. The sole exception to this rule is made for the euro coins contained in the starter kits and eurokits, which may be distributed among the public, although giving the coins in payment is not allowed until e-day. Other terms in the frontloading agreements include rules for the payment for the pre-supplied euros, which is deferred until the euro has become legal tender. In conformity with the decisions made by the ECB, the national central banks will debit the banks in three equal steps, on 2, 23 and 30 January 2002. For delivery to their clients, the banks will take 2 January 2002 as the value date.

As things stand at present, the Bank expects to be able to deliver more than half of the notes and coins ultimately required for the entire circulation before 1 January 2002. In practice, this means that during the last quarter of this year 50% more banknotes (guilders plus euros) will be shipped compared to the normal situation, and more than four times as many coins. Shipping of banknotes will take place as always from the Bank’s four Agencies, whereas the euro coins will be distributed from the ODC (Storage and Distribution Centre) at Lelystad. It is not easy for individual retailing businesses to assess the amount of euro coins and notes they will need in early January 2002. For this reason, the Bank has published a model which enables chain store companies to estimate requirements. The model was developed on the basis of research conducted by the Bank in cooperation with the Dutch Retail Association (Raad voor de Nederlandse Detailhandel). Based on the model, straightforward rules of thumb have been devised for smaller businesses to determine how many euro coins and notes they will probably need during the first week after e-day.

Transportation
Over 6,000 bank branches and post offices and some 18,000 larger retailing businesses will, as in the normal case, be stocked with euros by the cash-in-transit companies. These companies have consulted their customers in order to assess the volumes of euros ordered and of guilders returned. Based on these assessments and on several rounds of consultations with the Bank, transportation plans have been drawn up. These plans cover the entire period from September 2001, when the frontloading operation first begins, until February 2002, when the first rush in guilder return flows will be past. Banknote transportation will follow normal procedures. For the transportation of the coins, the cash-
in-transit companies have enlisted additional capacity, in the form of vans specially equipped for the transportation of coins in conformity with Ministry of Justice regulations.

As was already indicated in the changeover scenario approved by the Ministry of Finance, the Bank has made a financial arrangement with the cash-in-transit companies, so that the extra cost of transportation in connection with the changeover is not brought to bear on the companies’ customers. A budget of just over €20 million has been earmarked for this purpose. In August, the cash-in-transit companies’ customers sent full information about the arrangement to their customers.

Microdistribution of coins
For the transportation of coins to and from retailers who do not use cash-in-transit services, the Bank has developed a temporary ‘microdistribution’ system. In principle, this service may be used by all retailing businesses which make cash deposits and withdrawals at their banks on a regular basis, do not use cash-in-transit services and are registered with a Chamber of Commerce. This service, unique in the euro area, is offered in close cooperation with the banking community. The banks have selected some 300,000 customers eligible for microdistribution, to whom they have sent an information brochure and an order/registration form in early September. Using this form, retailers have one month to register for the microdistribution, stating the amount of euro coins and notes they will want to stock prior to 1 January 2002. From 17 December, they may then collect the euro notes at their local banks, while throughout the country, the euro coins will be delivered to their doors in the days after Christmas. This large-scale logistical operation will be conducted by TNT Post Groep (TPG). Retailers registered for microdistribution may, in January, place further orders for euro coins through a website, www.fijndistributie.nl, or through a call centre arranged at Het Callcenter Netwerk (HCN). These orders will be delivered within 48 hours. Until 11 February 2002, these channels may also be used to return guilder coins, provided they are sorted and packaged in standard quantities, in the special coin bags which will be provided for the purpose.

Naturally, the preparation of this entire project, for which a total budget of EUR 50 million has been set aside, is a major concern for the Bank. The comprehensive chain tests involving TPG, HCN and the participating banks have recently been successfully concluded.

Likewise, the brochure and registration/order form sent to the retailers did well in a mass poll. For the changeover operation to be successful, it is important that the target group makes massive use of the microdistribution services. Retailers will be unable to stock up on change at their local banks, as the supply there will be insufficient.

Eurokits and starter kits
Another element uniquely Dutch will be the issue of free ‘Eurokits’. In early December, the NPB will mail an information package about the cash changeover to all Dutch residents over 6 years of age. Included in the package will be a voucher in the addressee’s name and good for one ‘Eurokit’ – a set of eight euro coins, one of each denomination. The kits will be available, in exchange for the tokens, from 14 to 31 December at CombiFoto and Hema outlets, Shell filling stations and cash-service branches of ABN AMRO, ING Bank, Postbank, Rabobank and Fortis Bank/GWK. The free Eurokits are intended to make everyone in the Netherlands acquainted with the new euro coins in advance of 1 January, in order to help speed up payments.

Also from 14 December, the starter kits of euro coins will be available to the public. These are sets of 32 euro coins worth NLG 25, and will be sold by all banks, by most supermarkets and many other retail outlets. Some businesses have considered giving the packs away to employees for Christmas. For a smooth changeover it is of the utmost importance that the public will buy the packs in large quantities and will use the coins from e-day onwards to make exact payments. Some 9 million starter kits will be produced, together containing at least 270 million coins, which is more than the number of coins normally present in the purses of the Dutch public. In order to enable smaller retail businesses that do not use a cash-in-transit service to participate in the sale of starter kits, the Bank has made an arrangement with PTTPost under which medium and small-sized businesses may order the packs from PTTPost.

e-day and after

The conversion of ATMS
In order to facilitate the cash changeover, the ATMs in the Netherlands will dispense more NLG 25 banknotes and fewer NLG 50 and NLG 100 notes than usual during the last days of December. Finally, on 31 December, part of the ATMs will be taken out of service, and from 1 January 2002 00:00 hours, all ATMs will stop issuing
guilder notes. From that moment, some ATM s will begin issuing euro notes, while during the night, a good three out of every four remaining ATM s will follow suit. ATM s protected by vandal-proof covers as a normal procedure for the turn of the year will return to service in the course of New Year’s Day morning. Within the NFI framework, it has been agreed with the banks that 40% of ATM s will not only dispense the usual EUR 10, EUR 50 and in some cases EUR 20 notes but also, during the first week of January, the smallest euro note denomination, the EUR 5. The banks will make temporary adjustments to their ATM s for this purpose. This agreement will help to put this denomination into large-scale circulation right from the start, which will limit the amount of change needed by the retail sector. The Bank has established that most banks have now finalised detailed changeover plans.

