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MONETARY SOVEREIGNTY IN CONTEXT OF EUROPEAN INTEGRATIONS Comparative Study upon a Student Population in Croatia and Bosnia and Herzegovina

Abstract

Monetary sovereignty allows control over national monetary policy, exchange rate and currency circulation and is a sign of national central banks' independence. It is an instrument for fulfilling national economy goals and, especially in small countries, is an ultimate part of national sovereignty (like the hymn or national flag).

On the other hand, the process of (European) monetary unification requires from member countries to transfer their national sovereignty to a supranational level. The monetary policy then becomes a "one-size-fits-all" and is oriented towards common goals, putting national interests to the second place. The common opinion, especially in transition countries, is that entering European economic and monetary union is their final and ultimate goal that requires long term, committed fulfilling of rigorous criteria. But, the recent crises throughout European monetary union can be discouraging for accession countries, while the common monetary policy is confronting serious difficulties.

This paper analyses recognition on monetary sovereignty in context of European integrations on a sample of student population for the final years of undergraduate study at Faculties of Economics and Business in Zagreb (Croatia) and Mostar (Bosnia and Herzegovina). Our aim was to explore their perception of both monetary sovereignty and European integrations in turbulent circumstances of global financial crisis. The study was based on a questionnaire and, oriented primary to the qualitative explanations, included also the ranking of given (dis)advantages of the sovereignty and integrations on a given scale.

Key words: *sovereignty, monetary policy, Croatia, Bosnia and Herzegovina*

JEL: E42, E58

1. INTRODUCTION

Monetary sovereignty (especially in smaller countries) traditionally is considered as an important part of national economic and political sovereignty. Although it is manifested mainly through the control of national monetary and exchange rate policy (including the national currency emission), in its overall sense it is a complex issue that consists of more than just an economic aspect.

As the opposite from national monetary sovereignty, there are processes of economic and monetary integration. They result in transposing national monetary sovereignty to the supranational level, common currency and *one-size-fits-all* monetary policy, as is the case of European Union counties. Additionally, for the full membership in the euro zone, accession

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countries need to fulfil numerous criteria, given in Maastricht and Copenhagen Treaties. But, besides the common arguments in the debate of pros and cons of full membership in the European economy and monetary union, the current global crises shed a new, more cautious, light on the future of European integrations. There is a wide and growing discussion on characteristics and roots of *euroscepticism*, a term that was coined in the 1980s, referring to the (growing) scepticism about the European integrations. Although the euroscepticism was not a question of our primary interest, it is assuredly important for the research. Yet, countries in transition (including the two from our sample) still consider EU membership as their ultimate goal and the proof of success in economic policies.

Our interest for the study was to recognise the attitude and the pros and cons of European integrations (and, on the contrary, national sovereignty) on the side of younger population that has some knowledge and a critical attitude to the subject. That is why goals of the study were twofold: to explore the attitude of students' population about the accomplishments of national monetary sovereignty and, secondly, analyse both positive and negative consequences of European integrations, based on rankings of the (dis)advantages for both sovereignty and integrations. Because of the rigid monetary policies during the previous years (resulting in stable currencies and high levels of foreign – exchange reserves, but also in real economy rigidities) and the high level of euroization, national currencies were primarily accomplishing the transaction function of money. Furthermore, global financial crisis opened numerous new questions in terms of central banking and, jeopardizing the stability of European union and euro, shed a new light on the benefits and costs of full EU membership.

The paper is organized as follows: after the introduction, there is a short discussion on theoretical and literature background of monetary sovereignty. In the third part, we present the results of the research in both countries and a discussion. Finally, the last part concludes.

2. ON MONETARY SOVEREIGNTY – LITERATURE REVIEW AND THEORETICAL BACKGROUND

The role of central bank, monetary sovereignty and characteristics of monetary and economic integrations are widely described in literature. The relation between political and monetary sovereignty is particularly important for small open economies, considering also the consequences of monetary integrations. Monetary sovereignty includes essentially three exclusive rights for a given state (Mann, 1992, 460):

- the right to issue currency, that is, coins and banknotes that are legal tender within its territory
- the right to determine and change the value of that currency; and
- the right to regulate the use of that currency or any other currency within its territory.

