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EVOLUTION AND CONTEMPORARY TRENDS OF THE INTERNATIONAL MONETARY SYSTEM

РАЗВОЈ И САВРЕМЕНЕ ТЕНДЕНЦИЈЕ МЕЂУНАРОДНОГ МОНЕТАРНОГ СИСТЕМА

Summary: *The growth dynamics of international exchange and capital flows is conditioned by the efficiency of the international monetary system whose basic task is to provide for international liquidity and smooth international payments. The tendencies in international economic relations in the time of globalisation have determined further directions for the development of the international monetary system. The breakup of the Bretton-Woods System initiated the establishment of a new European monetary system with the aim to stabilise the exchange rates and improve further process of integration and international economic relations. In this research paper we have pointed out to the fact that economic interdependence of sovereign countries leads to coordination of macroeconomic policies, and that it can motivate monetary integration within the monetary policy. The objective of this research paper is to emphasize the stability of the international monetary system as a prerequisite for sustainable growth of national economies and monetary union. The contemporary international monetary system is characterised by the trend of reduced number of national currencies, as this is a logical consequence of increasing European integrations, but also because of significant economic advantages. Simultaneously, the costs of the euro changeover and introduction of a common currency are lower if economic performances of member countries mutually converge.*

Keywords: *International monetary system, International Monetary Fund, European monetary system, monetary union, monetary convergence criteria, economic growth.*

JEL classification: *E52, F36*

Резиме: *Динамика раста међународне размјене и токова капитала условљени су ефикасним међународним монетарним системом чији је основни задатак омогућити међународну ликвидност и несметана међународна плаћања. Тенденције међународних економских односа у условима глобализације, одредили су даље правце развоја међународног монетарног система. Сломом Бреттон-Вудског система настају импулси за нови, Европски монетарни систем, а у циљу стабилизације девизних курсева, унапређења даљег процеса интеграције и међународних економских односа. У раду смо указали да економска међузависност суверених држава води координацији макроекономских политика, а у области монетарне политике може бити мотивација за виши степен монетарне интеграције. Циљ рада је истаћи значај стабилности међународног монетарног система као предуслова за одрживи раст националне економије и монетарне уније. У савременом међународном монетарном систему карактеристичан је тренд смањења броја националних валута, као логична посљедица растућих економских интеграција, али и због значајних економских предности. Истовремено, трошкови промјене и увођења јединствене валуте су нижи уколико економске перформансе земаља чланица уније међусобно конвергирају.*

Кључне ријечи: *међународни монетарни систем, златни стандард, Европски монетарни систем, монетарна унија, монетарни критеријуми конвергенције, глобална криза.*

ЈЕЛ класификација: *E52, F36*

1. INTRODUCTION

Efficient international monetary system and stable monetary medium which would function as international means of payment, international monetary reserves and clearing means of payment in international transactions distinguishes itself as a prerequisite for the development of international trade and capital flows. Contemporary international monetary systems reflect complex economic and socio-political relation and as such should be observed from various aspects.

Evolution of contemporary international monetary system has started on the principles and systems of the gold standard. The backbone of the gold standard was defining the value of a national currency by a stated quantity of gold and its unrestricted convertibility into gold. By fixing a currency price to gold, the gold standard aimed to restrict the monetary increase in the world economy providing thus stability of the world price level. The first organised forms of international monetary systems were therefore based on the gold standard system. Discovery of big gold deposits in the

middle of XIX century led to the establishment of gold value as a system of monetary organisation throughout the world. Successful functioning of the gold standard colided with the transfer to liberal stage of capitalism in which conditions for its automatism in regulation of international monetary relations were met. At that time Great Britain was the leading economic power in international trade and was simultaneously developing its financial institutions, which made it become the center of international monetary system.

Increase of the USA role in the world economy as well as tendencies in international economic relations in globalisation have determined further directions for the establishment and development of international foreign currency and monetary system. Goals of countries' internal policies after the period of the gold standard have been gaining on importance, and attempts to reestablish the gold standard have resulted in creation of different systems of fixed exchange rates. The end of the World War II was also the beginning of reforms of the international monetary system which endeavaoured to reconcile the goals of internal and external equilibrium. Having learned from the consequences of the World War II, the allies started to propose a new changed form of the international monetary system, the result of which was the establishment of the Bretton-Woods international monetary system.

Due to changes in international economic relations in the end of the 1960s, the establishment of the new world monetary and exchange rate system was initiated. The European Monetary System was established with the goal to stabilise the exchange rates, improve further integration process and contribute to stabilisation in international economic relations. The European Monetary System delivered satisfying results, as it provided for convergence, decrease in inflation rate and exchange rates stability. Monetary stability and discipline imposed by the System led to price stability, which was the goal of monetary policy even in the countries with relatively high inflation rates. The success of the System initially created to protect Europe from international exchange rate disturbances accounted for the establishment of the monetary union as the consequent step. Being the highest stage of the European integration, the monetary union could succeed only with the economic convergence of its member countries.

