Market aimed at stimulating inter-European trade. A solution which, finally, would also cover the aspect of social solidarity.

Allow me to insist, somewhat, on this last point which is perhaps not so obvious. Communal solidarity within the EC has two sides to it. Support for the lesser developed member-countries through the structural funds, and the support of the non-privileged strata of society -- workers' insurance, working conditions and programmes for reducing unemployment. We can observe similar phenomena in the broader economic area of the western world.

Only here the roles are shared somehwat differently. The area which is tending to become marginal is Europe in its entirety. I would like to give you two examples. One refers to West Germany which is rightly considered to be the heart of the European economy. With the devaluation of the dollar, Germany is exporting less in volume than it did in 1985 while its imports have increased by 6%. The pressure on its national income will oblige it to grow at a rate of less than 2% in 1988. The second example is more typical, because it refers to the entire Community.

Last year, the EC countries had a total external deficit in high technology goods which is estimated at 10 billion dollars, while the United States had a surplus of 1.3 billion dollars and Japan a surplus of 8.6 billion dollars.

This aspect of the European problem was beautifully summarised by Alain Madelin, France's Minister for Industry. "Europe," he said, "has no other choice but to try and become a third pole of equal weight with the other two. Otherwise, poor as it is in raw materials, politically divided and technologically dependent, it is destined soon to end up as a sub-contractor of the other two industrial powers."

The integration of Europe, for which 1992 has been set as a deadline, aims precisely at creating the conditions in which economies of scale and the encouragement of new products will provoke an increase in productivity to the extent that Europe can definitely establish itself as a third industrial power, equal to the other two.

It is, I think, obvious that the road to 1992 will become very difficult or even impossible if the entire western world was plunged into a severe economic depression. From this point of view, Europe, by promoting a commercial cooperation which would help the United States to restore its foreign trade without a depression, would in effect be helping itself.

It would be creating favourable conditions for that member of the western triad which is in danger of becoming marginalised by competition -- for Western Europe itself. This is the first element of social advantage to be derived from a policy of economic cooperation on a world scale.

The second refers to the workers, or rather to the unemployed of Europe. At this moment, in the entire European area, the number of unemployed is 16.7 million. The average unemployment percentage in member-countries is about 11.5%. Greece, in this respect, has managed to be in a better position, with an unemployment rate of 7.5%. But any longlasting unemployment, with the exception perhaps of a small percentage of transitory unemployment, is not permissible in modern conditions. In this respect, European integration in 1992 will not be of much help.

Recent calculations have estimated the number of new jobs that will result from the unification of the European market at 1.7 million. This is a negligible number compared to the 17 million unemployed who will have to be absorbed.

It would be, therefore, a mistake for us to consider that the achievement of a unified market in 1992 will absolve Europe of the need for broader international cooperation. It would be a mistake to consider unification as the stepping stone for future European domination. It would be an almost equally dangerous mistake to for the United States to base themselves on the devaluation of the dollar in order to prevail over their other two partners.

The proper way is to look at 1992 as the basis for a policy of equal cooperation with the other two strong economic poles in the modern western world.

Moreover, we should not overlook the fact that 1992 is perhaps not so near as it looks on the calendar. In order for unification to be achieved, 300 of the Commission's proposals need to be accepted. So far, only 69 of these have been passed. If one adds the establishment of a Central European Bank and the currency unification of Europe, measures which Greece supports within the measure of its powers, we see that a long road still has to be travelled before a strong enough Europe can be created which can cooperate on equal terms with America and Japan.

A long road and a good deal of work lie ahead for all and, naturally, for the Greek presidency which begins on July 1.

AN OVERVIEW OF THE GREEK ECONOMY

Theodoros B Karatzas
Deputy Minister for National Economy

Mister President,

I thank you for the opportunity you give me today to address such a distinguished audience and to present the Greek economy as a whole as it is today, but also its prospects, both immediate and long-term.

Ladies and Gentlemen,

Before starting, I would like to welcome you and to thank Euromoney but also the five banks which adopted its initiative for the organization of this Congress in the City of Athens. I hope that your two-day work, with the presence of so many distinguished speakers, will allow you to shape a clear picture of what has been taking place in our country in a period when the European economy has entered a new decisive stage for its internal integration.