Božina, L. (2008, 507 - 508) is analysing motivation for giving up national political and monetary sovereignty in exchange for a membership in any kind of integration. Although this, supranational sovereignty might ensure the sense of stronger financial stability and protection in a globalized world, the question of its control still remains open. Apart from the gold standard models, in monetary systems based on inconvertible paper currency central bank has to be independent, especially from political pressures. Still, there are no clear evidence that the political autonomy of central bank would lead to price stability and credibility.

The countries from our sample have strong limitations on their monetary sovereignty; especially in terms of currency board arrangement in B&H. Currency board's currencies are based on the full, on-demand convertibility with stable, foreign anchor currency that is usually regulated by the national law on central bank. In such cases, national monetary sovereignty is only formal and central bank is a *warehouse* institution while exchange rate stability is the ultimate goal. Despite the fact that *de jure* regime in Croatia is described as

managed floating, its narrow margins of fluctuation, strong commitment of national central bank to price stability goal and high level of euroisation (reflected also in exchange reserves) makes it *de facto* a *quasi* currency board. So, the politics in both countries during the previous period resulted in stability but also, since based on the exchange rate anchor, were rather passive.

The European integration processes result in transposing of national sovereignty to the supranational level of European central bank (ECB), with governors of national central banks in counselling functions. The concept developed by the ECB requires independence in terms of (1) institutional independence; (2) legal independence; (3) personal independence of the members of its decision-making bodies; (4) functional and operational independence; (5) financial and organizational independence.

It has been mentioned in the introduction of the paper that there is a common perception on the necessity of EU membership and fulfilling all the criteria required as the ultimate goal for the accession countries. Still, there is a rising “popularity” of euroscepticism, apart from the political parties and on the ground of “ordinary” people. The euroscepticism in Croatia on the sample of student population was studied at the Department of Economics at the University Juraj Dobrila in Pula (Kersan-Škabić, I., Tomić, D. (2009)). The results indicated that the roots of euroscepticism are in economic costs of Croatian entrance in the EU. Besides the lost of sovereignty (that was indicated as a reason for being euro sceptical), they also highlighted the fear of poverty and exploitation of national resources and stronger emigration pressures. On the other hand, there were observed some positive aspects of EU membership, such as better employment possibilities, higher living standards and more efficient state of law. Our interest in terms of the euroscepticism was partial and oriented primary on its influence on our analyses of monetary sovereignty. In our research we analysed the level of criticism to the EU membership separately using the ranks of given statements about (dis)advantages of monetary sovereignty and integrations.

3. RESEACH OF STUDENTS POPULATION ATTITUDE ON MONETARY SOVEREIGNTY AND EUROPEAN INTEGRATIONS

As previously explained, our first goal was to explore student’s statements about monetary sovereignty and advantages of its retaining while the second goal was oriented to he perception of membership in European economic and monetary union. Specific objective of this research is an attempt to determine the level of influence of national monetary regime characteristics in the two countries included in the research (considering monetary autonomy in Croatia and currency board in B&H) on students' attitude about the importance of national monetary sovereignty on its path to the wider economic integration. Research was conducted among third year students of business economics that are familiar with the concept of monetary sovereignty. That is why the criterion for the selection of the sample included in the survey within the whole undergraduate student population was the Monetary Policy course (at least attending the lectures) both at the faculties in Mostar and Zagreb. This type of research has been done only within limited areas so far, like those on the Istria region that is cited also in this paper. There are no relevant researches for the whole student population in B&H and Croatia. Future researches should be extended to other students of Faculties of Economics in Croatia and Bosnia and Herzegovina and aimed towards the actualization of the sovereignty issues in terms of financial instability.