This paper demonstrates that economic interdependence of sovereign countries leads to coordination of macroeconomic policies, which within the monetary policy can be motivation for monetary integration. This derives from the fact that introduction of a common currency has significant economic advantages-lower transaction costs, higher price transparency and monetary stability. Simultaneously, the costs of the euro changeover and introduction of a common currency are lower if the economic performances of member countries mutually converge. The member countries' convergence from the aspect of the currency criteria shows that values and levels of inflation rate, height of interest rates on government bonds and exchange rate mechanism were a prerequisite for the establishment of the union and an indicator of stable movements in the contemporary monetary system. However, escalation of the global crisis led to great market oscillations, instability and assymmetric shocks in various countries.

2. CHARACTERISTICS AND DEVELOPMENT OF THE INTERNATIONAL MONETARY SYSTEM

In the period before the World War I the world economy was based on the gold standard, which was a guarantor of printing paper money with gold coverage and which implied direct gold convertability for the majority of currencies. „Linking currencies' value directly to gold caused the establishment of an international financial system with a fixed exchange rate between currencies. “A significant advantage of the fixed exchange rate according to the gold standard was in stimulating the world trade, as the fixed exchange rate eliminated uncertainty as part of the fluctuating exchange rate.“ (Mishkin 2006). The gold standard implied the following basic rules necessary for its regular functioning and respect by the countries which accepted it:

- monetary authorities of each country had to determine the fixed value of the national currency in gold;
- there was free import and export of gold;
- there was possibility of automatic money supply fluctuation depending on the gold status and movements and

- there was sufficient prices and wages flexibility.

The fact that the monetary authorities of the respective countries respected the regulations enabling the functioning of the gold rule provided for automatic equilibrium between balance of payments and world prices.

During the gold standard the main responsibility of the central bank was securing the official parity between its own currency and gold; for the maintenance of this price, the central bank needed adequate gold reserves. Creators of the policy have thus considered the external equilibrium not in the context of the aimed current account status, but as a situation in which the central bank neither acquired some gold from abroad nor (which is more important) lost it too fast in relations with other countries (Krugman and Obstfeld 2009).

Nevertheless, the flow of gold between the countries changed with time, which simultaneously led to frequent oscillations of the money amount and prices, and pointed to the fact that by respecting the gold standard a country had no control over its monetary policy, as the money amount depended on the flow of gold between countries. The focus was on external goals, i.e., putting the world economic stability ahead of internal stability and economic policy. This makes us conclude that the gold standard was the first form of transfer of the monetary sovereignty of one national economy and weakening of the central banks' discretion right in conducting monetary policy.

The First World War marked the end of the gold standard, as due to recession and great market disturbances countries were not any longer capable of converting their currencies in gold. International liquidity became a more frequent issue because of continuous fear that the world monetary gold reserves were not sufficient to provide for smooth international payments. The war and great expenditures for its financing, and thereafter for the recovery of the war-torn economies, great economic crisis and economic policies with the focus on full employment significantly changed circumstances in which the international monetary system was functioning. Many countries were considering options between external and internal equilibrium, which led to monetary desintegration at the beginning of the 1930s.

2.1. Bretton-Woods international monetary system

The increase of the USA role in the world economy and the establishment of new international relations have determined directions of the establishment and development of the new monetary system. After the period of gold standard, the goals of countries' internal policies were becoming increasingly important, and attempts to reintroduce the gold standard resulted in formation of different systems of fixed exchange rates. Just before the end of WWII, the allies started suggesting a new form of international monetary system. Although there were four plans suggested for the organisation of international monetary cooperation, White's Plan was chosen to be the basis for the establishment of an international financial organisations. The Plan was based on the main principles of the agreement signed by 35 out of total 44 countries present at the conference in the American city Bretton Woods in 1945.

White's Plan reflected the economic and political policy of the USA which was then economically stronger than the majority of countries, and with huge gold reserves. The Plan introduced by White recommended a kind of universal acceptance of the gold standard. The new system was guided by the following principles:

- monetary policies in the world can be adequately governed only with the full cooperation of all, and primarily of the main financial centers in the world and
- international equilibrium cannot be established unless there is internal equilibrium and economic policy of each country has to be directed to the achievement of internal and external equilibrium.

