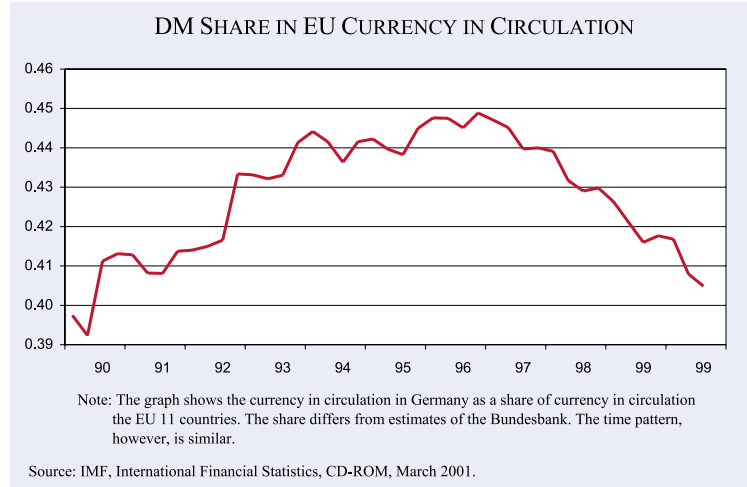


WHY HAS THE DM-SHARE FALLEN?

The share of deutschmarks in the joint Euro-11 stock of money in circulation has declined rapidly in recent years. In the first quarter of 1997, it was nearly 45%, and when the euro was introduced it was still 43%. Two years after the introduction of the euro it had declined to only 40%, and an end of the downward trend is not in sight.

Only a small part of the reduction in the DM share is explained by a decline of Germany's share in aggregate EMU-GDP during the relevant period. Since Germany's black market share in GDP is not above the European average, but the deutschmark is the only European currency to be extensively used in eastern Europe, there is hardly another explanation for this decline in share than that deutschmarks are returning from eastern Europe and other parts of the world.



The reduced preference of the east Europeans lowers the value of the euro and the European interest rate in the absence of ECB intervention. If the ECB intervenes passively (selling bonds for money balances) so as to stabilise the interest rate, the euro will still decline, although to a lesser extent, as more European bonds are held in the aggregate international portfolio of all private agents.

See H.-W. Sinn and F. Westermann (2001), "Why Has the Euro Been Falling? An Investigation into the Determinants of the Exchange Rate," CESifo Working Paper No. 493. R.K.