3. 1. RESEARCH METHODOLOGY

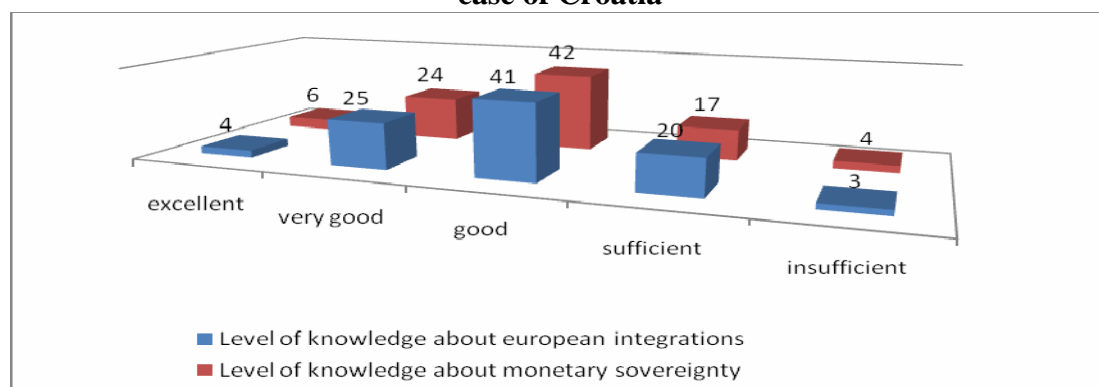
The research was done during May and June 2010 using the questionnaire, on a sample that consisted of 93 students from the Faculty of Economics and Business in Zagreb, Croatia and 53 from the Faculty of Economics in Mostar, Bosnia and Herzegovina. Students anonymously filled the questionnaires during the class, after the aims of research were explained. The same questionnaire was used for both countries. The questionnaire was structured towards more qualitative, than quantitative research methodology and descriptive statistics that leaves us scope for further research in the field of study, especially with the recent consequences of global crises on the EU member countries.

3. 2. RESEARCH RESULTS

The sample for Croatian part of research consists of 93 students of the final year of undergraduate study on the Faculty of Economics & Business (at the University of Zagreb). During the earlier years of study they passed courses with elementary knowledge on the European integrations and monetary sovereignty so the researchers assumed that they were representative sample. However, the first step was to ask the students to self-esteem their level of knowledge about European integrations and monetary sovereignty³

Graph 1.

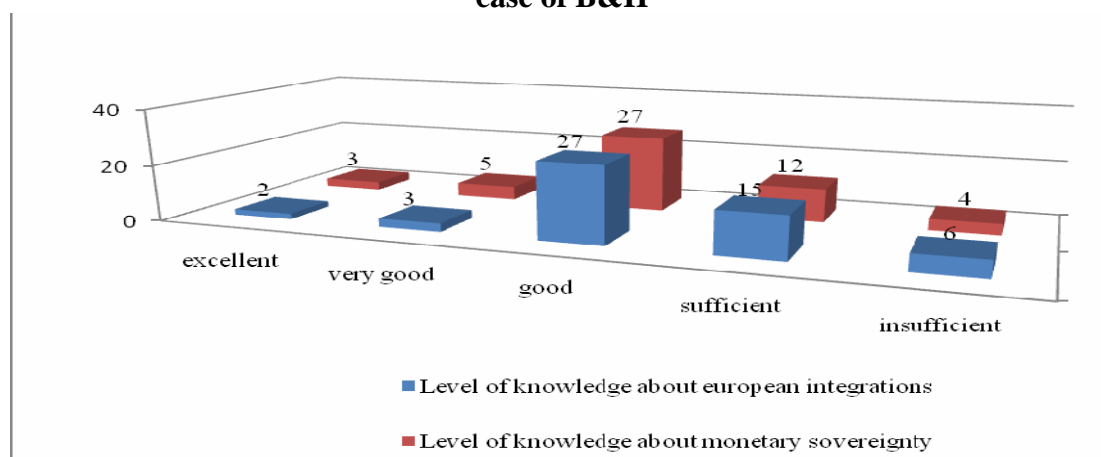
Self esteemed level of knowledge on monetary sovereignty and European integrations, case of Croatia



Source: author's calculations based on the questionnaires

The majority of students in Croatian sample (Graph 1.) verified their knowledge as “good” both in terms of European integrations (41 or 44%) and monetary sovereignty (42 or 45%). Furthermore, the answers were in ranges from very good to sufficient (92, 4% for the level of knowledge about European integration and 89, 2% on monetary sovereignty), while extreme values (excellent and insufficient) had low shares. This has shown that there is a solid base for further discussion on the subject.

³ For easier evaluation, we used a five-grade scale, similar to those used on the students' exams

Graph 2**Self esteemed level of knowledge on monetary sovereignty and European integrations, case of B&H**

Source: author's calculations based on the questionnaires

The majority of students in the B&H (Graph 2.) sample verified their knowledge as “good” both in terms of European integrations (27 or 51%) and monetary sovereignty (27 or 51%). This has shown that there is a solid base for further discussion on the subject.

Next four questions were related to the perception of the (dis)advantages of national monetary sovereignty and the consequences from participation in wider economic and monetary integrations.