Taking into account the fact that after the WW I the USA was the most powerful economy, the majority of international exchange transactions were conducted in dollars, and thus the basic characteristic of the Bretton-Woods system was the establishment of the fixed exchange rate based on the convertability of the US dollar in gold. Central banks were buying and selling dollars and were keeping them as exchange rates and through operations at the exchange market they were maintaining

the exchange rate. The US dollar which was used also by other countries to nominate the funds kept as exchange reserves was granted the status of reserve currency (Mischin 2006).

When subjects abroad, primarily central banks, want to keep their exchange reserves in foreign currency, this means that the respective foreign currency has the status of the world reserve currency. The second important proof that one currency represents a world reserve currency is the fact that it is often used in international financial transactions. Today this is the role of the US dollar and euro. International status of dollar was established in Bretton Woods system (Kovačević 2014).

The International Monetary Fund and the International Bank for Reconstruction and Development were established on the basis of the Bretton-Woods agreement. The basic task of the International Monetary Fund was to promote the development of the world trade by establishing rules for the maintenance of the fixed exchange rate and by granting loans to countries facing difficulties in the balance of payments (crediting their deficit). Advancement of the international cooperation through consulting and joint problem solving of monetary issues, growth of the international trade, employment, income and production increase, stabilisation of exchange rates and prevention of competitive depreciation have been pointed out to as the basic functions of the Fund. Besides the aforementioned, some of more important functions of the IMF are multilateralism in international payments for current transactions and removal of exchange restrictions impeding the increase of the international trade, provision of financial funds for helping the member countries to balance their balance of payments and decrease imbalances. The task of the IMF is not only solving problems of respective countries, but the functioning of the international monetary system as a whole for the purpose of the establishment of the world growth. Being such, the Fund represents today an inevitable financial institutions influencing the main global financial flows.

The Fund's capital was formed in the way that all member countries paid in certain quotes based on their economic capacity taking into account the following: amount of national income, gold or dollar reserves, average import and its movements. At the beginning there were 30 member countries in the IMF and until today the number of the member countries has increased to 188. However, when the Bretton Woods system collapsed in 1971, the IMF was entitled to much wider power of attorney and new, more important roles it had initially.

2.2. European Monetary System

The modern world economy is characterised by the trend of decreasing number of national currencies, which is a logical consequence of increasing international economic and monetary integrations. Domestic currency makes important constituent of the country's sovereignty, with the possibility of exerting active influence on real economy. A stable and convertible national money unit is thus considered to be a reliable economic measure of value and success of the economic system, especially in monetary policy.

Economic as well as political factors have always been the basis for European integrations: from the desire to prevent wars and destructions to economic benefits of enhanced integrations and establishment of democratic society in the entire Europe. Due to changes in international economic relations in the end of the 1960s new impulses for the establishment of the new world monetary and exchange system arose. It was said that the main reason for this was that "the sixties were the time of irresponsible inflationary monetary policy of the USA – which printed money for the financing of Vietnam War". With regard to the fact that at that time all main currencies were pegged to dollar (through global system of fixed exchange rates, i.e. Bretton Woods system), American inflation was transferred to Europe. This resulted in gradual breakdown of global system of fixed exchange rates. Historically, European Monetary System served as a bridge between Bretton Woods system, the center of which was dollar, and monetary union" (Baldwin and Wyplosz 2010).

Economic theory foresees that when reserve currency countries accelerate their monetary increase, as this was the case with the USA in the second half of the 1960s, one of the consequences is automatic rise of the monetary increase and inflation abroad, with regard to the fact that the foreign central banks buy reserve currency in order to maintain their exchange rates and increase their own money supply during this process (Krugmann and Obsfeld 2009).

As response to decreased demand for American dollar and divergence priority of economic policies of the EEC member countries, modes for recovery of the intereuropean stability of exchange rates were sought for. In order to stabilise their own prices and restore the internal equilibrium, they had to abandon fixed exchange rates and let their currencies fluctuate.

In 1977 the European Commission suggested the establishment of the European Monetary System which was founded at the conference of presidents and prime ministers of the Nine in Bremen in June 1978, and which came into force on 13 March 1979. At that time members of the EMS were all EEC member countries: Germany, France, Great Britain, Belgium, Netherlands, Luxemburg, Denmark, Ireland and Italy. The EMS was founded with the aim to provide for monetary cooperation and stability between the countries accelerating in this way the creation of common currency, monetary authority and monetary union in Europe and achieving higher level of economic integration. The European Community countries decided to establish stability system in Europe characterised by the lowest inflation rates, tighter economic cooperation between its member countries and prevention of negative effects of external economic shocks in form of too frequent dollar fluctuations. After the four-year adaptation of central exchange rates between member countries' currencies and alignment of economic policies, i.e. after 1983, better conditions for higher level of stability between the currency exchange rates in the EMS were created.

