|  |
| --- |
| **Lesson 1: A Traders Introduction to the Euro, Part I** |
|  |

In our last lesson we finished up our discussion of the US Dollar, with a look at some of the economic indicators which move the currency, and where traders go for commentary on those numbers. In today's lesson we are going to begin our discussion on the next most traded currency in the world, the Euro.

The Euro is now the official currency of 15 of the 27 member states in the European Union (EU), which makes it the currency used by over 320 Million people. Like Europe itself, the Euro has an interesting history, which we as traders must understand to have a full understanding of the fundamentals of the currency. There are two major factors which lead to the eventual formation of the European Union, and therefore the Euro, which are important for traders to understand.

1. The major powers in Europe had been battling each other for hundreds of years prior to World War II. Nothing like the decimation that the World Wars brought to Europe had ever been seen before however, so after World War II, there was a realization that a drastic reordering of the political landscape was needed, in order to put nationalistic rivalries to bed once and for all.

2. Also as a result of World War II, the world's power structure had shifted, and the major European countries who were once the superpowers of the world, were replaced by two new superpowers. The United States and The Soviet Union were now the unrivaled superpowers of the world, and as a result there was a keen awareness among the former world powers of Europe, that banding together was the only way for Europe to have comparable clout on the world stage.

It was primarily as a result of these two factors that the European Coal and Steel Community (which eventually became the European Economic Community, the predecessor to the European Union) was founded in the 1950's with the general goals of:

1. Lowering trade barriers and facilitating economic cooperation for the benefit of the member nations.

2. Increasing Europe's clout on the world stage

3. Integrating the economies of the major countries in Europe to the point where they were too reliant on one another to go to war again.

During the next several decades many things happened from a diplomatic and trade standpoint that are very interesting, and which can be read about by doing a search on google for the history of the European Union. The next important event for us as traders however, came with the ratification of something which is known as the Maastricht Treaty in the 1990's. Up to this point, the idea of a tie up between nations in Europe was primarily focused on removing trade barriers and promoting economic cooperation. With the Maastricht treaty, member countries moved from a simple economic cooperation, to the much grander ambition of political integration between member nations.

This is important to us as traders as it was here that plans for a single currency to be used among member nations was introduced, and therefore here that the basic fundamentals of the Euro were laid out. There were three steps outlined in the Maastricht treaty that had to be completed before the currency could be released which were:

1. Free circulation of capital among member countries.

2. The second, and most important step for us as traders to understand, was the coordination of economic policies. Once the Euro was introduced, each of the member countries would be bound by the monetary policy as set by the European Central Bank. With this in mind, you could not have countries with extremely different levels of inflation and interest rates, replace their currency with the Euro, without undermining the credibility and fundamentals of the currency. To make the currency credible, and to make its introduction as smooth as possible, member countries were required to keep inflation, interest rates, and debt below certain levels. Lastly, they were also required to maintain an exchange rate that was basically a banded peg, allowing their currency to fluctuate only within a narrow band.

3. In 1999 the European Central Bank was established and the eleven countries listed here began to use the Euro in electronic format only.

Spain, Portugal, Italy, Belgium, the Netherlands, Luxembourg, France, Germany, Austria, Ireland and Finland.

These countries formed what is known as the European Monetary Union, which is comprised of countries who are members of the European Union, and use the Euro as their currency.

Greece, the United Kingdom, Sweden, and Denmark (the other members of the European Union at the time) remained outside the European monetary Union for different reasons.

While this may seem a bit like a history lesson rather than a lesson in trading, it is very important for traders of the Euro to have an understanding of the history we have just gone over. As we will learn in coming lessons, it is because of this history that the Euro is where it is today, and many of the concepts we have just outlined still affect the value of the currency in today's market.

That's our lesson for today, in our next lesson we will continue our discussion of the Euro, with a look at what happened when the Euro was officially introduced, and how the European Union and European Monetary Union have expanded since the introduction of the currency.

|  |
| --- |
| **Lesson 2: A Traders Introduction to the Euro, Part II** |
|  |

In our last lesson we began our discussion on the Euro, with a look at the history leading up to the formation of the European Union and the criteria that had to be met before the Euro's launch. In today's lesson we are going to continue our discussion on the Euro, with a look at the introduction of the currency, as well as some of the factors which affect its long term fundamentals.

As we discussed in our last lesson, the Euro was launched as an electronic currency on January 1st 1999. As you can see from this chart, the markets initial confidence in the Euro, and really the European Union as a whole, was initially not very high. Over the next year the currency sold off from just above 1.1600 dollars to 1 Euro at its inception, to a low point of around .8200 cents to 1 Euro towards the end of 2000. While the tables have turned now in the Euro's favor, it actually took the European Central Bank intervening in the markets and buying Euros, to keep the currency from sliding further in 2000.