The 53% of students from the sample agreed with the statement that *Croatia does not sufficiently use advantages of monetary sovereignty (Graph 2.1.)*, while 20% disagreed. A little surprising was the high share (27%) of those that were indecisive about the right answer. The 72% of students in Bosnia and Herzegovina from the sample agreed with the same statement (*Graph 3. 1.*), while 19% disagreed. Just 9% of the students from this sample were indecisive. With given answers on first set of questions students population showed rather negative perception with current monetary regime, despite the stability of national currencies, especially in B&H. Orthodox currency board that has been in use in this country since 1997, with its strong restrictions of national monetary policy discretion is recognized as a strong barrier to the monetary but also to the active economic policy.

On the other hand, 57% of Croatian students did not agree with the statement that *for small open economies national currency can be more harmful than advantageous (Graph 2.2.)*, while 28% agreed. Lower than for the previous question, but still rather high (15%) was the share of those that not agree nor disagree. The results for B&H were quite similar since 58% of students did not agree with the statement (*Graph 3. 2.*), while 34% were negative. Lower than in Croatia, but still rather high (8%) was the share of those that did not have a clear opinion.

Graph 2. (1. and 2.)– Monetary sovereignty: advantages and disadvantages, case of Croatia



Graph 3. (1. and 2.)– Monetary sovereignty: advantages and disadvantages, case of B&H

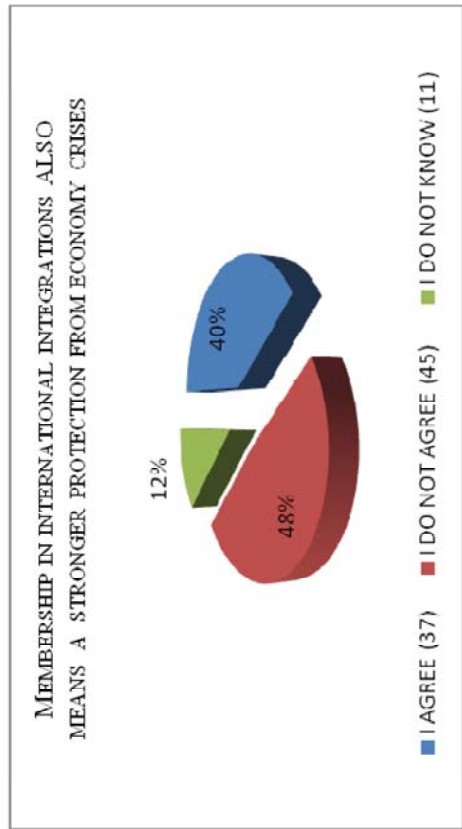
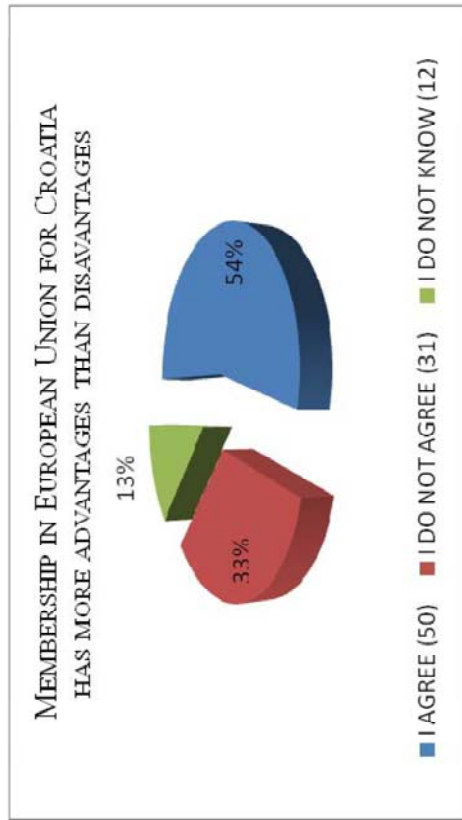