Changeover of EFT-POS terminals and electronic retail payments

Also at 00:00 hours on 1 January 2002, electronic retail payments will switch from guilder to euro. All payments by debit or prepaid card will be in euro only. In order to make the change, the EFT-POS terminals must have been adapted for the euro. By mid August, 125,000 of the 165,000 debit card terminals in the Netherlands had been converted. Conversion orders for another 32,000 terminals have been placed and are expected to be carried out before the end of October. For 10,000 terminals no orders have as yet been received. According to information released by Interpay, these terminals are at present used to process some 5% of total sales. The majority will not be able to be converted in time to continue functioning on 1 January. Chipper prepaid card users may continue to use it without any problem. The precharged guilder balance will automatically be converted to euro. Users of the Chipknip prepaid card (recognisable by the logo on the reverse side) must after 1 January, 00:00 hours, convert their balance to euro at a reloading terminal. The public is encouraged to use the prepaid card in the early hours and days after the changeover, particularly for small payments. Payment will take place in euro, the shopkeeper need not give change and the transaction is processed more rapidly than a PIN debit card transaction because it does not require an online connection to Interpay.

The Bank has established that the preparation for the conversion of Interpay’s central systems has been completed. In addition, Interpay will upgrade its central processing capability before 1 January to a level not expected to be required until 2005. In practice, this means Interpay will be able, in January 2002, to process almost twice the number of transactions it can handle today.

Extended banking hours

The banks have agreed on a common line of action regarding an extension of their banking hours around e-day. From Thursday 27 December 2001 through Friday 4 January 2002, bank branches and post offices with cash facilities will be open from 9 am until 6 pm on normal working days. If the need arises, the same hours will also be kept in the second week of the year 2002. In addition, these offices will be available on Monday 31 December and Saturday 5 January, from 10 am until 2 pm. On e-day itself, the offices will be available for a few hours to enable business clients to collect pre-ordered packages of euro banknotes.

Paying in guilders and euros during dual stage

For retailers, the fact that they will, in January, be faced with payments in guilders and euros at the same time will present more difficulties than any other aspect of the changeover. Checkout transactions in particular may prove a bottleneck. As has been established in simulated environment tests, delays and mistakes will be especially likely to happen if customers wish to make payments partly in guilders and partly in euros. Although such payments are not forbidden, they will be strongly discouraged. The changeover scenario has been devised to make the public pay in euro from the earliest time possible. This will also be emphasised by the publicity campaign. It is of major importance that people buy a starter kit of euro coins and start withdrawing euro banknotes from an ATM or one’s bank at an early moment. The remaining guilders may then be spent at a later, quieter time or exchanged at one’s bank. In addition, it will be recommended to the public to carry a well-charged prepaid card with which in numerous situations small payments may be made quickly. This way, individual persons will make things easy not only for themselves, but also for society as a whole. The objective is to have three out of every four payments made in euro after one week. One exception has been agreed within the NFI framework: for security reasons, all payments to drivers of buses and trams will have to be in euro right from the start. Many coin or banknote operated vending machines will also not accept dual payment. Many parking meters, however, will work with both currencies.

Return flow of guilder notes and coins

As is described in the article ‘Current developments in
January in particular, the number of deposited guilder notes has been declining – the coin circulation little if at all. In order to encourage the liquidation of cash hoards, the banks have organised a ‘Savings Weeks’ campaign, running from mid-October through December, urging the public to deposit the hoarded notes and coins into their bank accounts. Starting 1 January, the public will be asked to wait a few weeks until quieter times before they bank any remaining hoards of guilder notes and coins. At least until 1 April, this may be done free of charge. From September 2001 until February 2002, the organisations Stichting Nationaal Collecteplan and Coins for Care will collect guilder coins, but also coins on behalf of more than a hundred recognised charitable organisations. Collecting-boxes will be placed at 5,000 banks and post offices and in several thousand shops. During the second half of January, over 200,000 voluntaries will go from door to door to collect remaining coins.

Only a limited part of the guilder coins and notes is expected to return in January in the form of retail payments. An inquiry by the Bank has pointed out that people in the Netherlands carry with them only 30 million of the 380 million banknotes and only 200 million of the three billion coins still in circulation. The remaining coins and notes lie in money boxes, hoards, firms’ cash boxes and in banks, or they have crossed the border.

Banks, the retail industry and other organisations are partly refunded for the cost of taking in and depositing the guilder coins. Retailers who have registered for the microdistribution system will receive EUR 11 in compensation for each standard bag of guilder coins they return. This amount will, after the bags have been checked, be transferred to the sender’s bank account together with the coins’ nominal value. EUR 11 is also refunded for each bag of coins returned to the odc through the cash-in-transit companies. A total of EUR 36 million has been set aside for this purpose, on the basis of an expected 3 billion guilder coins returned. The compensation arrangement will end in mid-February. The banks, under the Savings Weeks arrangement, will be receiving the same compensation in the October-December period for the net extra guilder coins they return. The guilder coins received at the odc will be destroyed, and the scrap metal will eventually be melted down.