I would also like to convey to you the greetings of the Minister of National Economy Mr. P.Roumeliotis, who regrets for not being able to be here with us today. Official engagements obliged him to accompany the President of the Republic in an official visit abroad.

Ladies and Gentlemen,

In presenting the Greek economy and the economic policy, the speaker of the Ministry of National Economy should explain -and not necessarily justify - the economic situation and the economic policy applied, as well as to make, in rough lines, a summary of the economic prospects for tomorrow and for the distant future. This is what I shall attempt to do. I hope, however, that you would agree with me that an economic policy should be explained - and assessed - not only on the basis of the needs of "today"; it should <u>also</u> proceed on the basis of the experience and the necessities of "yesterday" and have as a criterion the prospects and the limitations of "tomorrow" <u>as well</u>.

I. Having made these introductory remarks, I would propose to you to consider the economic policy applied for four months now as marking the beginning of the <u>third phase</u> of the more general economic policy of the Government which ensued from the elections of 1981. The two previous phases of this economic policy were the period from October 1981 to October 1985 and the period from November 1985 to December 1987. Before explaining the policy of the present phase, it would be useful to remind you of some characteristics of the two previous periods as well as of some characteristic magnitudes of the period before 1981.

First, I would like to draw your attention to the two last years before 1981: The Greek economy, not having adapted on time to the necessities resulting from the two oil crises of the '70s, appears in the years 1979 and 1980 with some very strong structural characteristics:

i). With a doubled current account deficit as a percentage of GNP : from about 3,5% of GNP in 1978 to about 6% of GNP in 1979 and 1980.

ii) At the same time, inflows of non-borrowed capital as a percentage of the current account deficit decrease <u>dramatically</u> during these crucial two years: from about 100% in the period from 1975 to 1978, to about 56% in 1979 and 1980.

iii) The combined effect of these two factors produces a dangerous rise in the net liabilities of the country towards foreign countries, which from 0,3% of GNP in the period 1975 - 1978, multiply by seven times in 1979 and 1980 and thus become 2,1% of GNP.

iv) The year 1981 is the year when the above magnitudes of the economy become permanent and deteriorate further, <u>since within one single year</u> the net borrowing requirements of the public sector double: from 8,1% of GNP in 1980 they rise to 14,3% of

GNP in 1981. In that same year, 1981, the current account deficit deteriorates even more and becomes 6,5% of GNP. In addition, inflows of non-borrowed capital, as a percentage of the current account deficit (which was 100% in the period 1975-78 and became 56% in 1979 and 1980) decrease even further, down to 45% of the deficit during this year. Finally, net overdue liabilities of the country towards foreign countries (which were 0,3% if GNP in 1975-78 and multiplied by seven times to 2,1% of GNP in 1979 and 1980), increase still further in 1981, becoming 3,1% of GNP.

Although I would not characterize the figures of 1981 as particularly worrying, it is yet important to note that:

In the first place, they reached these levels tremendously fast, within only two to three years. And precisely this is worrying because it indicates a tendency of the economy.

In the second place, the external deficit as an absolute percentage of GNP (6,5%) does not appear perhaps to be particularly worrying, yet the percentage of this deficit is affected by the fact that investments are barely growing, what is identified as a permanent structural phenomenon of the economy. And this last fact is worrying.

II. Many have criticized - in good faith I have to admit - the government policy of our first period (1982 to October 1985), and the critic can be summarized as follows:

"Since the downward process of the economy in the three-year period 1979-1981 was already known, why did you follow an expansionary income, fiscal and monetary policy which would preserve or even worsen the public and external deficits?"

I shall argue that this critic - no matter how sincere it is - suffers because it is incomplete. It ignores the real financial and social situation of the country during these times and it confronts our economic policy of the period 1982 - 1985 under the simplictic - and therefore wrong - keynesian prism of "overheating". And this because it ignores that especially during the previous three years the income situation of the working people had reached levels which were no more tolerable. It ignores that the introduction and setting into action of new social and economic institutions (which was a request of the Greek society as a whole), the change in the educational and social policies (health, welfare, etc.) aimed at the establishment of a minimum level of social and economic protection, all these things new for Greece but already very old and well-established for the whole West-European territory have two characteristics:

firstly, they create the permanent and safe precondition for a minimum social consensus, which will allow the realization of the modernization breakthroughs our economy and our society are in need of and,

secondly, all these things involve cost: cost in public expenditure, cost in foreign exchange, cost in monetary circulation and, naturally, cost as regards inflation.