Source: author's calculations based on the questionnaires

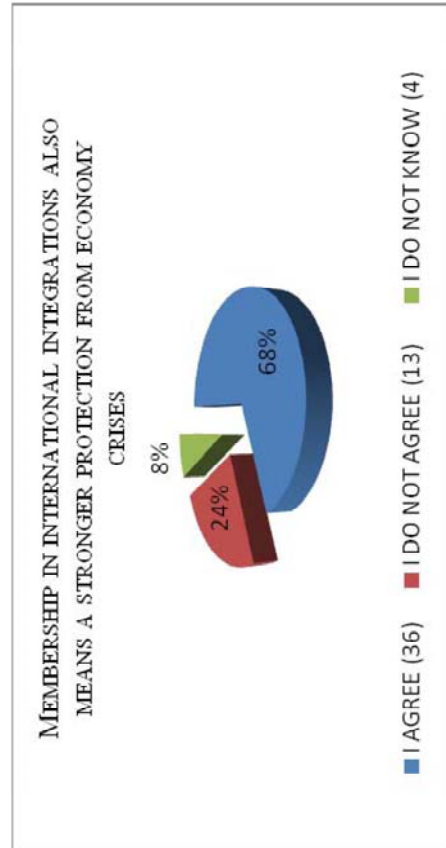
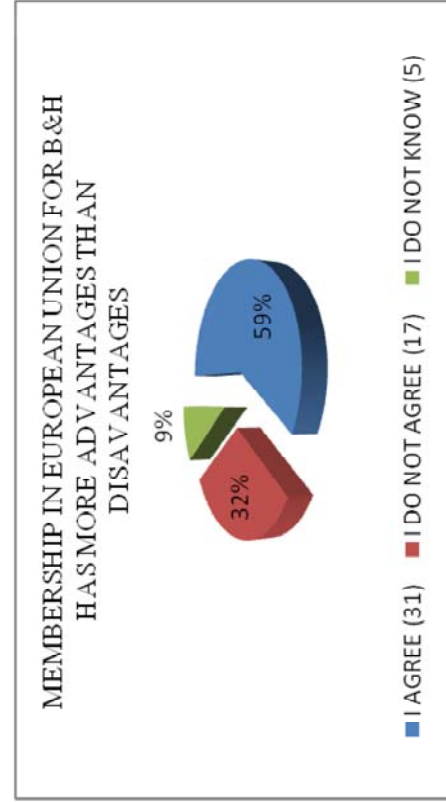
Besides the problems that the European Union is confronting during this global financial crisis, the level of support for monetary integrations is still rather high. In terms of membership as a protection from economy crisis, 68% of students in B&H agreed, while 8% were indecisive; the rest of them (24%) disagreed (the statement assumed that *membership in international integrations also means a stronger protection from economy crises*, Graph 5. 1.). Rather high share, 59% of examinees, agreed with the statement that *membership in European Union for B&H has more advantages than disadvantages*, while 32% disagreed and 9% were indecisive (Graph 5. 2.). This strong support is not surprising and was expected considering the criticism on insufficient use of national monetary policy (shown in the previous set of questions) and knowing that the currency board rules result in strong adjustment of the two economies.

In the Croatian sample, the students were more indecisive (Graph 4. 1.): 48% of students did not agree, while 40% agreed that *the membership in the integrations would mean protection from economy crisis*. The rather high amount (12%) did not have a clear answer. Positive attitude on the *advantages of European integrations* is shown in the 54% of agreement, while 33% disagreed and the rest (13%) were indecisive (Graph 4. 2.).