The guilder banknotes must be deposited through the usual channels and normal procedures. Retail businesses will deposit them at their bank, whether or not via a cash-in-transit service. During the first week of January in particular, the number of deposited guilder notes will be much greater than usual. In a normal situation, the deposit provision payable to the bank would therefore also go up. In order to avoid this, the major banks have decided to accept guilder notes deposited by smaller retail businesses free of charge during the first week of January. Individual arrangements will be made with the larger retailers, as is the customary procedure. The guilder banknotes returned to the banks will be transported by cash-in-transit companies to the four agencies of the Bank, whose opening hours will be much extended around 1 January. After the usual authenticity check, the notes will be destroyed.

Security and coordination

Security

The security aspect of the cash changeover has high priority status. Wherever necessary, the authorities have taken additional measures. The Bank has been closely involved in preparing these measures. During the changeover period, more cash will be transported, while banks, arm’s and retail businesses will also handle more money than usual. Therefore, the safety of the parties involved in the changeover and of the public will be supported by an extensive and coordinated police effort and by additional measures by the judicial authorities. Responsibility for the policing measures lies at the police region level, while coordination of the entire effort will take place from a nation-wide platform under the direction of the Board of Chief Superintendents, the committee of regional commanders and the public prosecution and police joint committee.

There have been close consultations about crime prevention measures with parties involved such as cash-in-transit companies, retailers and ttp. Additional arrangements are made locally with regard to the policing effort. This effort will peak in the weeks between Christmas and mid-January 2002, manifesting itself especially in a markedly increased street presence of uniformed police, in particular near bank branches, arm’s and around shopping malls. The existing police instructions to enhance safety and security in shops will be given new emphasis in the runup to e-day, and they will be supplemented by changeover-specific advice in a special crime prevention brochure entitled De euro de baas (‘Mastering the euro’). The transportation of coins and banknotes is surrounded by equally elaborate security measures, including police surveillance of transportation journeys and of arm’s being loaded. Regarding the microdistribution, special arrangements have been
agreed, conforming as closely as possible to the existing legal framework for armoured vehicle transportation. The Bank and the Ministry of Finance have contracted licensed security service firms for the supply of personnel to accompany tpg vans. Also, measures have been taken regarding security procedures to be followed, levels of training and technological equipment.

Coordination framework
During the period from 1 December 2001 until end-February 2002, the National Coordination Centre will act as the centre of gravity for information, coordination and decision-making, where all government-relevant information about the changeover from all parties involved will converge. The Ministry of Finance acts as the central coordinator. Within this framework, the Bank will play a coordinating role vis-à-vis the business parties involved most closely in the changeover process. In addition, the Bank will keep in contact with the other central banks in the Eurosystem.

The decision making process at this stage will be based on contingency scenarios and fall-back options contributed by the organisations involved. There will be backup distribution plans, for instance, and possibilities for reinforcement of security measures should there be incidents in the security sphere.

Conclusions
The production of euro coins and notes has almost been completed. Preparations for the cash changeover by the parties bearing joint responsibility for the changeover infrastructure (banks, the parties involved in cash transportation) are in their final stage. Thus, long periods, in some cases years, of preparations are drawing to a close. All that could be tested has been tested. The measures required for reasons of safety and security during the cash
changeover are also being prepared with the utmost thoroughness. All that is left to complete are the contingency scenarios and fall-back options which will ensure completion of the changeover operation even if problems should occur. For a smooth and rapid changeover process, it is important that retailers who have not finished preparing for the changeover do so while there is still time. Crucially, all retailing businesses should place their orders for the euro change they need on e-day during September.

The public spirit will eventually be material in determining the course of events during the changeover. If people spend or bank unneeded guilder coins and notes in time; if in December they buy starter kits of euro coins and if from 1 January they begin paying in euro right from the start, they will make a massive contribution to a smooth and speedy changeover.

Sources of information

Websites
www.dnb.nl
www.euro.nl
www.ecb.int
www.fijndistributie.nl

Publications
e-day Nieuws (published by the Bank)
Eurokoers (published by nfe; Eurokoers and other nfe publications may be ordered by calling the Euro Line, 0800-1512, or by surfing to www.euro.nl).
In July 1999, the Minister of Finance presented a policy document to the Second Chamber of Parliament on the provision of information to consumers of financial services. The document named three objectives. Firstly, to explore whether existing financial services legislation offered consumers enough protection and gave them sufficient information to form a balanced judgement of the products on offer. Secondly, to improve the position of financial products consumers where possible and, thirdly, to foster market transparency. The document also contained a number of policy initiatives, giving special emphasis to the key features document.

The key features document in the Netherlands is somewhat similar to the one used in the United Kingdom. It is a paper issued by an institution under the supervision of the Pensions and Insurance Supervisory Authority, the Securities Board of the Netherlands or the Nederlandsche Bank, serving to enable potential customers to assess a certain financial product.
Introduction

The underlying aim of the key features document is to improve the provision of information to consumers, making it easier for consumers to obtain the facts and, where necessary, to protect themselves. In this context, the term consumer refers to a natural person insofar as he is not acting in a professional or business capacity. In itself, the objective of informing and protecting consumers is not new to supervisors. Banking supervision is after all aimed at protecting creditors, while the supervision of collective investment schemes seeks to ensure the adequate provision of information. However, this initiative, which is targeted at individual consumers, is an entirely new departure. And, in some ways, it is also a new area for the other financial supervisors in the Netherlands, the Securities Board of the Netherlands and the Pensions and Insurance Supervisory Authority.