The European Monetary System is the most powerful instrument of monetary integration in Europe and creation of common economic and monetary union, with its explicit goals as follows:

- exchange rate stabilisation through more intensive monetary cooperation between the EMS member countries,
- advancement of further integration process and
- contribution to stabilisation in international economic relations.

3. EUROPEAN MONETARY UNION AS THE HIGHEST LEVEL OF MONETARY INTEGRATION

Generally speaking, the European Monetary System has delivered satisfying results, as during the 1980s it provided for convergence and decreased inflation rate with stability of the exchange rates. The European Monetary System was successful in securing monetary stability, whereas the discipline it imposed led to setting as objective the price stability in the countries with the relatively high inflation rates. This paved the way to higher European integration stage, as the economic convergence of the member countries is the basis for the establishment of economic and monetary union.

Table 1: Euro introduction stages

06/1990 Beginning of the first stage of EMU	01/1994 Beginning of the second stage of EMU	15–16/12/1995 Resolution of the European Council in Madrid	Beginning 1998 European Council Resolution	01/1999 Beginning of the third stage of EMU	2002 Beginning of currencies' replacement in Euro-effective money
First stage	Second stage		Third stage		
Total liberalisation of capital movement	European Monetary Institute was founded	European currency will be named Euro	Decision on final beginning of EMU 01/01/1991	Establishment of irrevocably fixed exchange rates	Euro becomes official currency in eurosystem
Coordination of economic, fiscal and monetary policy	Autonomy of national central banks	Transition scenario was established	Selection of the EMU member countries Foundation of the European Central Bank (ECB)	The ECB takes over the responsibility for monetary policy Beginning of replacement in euro in the financial sector	Replacement of currencies with euro banknotes and coins Denomination of all financial instruments in euro

Source: adapted from Lovrinović and Ivanov 2009

Number of instabilities in the world monetary relations and disagreements between respective Union members regarding measures that should be undertaken towards the establishment of a common

monetary union delayed the introduction of the common currency in Europe for 12 years. The establishment of the European Monetary Union underwent three stages, the first of which started in the 1990s. This first stage was characterised by the full liberalisation of capital with the aim to eliminate protectionism measures and restrictions of free capital movements. Simultaneously, the economic policies were coordinated, particularly monetary and fiscal policy, in accordance with the Maastricht convergence criteria. The second stage started on 01/01/1994 with the establishment of the European Monetary Institute with its headquarters in Frankfurt. The EMI is a predecessor to the European System of Central Banks whose headquarters is today in Frankfurt. During the second stage the national central banks still kept autonomy in implementation of the monetary policy (Lovrinović and Ivanov 2009). The third stage started by irrevocable fixation of exchange rates to euro and transfer of monetary sovereignty of the EMU member countries to the common central bank. The overall role of the monetary policy was taken by the European Central Bank in Frankfurt.

Creation of Monetary Union according to Maastricht Criteria implies meeting the monetary and fiscal convergence criteria in order to achieve optimal functioning and survival of the EMU. In this paper we will reflect on monetary criteria in order to emphasize the importance of stable and efficient monetary system.

3.1. Monetary convergence criteria

One of the basic characteristics of the European unification in all the stages of the European history is heterogeneity of the countries which make up the Union. This heterogeneity reflects in socio-cultural specificities, history and level of the economic development. (Vukmirica and Špirić 2005). Exactly the similarities between the member countries, primarily regarding their economic development are considered to be a prerequisite for successful functioning of the monetary union. Nominal convergence implies fulfilment of the quantitatively precised criteria on member country's readiness to enter the eurozone, as prescribed by the Maastricht Treaty.

A country is allowed to accede to the monetary union if it meets the required criteria of the monetary convergence (De Grauwe 2004) as follows:

1. its inflation rate is not higher than 1,5% in comparison to the average of the three lowest inflation rates of the member countries,
2. long-term interest rate on government bonds is higher than the average long-term interest rate in three member countries with the lowest inflation,
3. accepts exchange rate mechanism (EPM II) of the European Monetary System, and if 2 years prior to its accession to the Union it does not execute its currency devaluation.

3.1.1. Inflation convergence

The primary objective of the European Central Bank was set with the establishment of the monetary union and transfer of monetary sovereignty of the member countries to supranational central bank, which contrary to the quantitative objectives, prioritised the qualitative, i.e. stabilising objective of the monetary policy. Contrary to the Anglo-French banking model, the German model of the Bundesbank, which was accepted for the formation of the European Central Bank, emphasises the stability of prices as the primary objective of the central bank. According to the analytical frame of the monetary integrations, monetary union between two countries implies the existence of the common central bank, whereas it is pointed out that formation of a monetary union with a country with high inflation reduces the prosperity of the country with a low inflation. This is likely to derive from the fact that the common central bank reflects the average preferences of the member countries causing thus increase in the inflation rate of the Union - benefits from the monetary union are lost, i.e. transaction costs and risks are lower (De Grauwe 2012). In order to attain the primary objective, i.e. meet the inflation convergence criterion with this anti-inflation process, the member countries faced an inevitable temporary increase in unemployment (according to movements along the short-term Philip's curve).