The launch of the Euro was the largest monetary changeover ever, and as you can see, was not guaranteed success. As we touched on in our last lesson, getting a dozen countries, which varied widely in their economic and political clout, to give up control over their own monetary policy and switch to a more centralized monetary system, was no easy task.

As we learned about in module 8 of our basics of trading course, one of the most powerful tools that countries have to try and manage their business cycle is monetary policy, a tool which those adopting the Euro were essentially giving up. Although we have not seen a real test of this yet, you can imagine a situation where the economy of one of the major countries in the EMU such as Germany, goes into recession, but overall growth in the rest of the EMU is steady. If Germany were not part of the EMU, they could cut interest rates to try and bring their economy out of recession. Since they are however, their hands would be tied in this situation from a monetary policy standpoint, which may drive their economy deeper into recession than would otherwise be the case.

As we also learned about in module 8 of our free basics of trading course, countries have a second tool to manage the business cycle, which is Fiscal policy. As the EMU nations are still primarily independent from a fiscal policy standpoint, they do still have this in their toolbox. The issue here however, is that one of the ongoing requirements established in the Massstricht treaty for countries which join the EMU, is that member country's budget deficits must be less than 3% of GDP. So here again member nations are someone limited in what they can do to help their own economies, should it falter.

Of all the things to understand about the Euro from a fundamentals standpoint, it is this that is the most important, as it is here that a true test of the Euro, will eventually come.

So far I think most would agree that the Euro has been a resounding success, and since the original 12 countries replaced their currencies with the Euro as their paper currency in January of 2002, 3 more EU member nations have joined the EMU, and 5 other countries outside the EU have adopted the Euro as their official currency.

As a result of its success and the large combined economies that the currency represent, many feel that the Euro will one day replace the US Dollar as the premiere currency of the world. If you have thoughts on this I would love for you to share them in the comments section below.

Thats our lesson for today. In our next lesson we will look at the major economies of Europe which traders watch closely for fundamental direction in the currency so we hope to see you in that lesson.

|  |
| --- |
| **Lesson 3: How to Trade Euro Fundamentals** |
|  |

In our last lesson we continued our discussion of the Euro with a look at its introduction, and the major factors which will determine the long term fundamental direction of the currency. In today's lesson we are going to continue our free forex trading course, with a look at the major economies in the Eurozone and how each affects the value of the Euro.

As you can see from this graph, member countries Germany, France, Italy, and Spain make up over 75% of the Eurozone's GDP. As a result of this economic data out of these countries has the tendency to move the Euro the most, so traders naturally pay them more attention.



There are literally thousands of economic numbers released in the Eurozone however, like we covered in module 3 of this course, those that affect the current account (trade flows) or interest rates (capital flows) are going to have the greatest potential to move the currency. All of the indicators which we cover in module 8 of our basics of trading course, have a counterpart in the EU. Most of the time they are also named the same, and as they show the same things, traders can expect the market to react accordingly. The only thing to keep in mind here is that the economic climate in the United States vs. the Eurozone will differ at times, so traders and therefore the market may react differently to the same number out of the EU than they do out of the US.

The second thing that it is important to understand about EU economic releases, is the different mandate of the European Central Bank, versus the Federal Reserve. Where the Federal Reserve has a dual mandate of maximizing employment and maintaining price stability, the ECB's mandate is solely to maintain price stability. With this in mind, the ECB is normally seen as more hawkish than the federal reserve, meaning they are more likely to hold steady or raise interest rates when economic data show price increases, and less likely to cut interest rates as quickly as the fed when growth in the Eurozone slows.

I could spend many lessons covering each of the economic indicators and their relative importance to the market but in the interest of maximizing our learning I am going to instead defer to two free sites which do an excellent job here.

Fxwords.com and specifically their page on Euro-Zone Economic Indicators which I have included a link to below this video. As you can see here they categorize the major economic reports and then list them out with stars representing the relative importance of the indicator to the market. If you click on the link for each indicator it will take you to a page giving a definition as well as commentary on how traders should expect the release to affect the market.

Once you have an understanding of the economic indicators then you can get the date, time, and forecast for the release from the global calendar which you can find by click the calendar button at the top of Dailyfx.com. As you can see here the importance of the indicator to the market is also indicated with stars on the calendar, and the important indicators have links where you can go for more information.

Thats our lesson for today and that wraps up our series on the Euro. In our next lesson we will look at the next most actively traded currency in the world, the Japanese Yen so we hope to see you in that lesson.