The Council of Financial Supervisors, a consultative body comprising the three supervisors, has forged ahead with this new and challenging project.

On 5 July 2001, the Council of Financial Supervisors (the Council) presented the report ‘Towards a Key Features Document for Financial Products’ to the Minister.

Along with a brief description of the current position in respect of the key features document, this article deals with its contents and the relevant legislation.

Objective of the key features document

The general objective of the key features document is to improve the provision of information to the consumer. The priorities are:

• Firstly, to give an overall picture of the product, enabling consumers to understand the main features of the product they are thinking of buying;

• Secondly, to permit comparison between different products of a similar nature;

• Thirdly, to enable consumers to choose between different types of products.

It appears that many consumers who begin to familiarise themselves with financial products decide which kind of product they want at an early stage. That is why the comparability of different products is given as the third priority. Nonetheless, legislation for banks, insurance companies and other financial institutions must be identical.

The key features document should be a concise and accessible document for the average consumer, containing brief and easily understandable responses to straightforward questions. It is not a manual on how to react in specific cases but seeks to give the consumer a complete picture of the product. The key features document must hence list the main characteristics of the product as well as the risks, particularly the uncertainties as to the returns. The most efficient method is to alert consumers to what are known as the ‘downside risks’, the idea being that the positive opportunities are usually already well-documented in promotional material.

Consumer survey

In April and May 2001, the nipo conducted a survey to evaluate the proposed format for the key features document. The survey reviewed whether the format matched the needs of consumers and assessed aspects such as comprehensiveness, clarity and accessibility.

The first part of the survey shows that many consumers find it difficult to fully comprehend the consequences of buying a certain financial product. It clearly emerged that:

– the respondents did not have a high level of knowledge about financial products;

– people generally have little interest in financial products, leading some to depend heavily on advisors;

– some respondents preferred not to be confronted with the risks of a product. Moreover, according to a number of those interviewed, the key features document lacked persuasiveness, precisely because it focuses on downside risks.

The Council concluded – on the basis of this survey and its consultations on the key features document with institutions and organisations – that the document could be extremely useful in helping consumers to choose financial products. However, it will have to be embedded in a programme of more general consumer education.

The public will have to be informed of the existence and objective of the key features document by means of an extensive publicity campaign. Advertisements for specific products will have to consistently refer to the availability of a key features document.

Format

The format for the key features document was drafted on the basis of results from the readers’ panel, com-
ments by institutions, and by drawing on examples and experiences in the United Kingdom. Gearing the document to consumers with no more than basic education, the supervisors attempted to find a compromise between the adequate provision of information, comprehensibility and easy reference.

A key criterion is the uniformity of structure and content for all products, even across the sectors. The first sections hence follow a set order, dealing with topics such as the objective of the key features document, the objective/nature of the product, performance and attendant risk factors and the supervisor. The texts are in the form of questions and answers, the questions being mandatory. The answers must be given by the institution.

Supplementary product information will be included in a number of other sections, compiled with the help of a comprehensive list of standard headings. This format was chosen as it is the only way to ensure uniformity while retaining flexibility, enabling key features documents containing all the relevant information to be drawn up for all products.

A sample selection of questions likely to appear on the key features document for a certain product is given in the table below.

### Returns and costs

The niro survey showed that, when reading the key features document, consumers quickly turn to the tables giving the (projected) returns. This underlines the importance of a realistic and verifiable presentation of the returns and costs, the overriding reason being that consumers almost invariably regard the returns and potential performance as the main features of a product and are likely to find a brochure lacking this information unsatisfactory.

With this in mind, the supervisors decided to include a standardised table in the key features document.

Various tables were tested in the niro survey. One version placed more emphasis on the costs than on the potential returns, while another simply showed potential returns. The final choice was for an extensive table (as shown below) containing calculations of the net pay-out on the basis of three percentages: two sample rates and the historical rate of return.

The rate of x-percent depends on the type of investment and could be negative in the case of risky investments. The downside risk is shown in the relevant column. The rate of 4 percent is the same for all types of investment. The rates can be adjusted periodically.

The trial results show that the respondents preferred this extensive table. Another advantage is that this table reflects the uncertainty of realising potential returns.

The basic assumptions of the table apply to all the various sectors, but certain sector-specific characteristics will be taken into account. The table shown here is intended for collective investment schemes.

The supervisors will work out the presentation of returns in more detail in their legislation. It emerged in the niro survey that consumers are not always aware...
that a presentation of returns is only an example or a projection and not a guaranteed yield. The document will have to include mandatory standard texts at the beginning and end of the section.

### Risks

The principal argument in favour of a key features document is that consumers are not always adequately informed about a product’s inherent risks. Advertisements and promotional texts issued by institutions seldom emphasise the specific risks of a product. In many cases, the risks are explained solely in the underlying documentation, expressed in legal and technical terms. A clear account of the risks is hence an essential element of the key features document and will appear in one of the first sections. The key features document for a product that is a combination of other products, e.g., investment and lending, must include all the risks of that combination. Specific country or sector risks should also be set out in this section, as should the risks of investing with borrowed funds.

The expediency and feasibility of including a uniform risk indicator in the risks section of the key features document were explored. A uniform risk indicator seeks to encapsulate the risks of a product, reducing them to a single index number. A set of (different) index numbers obtained in this way could result in a scale for categorising the risks attached to various investment products. The advantages for the consumer are that almost everyone can understand this classification intuitively and at a glance. Various studies to develop such an indicator were conducted by the Ministry of Finance, the Council and others. An essential requirement for an indicator is that it can be determined objectively, making it enforceable.

