



## Euro Symposium

# Mundell Changed His Mind

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### ABSTRACT

My own view has always been that stable exchange rates among the highly integrated European economies were devoutly to be wished. The only question was whether a common monetary standard or a common currency was the best way to achieve it. But after the Maastricht Treaty imposed credible fiscal constraints on the participating countries, I became convinced that a common currency was feasible and the best way to go.

One of the paradoxical aspects about the debate was that outstanding euro skeptics, such as Martin Feldstein and Barry Eichengreen, were essentially using the model in Robert Mundell (1961). They worried about asymmetric shocks: European countries suffered the business cycle out of phase and so needed exchange rate flexibility. However, Mundell himself became the leading enthusiast for the euro!

In McKinnon (2004) I showed that Mundell essentially changed his mind about 1970 in two articles published in 1973 in an obscure conference volume that virtually nobody read (Mundell 1973a, b). Henceforth, Mundell emphasized the importance of absolutely fixed exchange rates, which only a common currency could give, in order to secure full capital market integration and risk sharing.

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## About the Author



**Ronald I. McKinnon** is William D. Eberle Professor of International Economics at Stanford University. He is best known for an important article on the theory of optimum currency areas (1963); *Money and Capital in Economic Development* (1973), which highlighted how policies of “financial repression” retarded economic growth; *The Order of Economic Liberalization* (2nd edition 1993), which outlined how to traverse the perilous path from central planning to the market economy; and his work on regional and worldwide monetary arrangements.

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