With the development and enlargement of the monetary union, besides already mentioned heterogeneity of the member countries, Europe has been facing unequal increase in (macro) economic indicators of the member countries, which under the crisis circumstances particularly highlights the conduct of the common monetary policy. During 2004 eight middle and eastern European countries

and two Mediterranean countries became part of the European Union, and in 2007 Rumania and Bulgaria became its full members. Meeting the inflation convergence criterion within the nominal convergence criterion is an important step and demands effort from the new member countries on their way to monetary union.

Table 2: Inflation rates of the EMU member countries in the period 2003 to 2008

Year	2003.	2004.	2005.	2006.	2007.	2008.
EMU members						
Belgium	1,5	1,9	2,5	2,3	1,8	4,5
Germany	1	1,8	1,9	1,8	2,3	2,8
Estonia	1,4	3	4,1	4,4	6,7	10,6
Ireland	4	2,3	2,2	2,7	2,9	3,1
Greece	3,4	3	3,5	3,3	3	4,2
Spain	3,1	3,1	3,4	3,6	2,8	4,1
France	2,2	2,3	1,9	1,9	1,6	3,2
Italy	2,8	2,3	2,2	2,2	2	3,5
Cyprus	4	1,9	2	2,2	2,2	4,4
Luxembourg	2,5	3,2	3,8	3	2,7	4,1
Malta	1,9	2,7	2,5	2,6	0,7	4,7
Netherlands	2,2	1,4	1,5	1,7	1,6	2,2
Austria	1,3	2	2,1	1,7	2,2	3,2
Portugal	3,3	2,5	2,1	3	2,4	2,7
Slovenia	5,7	3,7	2,5	2,5	3,8	5,5
Slovakia	8,4	7,5	2,8	4,3	1,9	3,9
Finland	1,3	0,1	0,8	1,3	1,6	3,9
Reference value	2,2	1,3	3,7	4,2	1,2	2,5

Source: adaptation made by the author, adapted from Eurostat, European Commission 2008

According to the data from the Table 2, general evaluation is that there is a visible trend of inflation rate increase in all new member countries in the period from 2003 to the beginning of the recent crisis, i.e. 2008. Inflation rates movements are result of the then global increase in food and energy prices, which was clearly reflected in the price increase of the consumer basket in these countries during the observed period. New member countries also recorded high salaries increase which is not sustainable in the long term, as it does not accompany the appropriate productivity increase. Since the process of accession to the developed EU countries implies also higher inflation rate (Balasca-Samuelsom effect), they can be reduced by restrictive monetary and fiscal policy, which can result not only in lower increase and employment rates, but also in appreciations of the exchange rate. All this may lead to competition loss. A country can accede to the Union only if the inflation rate is not higher by 1.5% than the average of the three lowest inflation rates of the member countries.

3.1.2. Interest rate convergence

Long-term bond interest rate indicator represents a measure of continuity and sustainability of the country's convergence process, i.e. "reflection of the financial market on evaluation of the economic sustainability of the member country" particularly regarding stability of fiscal balance and risk premium. Interest rate convergence on long-term bonds is justified, as excessive differencies in interest rates prior to the accession to the Union may lead to great capital gains and losses when entering the EMU. This would cause great disturbances on national capital markets. But to be restricted, differences in interest rates have to be decreased before a country joins the EMU. On the other hand, the level of the interest rate is reflexion of investors' trust in country's finances and financial instruments and their inflatory expectations. The greater a member country's divergence from the fiscal convergence criterion, i.e. the farther the deficit from 3% GDP, the greater divergence between interest rates on member countries' government bonds (Akitoby and Stratman 2008).

Table 3: Long-term interest rates on government bonds of the EMU member countries in the period 2002 to 2017

Year	2002.	2007.	2010.	2013.	2017.
EMU members					
Belgium	4.99	4.33	3.46	2.41	0.72
Germany	4.78	4.22	2.74	1.57	0.32
Estonia	:(z)	:(z)	:(z)	:(z)	:(z)
Ireland	5.01	4.31	5.74	3.79	0.80
Greece	5.12	4.50	9.09	10.05	5.98
Spain	4.96	4.31	4.25	4.56	1.56
France	4.86	4.30	3.12	2.20	0.81
Italy	5.03	4.49	4.04	4.32	2.11
Cyprus	5.70	4.48	4.60	6.50	2.62
Luxembourg	5.41	5.28	10.34	3.34	0.83
Malta	6.06	4.54	5.57	3.83	0.31
Netherlands	4.70	4.46	3.17	1.85	0.54
Austria	5.82	4.72	4.19	3.36	1.28
Portugal	4.89	4.29	2.99	1.96	0.52
Slovenia	4.96	4.30	3.23	2.01	0.58
Slovakia	5.01	4.42	5.40	6.29	3.05
Finland	8.71	4.53	3.83	5.81	0.96
Reference value	4.91	4.32	3.60	2.99	1.09