Since the requirements of clarity and enforceability proved difficult to reconcile, expectations are that no risk indicator meeting these requirements will have been put forward on the implementation date of 1 July 2000. The Council of Financial Supervisors will continue its efforts in this area, however, to review whether the introduction of a risk indicator would be feasible at a later stage, for example as part of an evaluation of the key features document.

### Legislation

The point of departure for the legislation is that it should be as near to identical as possible for the various sectors.

Draft legislation for formal consultations has been presented to representative organisations such as the Federation of Insurers, the Netherlands Bankers’ Association and the Consumers’ Association. Important points in the draft legislation are:

- On taking effect, the legislation will not only apply to new complex and designated financial products, but also to existing products offered to the public;
- The scope of the legislation for institutions is not extraterritorial; in other words, barring obligations under European law, Dutch institutions will not be obliged to provide a key features document for products which are offered to the public abroad. The Council finds that, partly with a view to preserving a level playing field for Dutch institutions operating abroad, it would be unreasonable to impose such an obligation on them;
- The legislation makes a distinction between the obligation to have a key features document and the obligation to distribute it. The representative organisations argue that mandatory distribution of a key features document is not always feasible (for example when shares in unit trusts are traded on the stock exchange) and would, in some cases, be extremely problematic. During the formal consultations with the representative organisations, the Council will further consider a practical manner of implementing the obligation to distribute a key features document, without impairing maintenance of a level playing field for institutions.
Although the idea of a key features document met with general approval, fundamental criticism of parts of the document emerged from the formal consultations, which have not yet been completed. The criticism applied mainly to points where it appeared that the level playing field for the various suppliers of financial products was at issue.

Types of products requiring a key features document

The draft decree provides that a key features document is mandatory for defined complex financial products. These ‘complex’ products have two cumulative features: they are made up of different product types and at least one of these involves investment.

Partly in view of the great diversity of financial products on the market and the speed at which new products are developed, the draft decree also gives supervisors the power to designate certain products that require a key features document. Financial products will be designated if the supervisors hold that the key features document would assist the consumer in assessing the product. For example, all collective investment schemes holding an authorisation under the Act on the Supervision of Collective Investment Schemes could be designated. The Council has noted that collective investment schemes form an important segment of the market for financial products targeted at consumers. With a view to promoting the comparability of financial products, the Council finds it appropriate to make collective investment schemes subject to these obligations too.

Another consideration is that practice has shown that investors have little insight into notably the risks and costs attendant on (participation in) collective investment schemes. Many investors find the prospectus too extensive and difficult to fathom. Much of the prospectus hence goes unread. Thanks to its clear format and limited size, the key features document will make an important contribution to the provision of information to (potential) investors on the aspects of collective investment schemes that are most relevant to them.

The supervisors will be given the authority to grant general exemptions from certain obligations as well as to issue individual dispensations.

Starting date

The introduction of the key features document requires considerable effort by the supervised institutions; they must therefore be given the opportunity to prepare themselves.

It is also important that, where possible, the key features document is introduced simultaneously for all the products concerned. This offers the best safeguard for the comparability of products aimed for by means of the key features document.

Mindful of the above, the Minister of Finance is advised to make compliance with the rules on the key features document mandatory as of 1 July 2002, since the representative organisations expect to need six months to actually introduce the key features document in their organisations. The supervisors will draw up a recommendation requesting institutions to comply with the regulations as of 1 January 2002. The supervisors will keep a very close eye on the introduction of the regulations, from the time of their publication in the autumn of 2001 until they become compulsory.

Intermediaries

The Council of Financial Supervisors is examining what improvements can be made to the legislative framework for (legal) persons acting as intermediaries for financial services. The channel through which consumers obtain a complex or designated financial product should not make a difference: a key features document will be required for every complex or designated financial product.

At present intermediaries who are not subject to the appropriate legislation cannot be obliged to compile a key features document. Under the terms of the draft decree, a direct obligation to do so should, however, apply to supervised institutions acting as intermediaries. If intermediaries are not subject to a supervisory Act themselves, the supervisors will impose a duty via further legislation to the effect that supervised institutions must make every effort to ensure that, where their products are offered to the public via third parties, these intermediaries provide consumers with a key features document.
In the past few months Dutch businesses have been moving decisively to prepare for the launch of the euro in January 2002. The Nederlandsche Bank’s twelfth Euro Survey found that 70% of medium-sized and large enterprises have now made the necessary investments, and some 50% of small businesses. Although there is obviously still some way to go, entrepreneurs themselves see few difficulties.

The survey, which was conducted in July, discovered that two-thirds of the Dutch have faith in the euro as successor to the guilder, with both information satisfaction and actual knowledge about the euro and monetary union having improved significantly since March. There is also greater awareness of the length of time in which both guilder and euro will be legal tender, although this does remain an area of concern.

Neither the business community nor the Dutch public at large expect that it will be easy to make cash payments during the changeover period. Uneasy about the complexity of the exercise, they fear long queues at counters and check-outs. To help ensure a smooth transition, a growing number of Dutch consumers are prepared to use their credit and/or debit cards.

The survey revealed that four-fifths of the Dutch population fear covert price increases in the wake of the changeover to the euro. To date, both the Consumers’ Association’s Euromonitor Survey and research by the Nederlandsche Bank have found little evidence to corroborate these presumptions.
Introduction

On 1 January 2002, euro notes and coins will replace national currencies in the twelve EMU countries, completing monetary union. National governments, the business sector and consumers have three months left to prepare for the abolition of their currencies and to ‘euro-proof’ their organisations.