In other words, it is the Government elected in 1981 which had to assume the task of curing and modernizing the productive, economic and social structures of an economy and of a society which had not got modernized when it ought to have, i.e. already twenty or at least ten years before that.

Yet it is a fact that the policy of the period 1982 to October 1985 has an influence on business profits and on business perspectives. The investment inertia established in the years 1979-1981 continues during this period as well. In fact, perhaps it is getting even worse due to the more general reservedness of the private sector which shows to be sometimes worried, unjustifiedly I believe, by the income and and social policy of this period. However, I shall not deny that our actions had, at times, their share as well for the anxiety or the reservedness of businessmen during this first phase.

III. The period from October 1985 to December 1987 marks the second phase of our economic policy. It is the period of the Two-Year Stabilization Program, which I would also call "a period of the realization of the truth" as regards the Greek economy. Of a "truth" which, as I mentioned above, should have been "discovered" or rather revealed twenty or ten years before. Some define one-sidedly - and therefore wrongly - the Stabilization Program of the period from October 1985 to December 1987 as "Austerity Program". These sides ignore, and I believe on purpose, that during this two-year period, a tremendous effort was being made for the restoration of internal and external balances regarding, as a matter of fact, the whole post-war process of the economy.

The achievements of this two-year effort - which I must say were realized in some cases with hard measures - are numerous and important:

In the first place, a remarkable decrease of the current account deficit with an almost absolute attainment of the aims of its decrease set for the two years. More concretely, as a percentage of GNP, the deficit decreased from 9,8% in 1985 to 4% in 1986 and to about 2,5% in 1987. In absolute and current prices, the current acocunt deficit fell from 3,3 bn. dlrs. in 1985 and from 1,8 bn.dlrs. in 1986 to 1,3 bn. dlrs. in 1987. And, of course, it is of particular importance that the net external borrowing for 1987 was almost zero, while in 1985 it was running at a rate of 31% and in 1986 at a rate of 21%. At the same time, in the two-year period between 1985 and 1987 the supplies in foreign exchange of the Bank of Greece almost tripled.

In the second place, both inflationary expectations and inflation as absolute figures have already entered the track of constant de-escalation. In the last two-year period we have had a decrease in the rate of inflation by 9 percentage points while in other European countries a decrease of 7 -8 percentage points was achieved through stabilization programs of a five-year duration. In fact, I should underline that in the first quarter of 1988, after a negative inflation rate of January and February (a phenomenon which had not been observed in our country for a decade) the inflation rate was 2,4%. I should also remind you that in 1987 the inflation rate was 15,7% as against 16,9% in 1986, 25% in 1985 and about 26% in 1981. At the same time - and this is particularly important -the decrease of inflation in our country has taken and is taking place without an increase in unemployment, a thing usually observed in such cases. On the contrary, there was a slight decrease in unemployment in 1987. At present, our country has one of the lowest percentages of unemployment in Europe, amounting to about 7%.

In the third place an improvement of the competitiveness of the Greek economy has been achieved, according to the most recent estimations of the OECD.

In the fourth place, there has been an improvement of private investments in fixed capital in real terms, since in 1987, after many years, we had an important increase of 6,7%, while a more vigorous recovery is expected for 1988.

In the fifth place during the last two years there has also been a spectacular rise in the inflow of foreign capital for investments. More specifically, between 1985 and 1987 approvals for import in our country of foreign capital according to the provisions of L.D. 2687/1953 and of P.D. 207/1987 quadrupled (1985: 37 mn. dlrs - 1987: 150 mn. dlrs.).

In the sixth place as regards the public sector deficit: this deficit showed an important decrease, although not to the desired level: from 18% of GNP in 1985 it fell to about 13% in 1987.

Finally, as regards our net liabilities to foreign countries, I would like to remind you that in 1981 we found them at 3,1% of GNP. In the two-year period 1986-1987 we managed to lower this percentage by about six times, which has now become 0,5% of GNP.