Source: author's adaptation, adapted from Eurostat 2017

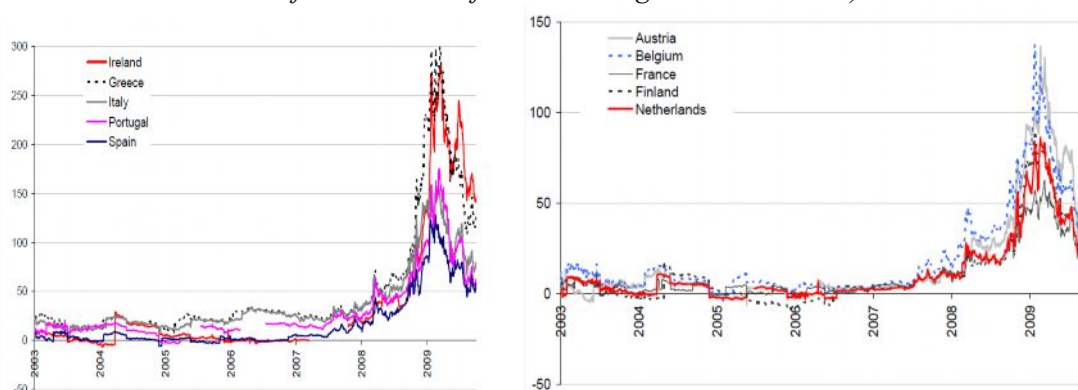
The Maastricht criterion specified permitted deviations of the long-term interest rates which in the EMU countries should not be higher than 2% from the average recorded in three countries with the lowest inflation (interest rate convergence criterion). The Table 3 displays negative convergence, i.e. divergence of interest rates on long-term government bonds during the crisis period. In 2010 there were significant differences as direct reflection of the most indebted member countries of the Union. Financial and economic crisis influenced rising need for financing the respective member countries of the Union and additional increase in indebtedness costs. Thus the increased difference in government bond yields signalled that investors were less motivated to lend money, which endangered this country's access to the international capital market and simultaneously increased indebtedness costs.

Market development urges creation of the government bonds yield curve. It contains reference values for yields on other bonds on the capital market. Difference in yield represents all differences between two countries or regions which influence bonds' offer and demand. These are e.g. political environment (political risks), expected returns, economic risks, expected inflation and expected exchange rate change, liquidity, mode of adapting respective country's bonds to most important investors' portfolio and similar. Spread changes, i.e. their rise, reflect increased concern of financial markets for capacity and capability of respective countries to face their debt in future (Žigman and Cota 2011).

Government bonds with fixed yields are the main pillar of the modern securities market. The curve (Figure 1) representing government bond yields is referent and serves as a guideline to future interest rate and inflation movements.

The yield span within the euro zone has had positive convergence since the Euro was introduced in 1999. Although there was a lesser spread widening at the beginning of 2000 due to dot-com bubble and terrorist attacks in September 2001. There was a pronounced convergence of yield on 10-year government bonds of the EMU member countries until 2007. After 2005 a moderate turn was noticed in Greece, Italy and Portugal in relation to the reference value. From the year 2007, the interest rate spread between German bonds and the remaining eurozone has been recording significant increase. This is also confirmed in the research made by Copeland and Jones (2001) who showed that differential appeared and expanded during crisis periods, as this was the case during the Russian crisis (1998), or currency crisis in Turkey (2001).

Graph 1: Yield spread on long-term bonds of the EMU member countries (according to the reference value of the German government bonds)



Source: Eurostat 2009

If the interest rates on government debt exceed the increase rate of the economy, the debt is set dynamically, which leads to ever increasing government debt and sustainability problem of the national economy. This causes negative cost and crisis spill-over, which has negative influence on the functioning of the monetary union.

4. INTERNATIONAL MONETARY SYSTEM IN THE PERIOD OF CRISIS

After ten years of relative stability and strenghtening of the euro as a common currency, the issue of the future of the euro and destabilisation of the European economic and monetary integration was raised particularly due to financial and debt crisis. The fact is that after the crisis the criteria have become indirectly tighter, accompanied by various new challenges and conditions and they have influenced further enlargement of the European monetary and economic integration as well as the entire international monetary system.