Over the past six years the Nederlandsche Bank’s six-monthly surveys have kept a close watch on euro-related trends in the Netherlands, covering issues such as euro sentiment, euro awareness, satisfaction with the provision of euro information, progress of euro conversion preparations and intended euro exchange and payment behaviour of households and enterprises. This article reviews the main findings of the Bank’s twelfth Euro Survey – probably the last in its present guise. The survey interviewed 734 private individuals over the age of 18 and 791 enterprises, with banks not included because of their special position.

Euro acceptance and knowledge

Euro sentiment stabilising

Compared with some neighbouring EMU countries, the Dutch have always shown firm support for the euro, but in the second half of 1999 and during 2000 sentiment took a turn for the worse in the wake of the fall of the euro against the US dollar. In the spring of this year things improved a little, and subsequent months saw support for the euro among private individuals stabilise at the March level. At this point, two-thirds of the Dutch consider the euro an acceptable successor to the guilder, a reading matching the European Commission’s Eurobarometer survey findings. However, a sceptical hard core of around 15% of the population remains unconvinced: 42% of these now indicate they fear higher prices upon the launch of the euro. This is a striking finding: until recently euro opponents mostly cited the falling euro exchange rate against the greenback as the reason for their unease, with only 10% mentioning higher prices as a factor in the autumn of 2000. It looks as if recent press reports about one or two steeply higher prices on euro conversion have hit a sore nerve.

Around 70% of Dutch businesses have a positive perspective on the euro. Not surprisingly, the business community was found to be more sensitive to the currency’s position in the foreign exchange markets. Admittedly, the number of enterprises taking a dimmer view of the euro launch has contracted since March of this year, but the percentage blaming the persistently weak euro-dollar rate for their disaffection has risen by nearly 20 percentage points. It is worth noting, however, that the actual fieldwork was carried out in July, so the poll fails to take on board the impact of the euro’s more recent, modest advance against the dollar.

Satisfaction with provision of information sharply up

With only three months to go, it is heartening to find a solid rise in the degree of euro information satisfaction among the Dutch population. Over 80% express their approval of the information provided, compared with 70% in March. The increase was found across all age groups. Enterprises also report higher satisfaction: 94% of those polled feel adequately informed. Some qualification is in order here: the catering, transport and building industries show comparatively lower satisfaction levels.

The euro area at large is much less pleased with the provision of information, according to the EC’s Eurobarometer: less than half of Europeans feel sufficiently up to speed with all things euro.

Euro knowledge rises

A regular feature of the Bank’s survey, questions gauging euro and EMU knowledge have recently focused on the euro/guilder exchange rate, the launch date for euro banknotes and coins, the number of countries participating in the euro and the length of time in which both guilder and euro will be legal tender.

As in March, awareness of the euro launch date among private individuals is high, albeit showing a decline from 97% to 91%. Among enterprises, the Bank’s survey dispensed with this question altogether: the broader business community had been found to be wise to the correct date for a long time.

As Chart 1 shows, there has been a marked upturn in public awareness of the length of time that the euro and the guilder will both be legal tender. In March 2000, less than one-fifth of the Dutch were able to name the correct period (1-27 January 2002), but by now half of them...
are clued up. That said, nearly 30% still mistakenly believe that this period extends to 1 July 2002. Less strikingly, the 10% advance at the business end takes the number of enterprises aware of the correct period to 60%. Food retailers were unable to retain their relative lead – a pity, because an awareness of the length of the so-called ‘dual phase’ is crucial so soon before the actual, physical birth of the euro. As long as enterprises believe the changeover period to be longer, they will feel under less pressure to make the necessary preparations and might come up against unpleasant surprises in four months’ time. The government would be well-advised to bring home the facts of the euro conversion term more sharply to Dutch business through targeted euro awareness campaigns.

Cash payments and conversion

Withdrawing guilders from circulation and distributing the new currency will be a major logistical challenge. The success of a smooth conversion hinges on careful preparation. Facilitating measures can only be taken if those in charge have a clear view of the needs and expectations of both the general public and the business community.

Familiarisation in the run-up to ‘e-day’

In previous surveys, the Dutch public expressed a strong desire for prices in both euros and guilders at restaurants and shops in order to familiarise themselves with euro prices to come. In a number of other euro countries such dual pricing had already become standard practice. The Bank’s latest survey found that 67% of companies now have dual price tickets on their articles and that retailers have taken the lead in this respect. Great strides indeed on the situation in March, 40%

Table 1  Euro awareness and knowledge: adult Dutch population, 1999-2001

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<tr>
<td>Sufficiently informed</td>
<td>79</td>
<td>72</td>
<td>69</td>
<td>70</td>
<td>82</td>
</tr>
<tr>
<td>Aware of euro exchange rate (2.20)</td>
<td>71</td>
<td>65</td>
<td>54</td>
<td>65</td>
<td>77</td>
</tr>
<tr>
<td>Aware of launch year of euro coins and notes (2002)</td>
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<td>70</td>
<td>77</td>
<td>97</td>
<td>91</td>
</tr>
<tr>
<td>Aware of number of EMU countries (10, 11, 12)</td>
<td>46</td>
<td>27</td>
<td>48</td>
<td>41</td>
<td>40</td>
</tr>
<tr>
<td>Aware of length of transition period (4 weeks)</td>
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<td>17</td>
<td>19</td>
<td>31</td>
<td>50</td>
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Table 2  Euro awareness and knowledge in business sector, 2000-2001