GRAPH 4. (1. AND 2.) –EUROPEAN INTEGRATIONS: ADVANTAGES AND DISADVANTAGES, CASE OF CROATIA



GRAPH 5. (1. AND 2.) –EUROPEAN INTEGRATIONS: ADVANTAGES AND DISADVANTAGES, CASE OF B&H

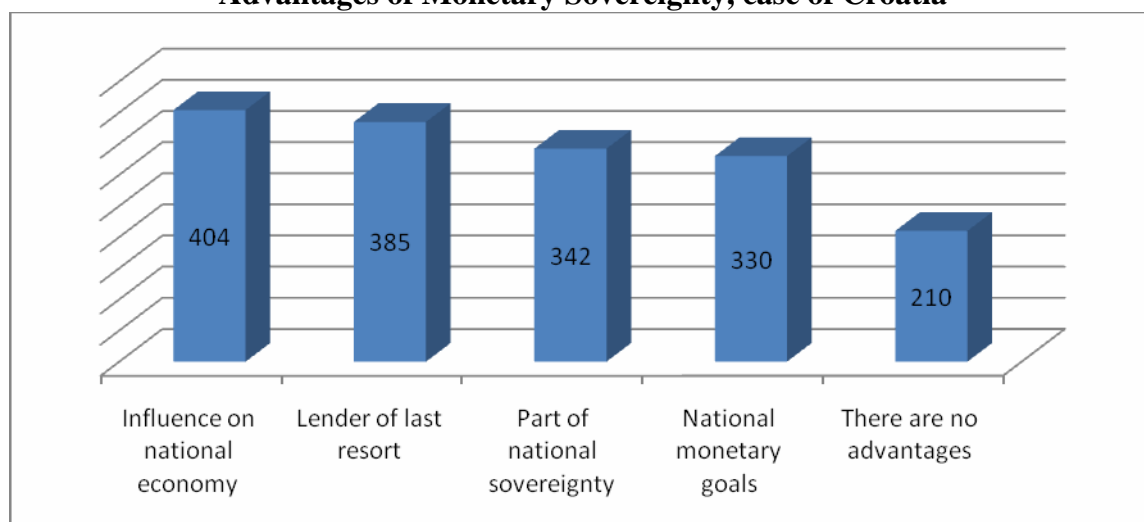


Source: author's calculations based on the questionnaires

Our next set of questions was oriented on ranking the advantages of monetary sovereignty and those of EU membership. The examinees were asked to verify the statements on a scale from 1 – 5 based on their importance (as a points from 1 (the lowes) to 5 (the highest)) on the advantages of monetary sovereignty.

Graph 6.

Advantages of Monetary Sovereignty, case of Croatia



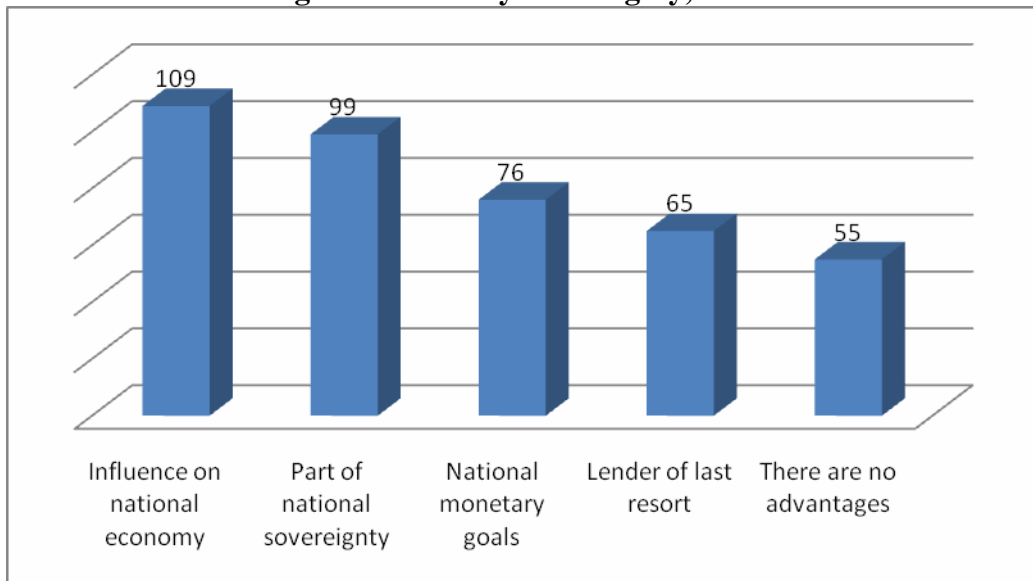
Source: author's calculations based on the questionnaires

In terms of *the advantages of monetary sovereignty* (Graph 6) the best ranks in Croatia were given to the “classic” functions: possible influence of (independent) monetary policy to the national economy with its measures and instruments and, on the second place, the lender of last resort function in the case of crisis. The results confirmed recognition of monetary sovereignty as a part of national sovereignty described above giving it the third place rank. It is closely followed with the possibility to favor national monetary goals. As anticipated, the lowest ranks were given to the statement that there are no advantages of monetary sovereignty. On the part of B&H (Graph 7.), the results were quite similar. Expectedly, the best rank was given to the possible positive influence of independent, active monetary policy.

Lower than in Croatia, fourth placed rank of a function of lender of last resort is a result of monetary regime, since Central bank of Bosnia and Herzegovina cannot provide this function to the commercial banks in B&H

Graph 7.