IV. However, I would like to emphasize mainly the huge psychological and social essence of the Stabilization Program. As I already mentioned, during this two-year period the Greek society and the Greek productive base were obliged, for the first time in decades, to come face to face with the truth, i.e. with the necessities of economic reality. And one, I think the most essential of these necessities, is that one cannot consume, permanently and for a long time span, more than what one produces. Thus, after the painful process of stabilization, our economy was exposed to the truth. At the same time, the productive base of our economy became conscious of the fact that, apart from organization and rehabilitation there is the dire necessity of capital accumulation as a primary factor of economic growth, which together with the restoration of the domestic and international competitiveness of the products, secure tomorrow's economic prospects.

V. The beginning of 1988 marks the third phase of our economic policy. The two potentials I just mentioned - the restoration of macroeconomic imbalances and the consolidation of a favourable climate in combination with business profits of the two previous years - allow the Greek economy to enter a stage of self-propelled economic growth which will not jeopardize the important achievements of the Stabilizatipn Program. Thus, our economy has inaugurated its new, equally difficult phase, the phase of growth in parallel with the preservation of stability.

However, I would like to stress that the possibilities for a spectacular recovery during the first year of this effort for growth are not unlimited. Both the absolute level of inflation and inflationary expectations have marked a substantial de-escalation, yet the rate itself, although lowered, remains still high. The Government will continue the effort for its further de-escalation and, I should repeat here that the figures of January, February and March 1988 are sufficiently encouraging since, despite the easing of income policy and despite certain clearly better income expectations, the inflation rate was negative (about -0,7%), a phenomenon which had not been observed in the Greek economy for decades. During the whole first quarter this rate was 2,4% as against 4,7% in the respective quarter of 1987.. Yet, we are fully conscious of the dangers which exist and our concern for the preservation of stability remains unchanged.

Particular emphasis will be given by the Government at the front of public deficits where, I have to admit, the power of resistance of the mechanisms responsible for the creation and for their swelling, is particularly strong. As was mentioned by the Prime Minister, "the public deficits and their further limitation are the main goal of the economic policy of 1988", and I think, that certain important conclusions towards several directions can be drawn from this declaration.

VI. To make possible the targets set for 1988, the individual components of our economic policy will be as follows:

i) The income policy enters into a period of careful expansion, which is not expected to have a negative impact on the stability of the economy, since at the same time care is taken for the increases to be sustainable by the economy. An example of this policy is the recent National Collective Agreement.

ii) The fiscal policy is formulated in such a way as to allow a reduction of net borrowing requirements of the public sector by about one percentage point (from 13,3% of GNP in 1987 to 12,2% of GNP in 1988). At the same time, a fundamental reform of the tax system is being attempted with a view to its rationalization and simplification, a more fair distribution of tax burdens and, finally, a tax relaxation for the average tax payer. The policy applied in public expenditure is in line with the attainment of macroeconomic targets, it expresses the priority scale of the government policy and will be achieved through improvement of management methods in the Public Enterprises and Organizations and by imposing transparency in the network of their expenditures.

iii) The monetary policy will consist of: (1) strict adherence to the monetary program, (2) continued application of last year's flexible interest rates policy, (3) preservation of the satisfactorily positive interest rates on deposits, (4) implementation of the basic economic principle implying that any borrower should pay as a loan interest rate the real money cost, (5) moving still further away from the banking system as an only source of drawing capital and further consolidation of the role of the capital market, (6) further encouragement of the competition among commercial banks and, (7) strengthening of the role of the Central Bank rather as the basic executive body of the monetary policy than as a place of issuing acts of the Governor which intervene administratively in sectors practically beyond control.

iv) The foreign exchange policy will be aimed at the preservation of the competitiveness of the economy by means of a careful adjustment of the drachma parity as the conjuncture may require it.

VII. Ladies and Gentelemen,

It is a fact that the Government has already created a favourable climate - I would say a "green-house" - for the flourishment of private investment initiatives. It has elaborated the appropriate policy, which reinforces the favourable climate. This policy aims at the following:.