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<tr>
<td>Sufficiently informed</td>
<td>86</td>
<td>88</td>
<td>87</td>
<td>94</td>
</tr>
<tr>
<td>Aware of euro exchange rate (2.20)</td>
<td>63</td>
<td>59</td>
<td>72</td>
<td>75</td>
</tr>
<tr>
<td>Aware of launch year of euro coins and notes (2002)</td>
<td>73</td>
<td>80</td>
<td>96</td>
<td>-</td>
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<tr>
<td>Aware of number of EMU countries (10, 11, 12)</td>
<td>33</td>
<td>52</td>
<td>51</td>
<td>37</td>
</tr>
<tr>
<td>Aware of length of transition period (4 weeks)</td>
<td>22</td>
<td>32</td>
<td>49</td>
<td>61</td>
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when this figure came in at 37%. The downside is that one in three companies is lagging and has failed to honour the agreement between the Consumers’ Association and industry organisations to implement dual pricing by 1 July 2001 at the latest. In fact, nearly half of this group does not intend to change to dual pricing until 1 January 2002. Enterprises surveyed are a cross-section of the Dutch business sector, and earlier research by the Nederlandsche Bank has revealed that this particular group of companies primarily consists of those that adjust their prices once a year at most and that wish to avoid any extra costs.

Growing fears of upward price effects
Media focus on pricing shenanigans in the wake of euro conversion has made Dutch consumers suspicious of covert price increases. Compared with 58% six months ago, nearly 80% now expect businesses to round up their prices to ‘attractive’ euro figures. One-fifth of those suspect this will rack up prices by at least 2%, while another fifth believes 5% is more likely. Men dominate this latter group, whereas a majority of those unwilling or unable to cite a percentage – 23% of those surveyed – are women.

In terms of their rising suspicions, the Dutch are ahead of most European countries: some two months ago 64% of Europeans feared that retailers would take advantage of the euro launch to increase prices (as against 50% a year earlier).

At the end of 1999 official agreements were reached to head off covert price increases through systematic, unjustified rounding-up. The Dutch Consumers’ Association constantly monitors compliance with these agreements by keeping tabs on a range of products. The Nederlandsche Bank has carried out its own research into possible price effects. It concludes that there are as yet no signs of price increases creeping in, but that vigilance is nonetheless needed.

In a notable finding, 69% of enterprises surveyed expect their sectors to round up in order to create attractive prices, with price increases put at 2% (cited by 14% of respondents) or 5% (12%). Over one-quarter does not know, whereas one-fifth reckons that prices will remain unchanged. However, when asked whether implementation costs and psychological price hiking would impact on their own prices, 59% indicated that nothing will change. Nearly half of the Dutch business community understand that price hikes might spark turmoil and uncertainty, compared with 47% who believe it will not come to this – because consumers display little price awareness as it is, one-fifth of them feel. As the survey highlights, fiercely competitive food retailers know better and are very careful not to underestimate consumers.

Cash payments and conversion around ‘e-day’
Institutions involved in the euro conversion need to know what households will do with their guilder notes and coins around ‘e-day’, allowing them to take appropriate action. The Bank’s latest survey suggests that one-third of Dutch consumers intend to spend their guilders this year and that 16% will put the money into their current accounts in the course of the fourth quarter. This implies that a significant proportion of guilders will have been withdrawn from circulation even before conversion gets going. Another third of the Dutch population plan to spend their last guilders in the period up to January 27th or convert their guilder holdings into euros as 2002 progresses. Over a quarter of respondents have yet to make up their minds or are considering a mixture of saving, spending and exchanging.

Consumer willingness to chip in to a smooth transition from guilder to euro is sharply up, with 83% of the population now agreeable to using their credit and/or debit cards. At 62%, PIN cards (a debit card) should be their favourite means of payment by far, but another 20% claim they are willing to use both their PIN cards and so-called chip cards to lighten the burden on retailers around ‘e-day’.

To allow consumers to pay in euros from day one, sets of euro coins worth NLG 2.5 will come on sale from 17 December. Some 60% of respondents intend to buy these – a big advance on the 45% figure recorded in
March. There has been no change in the number of sets households plan to buy: 1, 2 or 4, averaging 2-3 per household.

Mixed feelings about a smooth euro transition
Consumer willingness to lend a hand seems to tie in with growing concerns about a problem-free change-over. Close to 60% (March: 55%) fear hitches in cash payments, one-third (previously 24%) – with women dominant among this group – expect long queues at counters and check-outs and another third (33%) see the entire exercise as too complex in and of itself. And yet these concerns are not prompting any preventive action – considered unnecessary by nearly three-quarters of the population. A breakdown by sex reveals significant differences here: men take a far less gloomy view than do women. Also, comparatively more women plan to do extra shopping ahead of the first days of 2002.

The percentage of businesses predicting trouble at the euro-for-guilder swap is unchanged from March: 59%. Out of this, one-third (previously 23%) cites the complexity of the exercise and 15% lengthy queues at counters and check-outs. This latter percentage is quite surprising, as it has come down from 25%. Insufficient preparation on their own part is the fear of only a small group of businesses: compared with 11% in March, now only 9% feel the business sector might have to take the rap for preparatory shortcomings.

Business limbering up
Over the past twelve months public bodies have been very worried about the lack of momentum in Dutch business preparations for the euro. Outside the Netherlands, progress among the EU business community has been similarly lacklustre, with the European Commission urging greater efforts. Shrugging off such promptings, enterprises were found to see no need – yet – to significantly boost their investment drive. Oft-cited reasons for putting off their euro groundwork included ‘It’s no use preparing yet’ and ‘It won’t take much’. Enterprises appear to have increasingly given up on initial intentions to euro-proof their administrations and their cashless euro payments well before 1 January next year.