Advantages of Monetary Sovereignty, case of B&H

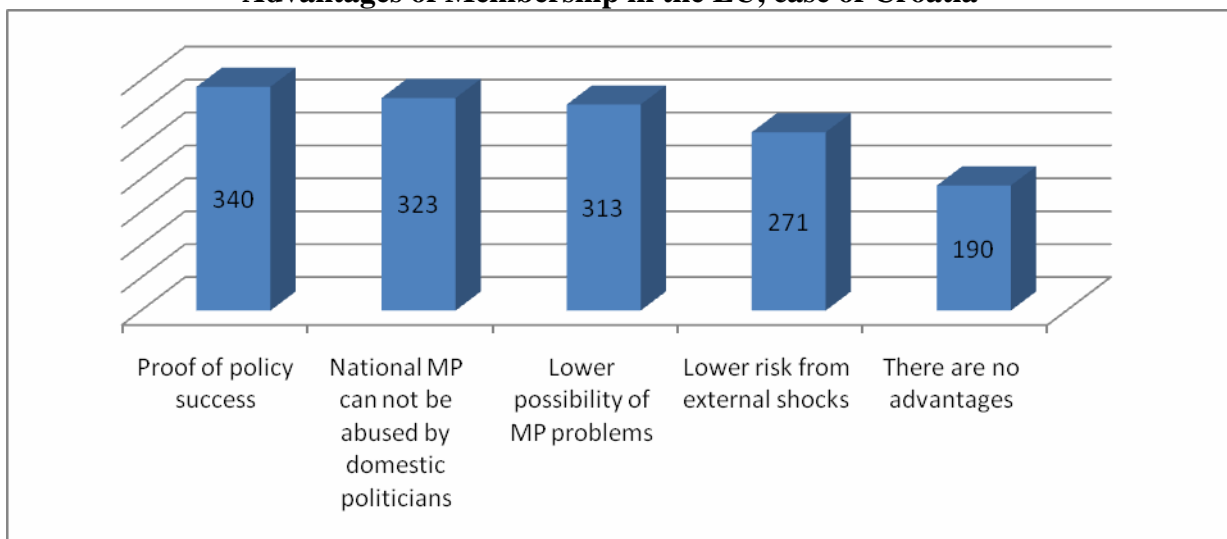


Source: author's calculations based on the questionnaires

The same model was used for ranking *the advantages of the EU membership* (Graph 8 for Croatia). The best total ranks, with rather small distances, the examinees in Croatia gave to the facts that (consecutive) the EU membership is a proof of policy success in terms of fulfilling the predetermined criteria, national monetary policy within an integration can not be abused by the domestic politicians and EU membership will reduce the possibility of problems in terms of monetary policy. The modest ranks were given to the possibility of lowering the risk from external shocks as an advantage of EU membership, while, again not surprisingly, the lowest ranked was the answer that there are no advantages of membership in the EU.

Graph 8.

Advantages of Membership in the EU, case of Croatia

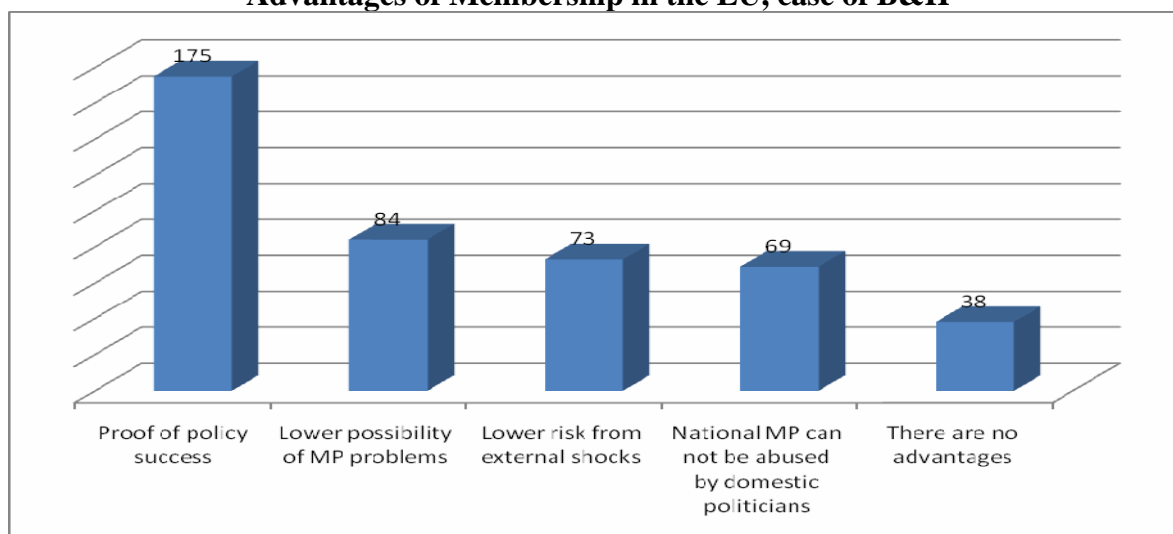


Source: author's calculations based on the questionnaires

In terms of B&H (Graph 9) the highest total rank was also given to the proof of policy success, while all other statements had more than double lower ranks.

