Date ___/___/______

Date :- 26/5/2020

Content Writer :-
Dr. Abhay Kumar Pathak
Deptt. of Economics,
Marwari College,
Darbhanga (LNMU)

Degree Part-I (Hons.)
Paper :- IV
Content of Paper :- International Economics
Module :- 6

TOPIC :- EURO-DOLLAR MARKET AND ITS EFFECTS ON INTERNATIONAL MARKET

By Euro-dollar is meant all U.S. dollar deposits in banks outside the United States, including the foreign branches of U.S. banks. A Euro-dollar is, however, not a special type of dollar. It bears the same exchange rate as an ordinary U.S. dollar has in terms of other currencies.

Euro-dollar transactions are conducted by banks not residents in the United States. Euro-dollars have come into existence on account of the Regulation issued by the Board of Governors of the U.S. Federal Reserve System, which does not permit the banks to pay interest to the depositors above a certain limit. As such, banks outside the United States tend to expand their dollar business by offering higher deposit rates and charging lower lending rates, as compared to the banks inside the U.S. Increase or decrease in the potential for Euro-dollar holdings, however, depends directly upon U.S. deficits and surplus, respectively.

Euro-dollar market is the creation of the international bankers. It is simply a short-term money market facilitating banks' borrowings and lendings of U.S. dollars. The Euro-dollar market is principally located in Europe and basically deals in U.S. dollars. But, in a wider sense, Euro-dollar market is confined to the external lending and borrowing of the world's most important convertible currencies like dollar, pound sterling, Swiss franc, French franc, Deutsche mark and the Netherland guilder. In short, the term Euro-dollar is used as a common term to include the external markets in all the major convertible currencies.

The characteristics of Euro-dollar market are as follows:-

(I) It has emerged as a truly international short-term money market.

(II) It is unofficial but profound.

(III) It is free.

(IV) It is competitive.

V) It is more flexible capital market.

Original customers of the Euro-dollar market were the business firms in Europe and the Far East which found Euro-dollars a cheaper way of financing their imports from the United States, since the lending rates of dollars in the Euro-dollar market were relatively less.

Effects of Euro-Dollar Market on International Financial System :—

Euro-dollar market has affected the international financial system in following ways:—

(I) The position of dollar has been strengthened temporarily since its operations of borrowing of dollars has become more profitable rather than its holdings.

(II) It facilitates the financing of balance of payments surpluses and deficits. Especially, countries having deficit balance of payments tend to borrow funds from the Euro-dollar market thereby lightening the pressure on their foreign exchange reserves.

(III) It has promoted international monetary co-operation.

(IV) Over the last decade, the growth of Euro-dollar has helped in easing of the world liquidity problem.