The latest survey findings suggest that the Dutch business community has now intensified its preparations. Chart 2 puts in a timeframe the average preparation of businesses for euro conversion on 1 January 2002. This average preparation figure is the percentage of the total preparation time already spent on average.

Enterprises have been broken down by size, but also by other features such as sector. Large businesses have made the greatest headway, closely followed by small and medium-sized companies. According to themselves, large enterprises claim to have done some 80% of the preparatory work, which compares with a little over 60% in March. At 78%, medium-sized businesses are just a tad behind, while small enterprises report having done nearly 70% of their homework. This latter group is currently focusing heavily on adjusting software and equipment, whereas the larger players are also looking at the significance of the euro for business strategy, regulations, marketing and logistics.

In March a negligible 16% of large enterprises had shaped their euro strategy, but by July this figure had zippered up to 64%. ‘Educating the workforce’ was another issue far from entrepreneurial minds in March, but which has now caught on. Nearly two out of three large enterprises now claim to have laid the necessary groundwork, compared with only one out of seven in the spring.

Broken down by sector, there has been a sharp uptick in preparations across the board. Wholesalers, business services and manufacturing have completed over three-quarters of their preparatory process (Chart 3), and retailers – particularly food retailers – have also made significant progress. In part, the benefits are visible to consumers, with two out of three retailers having now adopted dual pricing. Less obvious to the naked eye is the conversion of cash registers, point-of-sale terminals and cash points. Over-the-counter
businesses will be the first to face immediate and frequent cash payments in euro from the start of next year.

Compared with the March survey, giant strides have been made here as well: three-quarters of food retailers have now done what needed doing. Non-food retailers are somewhat behind at 63% of orders placed.

Nearly half of investment spending now made
The changeover to the euro will involve one-off expenditure for Dutch companies. Costs incurred give an indication as to how much progress enterprises have made in euro-proofing their organisations. The Dutch business community (ignoring banks) currently reckons it will need over NLG 7 billion to deal with the changeover. Enterprises reportedly spent some NLG 3 billion up until July, compared with NLG 1.5 billion through to March. In other words, nearly half of projected spending has now been effected, doubling the March figure. As Chart 3 shows, medium-sized and large enterprises have the highest score on this gauge and now have roughly 30% more to go in euro-related implementation costs in the second half of the year. Small businesses, by contrast, are looking at an outstanding 50% of costs. Breaking these findings down by sector, the manufacturing and business services industries have yet to execute a relatively large proportion of their plans.

Enterprises see few bottlenecks
Business efforts made in the past few months constitute a solid move in the right direction. As the figures show, enterprises have now seriously taken on the issue of euro implementation. But a lot still needs to be done if the final changeover is to be pulled off without a hitch. A smooth transition is important for everyone, not least for enterprises themselves. Most businesses – six out of seven – do not foresee any major problems or bottlenecks in preparing for and changing over to the euro, the survey found. This apparent unconcern even holds on the issue of attracting professionals (such as IT staff). Retailers express the greatest concerns – understandably so, as they will be the first to deal with cash payments in euros. One in three food retailers, for instance, fears difficulties at shops after 'e-day' when swapping over to the new banknotes and coins. To reduce the burden on retailers, it is imperative that consumers adapt their payment behaviour. As noted, many consumers are willing to do their bit in easing the transition. Information campaigns should clarify how to best to do this.

Business making a late switch to euro administration
Dutch enterprises are increasingly opting for a late switch to euro administration, relinquishing their previous ambitions of an early change. As Table 3 shows, small and medium-sized enterprises, in particular, are betting on a switchover of their business records to euros on 1 January 2002. It is unlikely that the euro will become a significant factor in non-cash payments much before that date. This, coupled with the rapid withdrawal of guilder banknotes and coins from circulation, suggests that the Netherlands is heading for what might be termed a quasi Big Bang.
Summary and conclusions

Key findings of the Bank’s twelfth Euro Survey are:
– Two-thirds of the Dutch population consider the euro a good replacement to the guilder.
– The vast majority of the Dutch population feels adequately informed about the euro and the currency union.
– Public and business sector euro knowledge has improved further in key areas. The correct length of the dual phase is a case in point here, although this particular issue does remain an area of some concern.
– Individuals and businesses continue to worry about disruptions in cash payments in January 2002. Principal concerns relate to the complexity of the operation and queuing at counters and check-outs.
– Four out of five consumers expect covert price increases following euro conversion.
– To help ensure a smooth transition in January 2002, Dutch consumers are prepared to use their PIN and/or chip cards.
– Dutch enterprises have now buckled down to matters euro, with preparations and implementation moving smartly ahead.
– A lot still needs to be done, but businesses see few bottlenecks.
– A growing number of businesses now plan to switch over to euro business records on ‘e-day’.

1 European Commission, Findings of the Eurobarometer 55, Brussels (July) 2001. The fieldwork for this survey was carried out in April and May 2001.

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Table 3 Administration partially or fully changed over to euros

As a percentage

<table>
<thead>
<tr>
<th></th>
<th>Completed</th>
<th>From 1 January 2002</th>
</tr>
</thead>
<tbody>
<tr>
<td>Small enterprises</td>
<td>17</td>
<td>21</td>
</tr>
<tr>
<td>Medium-sized enterprises</td>
<td>31</td>
<td>34</td>
</tr>
<tr>
<td>Large enterprises</td>
<td>32</td>
<td>38</td>
</tr>
</tbody>
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