Economic and political differences between the member countries of the monetary union constitute favorable grounds for the development of assymetric shocks. Shocks influencing different economies similarly are known as symmetric shocks, whereas those having various implications, or reflecting implications only to one country in a specific way are known as assymetric shocks. Negative implications of symmetric shocks are mitigated by methods of common economic policy, whereas the assymetric ones pose a problem for common currency area, as there are no measures of the local or regional monetary policy.

Financial sector and banks are the backbone of the functioning of the modern countries' economic systems, also of those within the Eurozone. The key issue of the recent crisis was in securing stability and solving accumulated problems of the mentioned sector. The crisis which broke out in 2008 with the breakdown of some of the biggest financial institutions led to necessity of the government financial aid to a great number of banks. This government aid was financed by indebtedness on financial markets, which resulted in drastic increase in budget deficit and public debt with the most developed core eurozone countries, and even more drastic one with other eurozone countries. The eurozone countries as Greece, Italy, Spain, Portugal, Ireland and other could take loans with favourable interest rates on the world financial markets even without fiscal discipline expected from them as the EMU member countries. This was enabled by the euro, as investors were ready to lend money even to countries with the bigger risk taking into account credibility and stability of this world currency. The abovementioned countries were referred to indebtedness even before the breakout of the crisis due to insufficient domestic accumulation (savings) for investments and need for faster economic development and competitiveness. Interest rates started to increase, and some of the aforementioned countries whose investments still had no results already recorded deficits in their balance of payments.

In the crisis spreading model according to which one country's banks are buying other country's bonds, the crisis can spread across borders also by banks. For example, if the banks in the fiscally insolvent countries have borrowed large amounts of money from banks from other countries, these banks will also encounter difficulties due to interbanking relations. But regardless of the problem

spreading mode, difficulties always arise because countries, i.e. governments, which due to fiscal capacity are in normal times considered to be first-class debtors and ultimately " savers" do not have financial capacity to guarantee for their stabilisation function.

Table 4. Identified problems within the EMU

Economic Issues	Central Issues of EMU
Financial stability	Lack of credit Interbank lending Widely divergent borrowing costs in terms of public debt issuance Risk of non-performance of states obligations
Fiscal discipline	High public debt High public deficits Tax divergences Divergence of social contributions and benefits
Economic growth	Recession Low growth Unemployment Social inequalities Slow transition to green economic growth Slow transition to smart growth
Macroeconomic imbalances	Increased divergences in economic growth, unemployment and investment rates High current account deficit and external indebtedness

Source: adapted by the author

Mitigation of the crisis effects and increased control mechanism are pointed out to be the primary objective of measures and models of political instruments in order to avoid such big crisis in future or to at least alleviate their consequences. Seriousness and duration of the crisis forced the EU countries and their governments to adopt numerous measures and programmes for countering negative effects of the crisis, supporting thus the key sectors of economy. The response of the countries' governments in the period of crisis and after crisis has important implications for the maintenance and functioning of the international monetary system.

The first consequences of the world financial crisis were illiquidity and losses due to devaluation of the property under the mortgage-backed securities and their financial derivatives. Recovery of the financial market liquidity was therefore the first measure to be undertaken. Decisions of the central banks on securing liquidity as well as the measure undertaken by the majority of the countries' governments and parliaments to give guarantees to the financial sector proved to be efficient in preventing the breakdown of the global financial system.

Uncertainty regarding fiscal insolvency of the member countries initiated the second crisis wave in Europe. There was rising fear from countries' insolvency crisis accompanying the banking crisis. Competition losses and vulnerable banking sector endangered the countries' solvency and questioned the sustainability of the public finances. Continuous deficit increase and huge public debt reached their peak during 2011. The eurozone debt crisis led to new financial disturbances on the market, loss of trust among market participants and finally to recession in Europe. Due to fiscal restrictions in implementation of the common crisis management, the EMU did not have redistribution mechanism and instruments to help its member countries, and thus other solutions were produced. Unrealised similarities among member countries' economies make the common monetary policy inadequate and less efficient for stronger as well as for weaker economies challenging thus the sustainability of the monetary union foundation.

On the basis of the aforementioned it is obvious that the member countries have attained different level of convergence and economic growth, and that it is justified to raise the issue of their implication to the economic situation within the monetary union. Doubts regarding sustainability of the economic and monetary union are not new, but they are gaining on intensity and importance only under crisis circumstances and market instabilities when asymmetric shocks are pronounced.

4.1. Role of the Internation Monetary Fund during financial crisis

The breakout of the recent financial crisis rose numerous issues regarding the role and participation of the Internataional Monetary Fund in the world financial flows, emphasising thus the necessity of powerful and timely response of this institution.