Graph 9.

Advantages of Membership in the EU, case of B&H



Source: author's calculations based on the questionnaires

Analyzing the advantages of monetary integration for candidate country or, in other words, the arguments that can justify losing monetary sovereignty are: lower possibility of monetary policy problems (currency board is unique logical solution for country with complex social order and unresolved political problems), fear from political pressure and central bank independence in connection with it accountability to nation, and protection from external shocks.

CONCLUSION

Monetary sovereignty is a part of national sovereignty and is probably the most visible in policy of independent national central bank and national currency. On the other side, there are benefits and costs of economic and monetary integrations, especially for small open economies. There is a live and ongoing debate on national exchange rate policy, but our interest was oriented primary on the students of the faculties of economics that already have some knowledge on the matter and are informed on the subject.

We used a qualitative questionnaire in order to analyse the level of knowledge and the attitude about the european integrations of the students population in Bosnia and Herzegovina and Croatia. The motivation for research was complex. First, we were interested in the perception of consequences of orthodox monetary policy on monetary sovereignty perception in terms of the global financial crises. Second, we aimed to explore the opinion about the monetary union membership, since it is usually considered as the ultimate goal for those countries, even in case of negative consequences to the member countries. Finally, we tried to rank the (dis)advantages of monetary sovereignty and EU membership that are commonly mentioned in the literature.

The results obtained with this research presented a rather high level of criticism to the monetary policies in the two countries, especially in B&H. Generally, in both countries the attitude to the European integrations is positive, although the opinion that the wider integrations also means protection from economy crises had stronger support in B&H than in Croatia. Influence of monetary sovereignty on national economy was ranked as its most important advantage, while EU membership in both cases was recognised as a proof of successful policy in the previous period. Although there is a support to the process of

monetary integrations, the students are aware that the EU membership will not protect them from the potential future economy crisis, although it can protect them from the political pressures and lower the possibility of problems in monetary policy.

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MONTARNA SUVERENOST U KONTEKSTU EUROPSKIH INTEGRACIJA Komparativna studija na studentskoj populaciji u Hrvatskoj i Bosni i Hercegovini

Sažetak

Monetarna suverenost omogućuje kontrolu nacionalne monetarne politike, tečaja i kolanja valute te je znak neovisnosti centralne banke. To je instrument ispunjavanja nacionalnih ekonomskih ciljeva i, posebno u malim zemljama, krajnji pokazatelj nacionalne suverenosti (poput himne i državne zastave). S druge strane, proces (Europskog) monetarnog ujedinjavanja od zemalja članica zahtijeva prijenos njihovog nacionalnog suvereniteta na nadnacionalnu razinu. Monetarna politika tako postaje jednaka za sve i usmjerena zajedničkim ciljevima, stavljajući nacionalne interese u drugi plan. Uvriježeno je mišljenje, posebice među tranzicijskim zemljama, da je ulazak u Europsku ekonomsku i monetarnu uniju njihov najveći i krajnji cilj koji iziskuje dugoročno i predano ispunjavanje rigoroznih kriterija. No nedavna kriza koja se osjetila u cjelokupnoj Europskoj monetarnoj uniji može za zemlje pristupnice biti obeshrabrujuća jer je zajednička monetarna politika suočena s ozbiljnim teškoćama. Ovaj rad analizira prepoznavanje monetarnog suvereniteta u kontekstu Europskih integracija na uzorku studentske populacije na zadnjim godinama dodiplomskog studija na Ekonomskim Fakultetima u Zagrebu (Hrvatska) i Mostaru (Bosna i Hercegovina). Naš je cilj bio istražiti njihovu percepciju monetarnog suvereniteta i Europskih integracija u turbulentnim okolnostima globalne financijske krize. Istraživanje se baziralo na upitniku i, uz orijentaciju uglavnom na kvalitativna objašnjenja, uključivalo je rangiranje danih prenosti/mana suvereniteta i integracija na zadanoj skali.

Ključne riječi: suverenitet, monetarna politika, Hrvatska, Bosna i Hercegovina