In order to meet the ever increasing financial needs of the crisis-stricken countries and to strenghten the global economic and financial stability, The International Monetary Fund has significantly increased its lending capacities during the financial crisis. Through advancement of the lending system and its increased volume, it offered to countries solutions for creation of economic policies as response to the crisis, and introduced reforms which helped countries to cope easier with the problems during the crisis. One of the solutions was an increased quote of the member countries and bigger loans as a key step in efforts to overcome the economic crisis. During 2009 and 2010, the member countries provided the Fund with additional 170 billion of Special Drawing Rights (SDRs) through billateral arrangements, which were then included in enlarged New arrangements to borrow.

In order to support the countries during the crisis the IMF has modified its lending frame with the aim to adapt to the countries' needs. The emphasis of this modification was the importance of crisis prevention and rationalisation of the conditions for programmes approach.

Table 5. IMF loans during the crisis

2009	2010	
Extended Credit Facility was introduced in countries with the lowest income as means of long-term financial aid for long-term difficulties in the structural balance of payments, and with the aim to reduce the poverty	Subsidy resources for the poorest countries designed through Poverty Reduction and Growth Trust and promotion of the economic growth (<i>PRGT</i>), have been part of the larger reform and financial support of the Fund since January 2010. - The new programme was introduced in June 2010 as debt relief for the poorest countries hit by natural disasters.	- Stand-by credit facility intended for short-term needs of the balance of payments and for precaution needs - Rapid Credit Facility (<i>RCF</i>) foreseen for urgent balance of payments needs due to external shocks, natural disasters, in events when programmes are either unnecessary or unfeasible.

Source: IMF 2010⁴, adapted by the author

In response to the crisis the IMF has implemented policy reforms and has provided for the risk analysis and counselling in the filed of policies in order to help the member countries to overcome the challanges and spill-overs of the global financial crisis. It has also implemented numerous initiatives for strengthening and adjustment of the surveillance over the more globalized and internationally connected world. In order to strenghten its legitimacy, during April 2008 and November 2010 the IMF complied with broad administration reforms as response to the increasing importance of the emergening countries. These reforms enabled even smaller emerging countries to maintain their influence in the IMF (IMF 2016).

5. CONCLUSION

The modern world economy is characterised by decreasing number of national currencies, which is a logical consequence of increasing international economic and monetary integrations. Respecting the fact that domestic currency is a constituent part of the country's sovereignty capable of actively influencing the real economy, a stable and convrtible national currency is regarded as a reliable measure of economic value and sucess of the economic system, particularly in monetary policy.

The increasing power of the USA economy in the after-war period as well as the status of the US dollar as the world reserve currency in the Bretton-Woods system imposed it as a leading currency. Taking into account the fact that the USA represented the biggest world economic power, the majority of international exchange rate transactions was conducted in US dollars. However, the adoption of the euro as the EMU currency has led to its affirmation in trade affairs in Europe and also in the world. As a stable currency of a huge currency area, the euro has quickly earned favour with business entities of the new eurozone members.

In this research paper we have pointed out to economic, social and political heterogeneity of the union member countries which may pose an obstacle in the establishment of the optimal area of a common currency as the highest level of monetary integration. But however, common interests and new world order are creating an idea of the establishment of a monetary union deriving from the fact that monetary integration has significant economic advantages from introduction of a common currency. Decrease in transaction costs, higher price transparency and monetary stability have more benefits in relation to costs of the replacement and introduction of a new currency. But history has shown that monetary unions, beside economic ones, were most often a result of political unions and compromise and the same can be said for the European Monetary Union as well. The monetary integration in Europe was established with the aim to bring about economic prosperity and political stability throughout Europe.

In this research we have analysed the initial stages of the development of a modern international monetary system and its most significant stages and changes. We have pointed out to the fact that monetary systems, although based on monetary policy in their nature, are actually a reflection of broader social, economic and international relations. The increasing role of a respective country is measured by the increase in participation of its currency in international transactions, capital flows and international foreign exchange reserves. As this research has shown, turbulences and volatility of the leading world currencies may cause larger market disturbances, influencing either directly or indirectly real economic movements and fiscal parameters of the countries. Therefore it is necessary to secure conditions for a stable international monetary system and an efficient international monetary medium.

Respecting the significance and prescribed criteria for accession to the monetary union we can notice that the countries demonstrated initial differences in real parameters, which creates an unstable basis for further development and success of the functioning of monetary union. Therefore, in the recent literature this has been defined as one of the key reasons for debt crisis. In view of this, in this research paper we have pointed out also to negative effects of the recent global crisis on further process of the monetary integration and stability of the monetary system.

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