- First and mainly at the further securing and the reinforcement of the stable economic and political environment.
- At the granting of investment incentives (grants, tax allowances, etc.).
- At the further accumulation of capital which will be used for the realization of investments.
- At the modernization of the public sector and at the improvement of the quality of services it provides.
- At the modernization and the further expansion of works of infrastructure..
- Finally, at the modernization of the whole institutional framework in which investments are realized,.

Thus we believe that the appropriate environment for the further development of profitable productive investments exists. Therefore, what remains for the enterprises - domestic and foreign - is to respond in time with serious intentions and vision to this favourable environment, undertaking appropriate investment, financial, technological and other initiatives all of which are both necessary and welcome.

We are at the threshold of 1992. Thus, as in the other EEC countries, in Greece, too, the pace has been accelerated, which will raise the adaptability of the economy to the contemporary requirements. With the reinforcement of the internal cohesion of the European Community, it is our conviction that soon we shall reach the point when the level of the economies of member-states will converge. Our aim is, in parallel with this convergence, our country to continue its upward course in which it has entered, so as to reach soon the levels of growth of other developed countries.

I hope that this Congress, apart from making you acquainted with the recent positive developments of the Greek economy, will help you understand why and how much it would be to your advantage to develop or expand any form of your economic activities in Greece, thus contributing to this overall effort for stable and fast growth of the country.

THE GREEK FINANCIAL SYSTEM - THE ROAD TO DEREGULATION

Dimitrios Chalikias
Governor
Bank of Greece

Address by the Governor of the Bank of Greece, Mr. Dimitrios Chalikias, to the Euromoney Conference titled "Greece in the World Economic Community" held in Athens, April 20-21, 1988

THE GREEK FINANCIAL SYSTEM-THE ROAD TO DEREGULATION

The Greek financial system and the scope and instruments of monetary policy have undergone significant changes in recent years. For several decades, the central aim of monetary policy was to influence the allocation of economic resources. To this end, a highly complicated system of selective credit controls and regulations had been gradually established since the 1950s, combined with a wide range of administratively determined interest rates. This system remained virtually unchanged until the early 1980s. The interest rate structure was arbitrary, in the sense that it did not comform to banking criteria and had to be supplemented by a reserve/rebate system on bank credit, which aimed at equalising the rate of return on different categories of bank credit, and by the earmarking of part of commercial bank funds for the financing of specific economic activities.

In practice, this system proved to be ineffective. It did not, and could not, contribute to an efficient allocation of financial resources; even worse, it led to serious distortions in the operation of financial markets. Extensive controls and regulations had the effect of isolating the Greek financial system from developments in international financial markets. In addition, the maintenance of low, subsidised interest rates hindered the development of an efficient money and capital market.

The conduct of an effective monetary policy was also adversely affected. The Bank of Greece was not in a position to pursue an interest rate policy which could be readily adjusted to changing conditions at home and abroad. Monetary policy had to rely excessively on direct controls, despite their obvious drawbacks. Moreover, since interest rates were set at lower than equilibrium levels, competition between banks was limited.

Another important constraint on the conduct of an effective monetary policy was the financing of a large part of the PSBR either directly by the Bank of Greece or by commercial banks, which were required to invest a proportion of their funds in treasury bills. Both methods resulted in the monetisation of the public debt. In addition, the dependence of the specialised credit institutions (namely, the Agricultural Bank, the mortgage banks and the investment banks) on central-bank financing increased the monetary base and undermined the effectiveness of monetary policy.

Finally, the conduct of an effective monetary policy was hampered by the practice of the central bank to refinance certain categories of bank loans solely in order to maintain low interest rates on these loans.

Since 1982, the conduct of monetary policy has taken a new direction, and the groundwork has been laid for a fundamental reform of the financial system. Appropriate conditions had to be created before the Bank of Greece could proceed to the liberalisation of the financial system.

A number of difficulties were primarily related to misconceptions concerning the role of monetary policy. In addition, the adjustment of monetary policy was also impeded by objective difficulties. The wide range of administratively determined lending rates that prevailed at the beginning of the 1980s could not be eliminated at once without undermining the financial position of a large number of enterprises. This is particularly true in view of the fact that negative real interest rates had led to excessive borrowing and to a deterioration of the capital structure of many enterprises. Under these circumstances, interest rate adjustments had to be gradual. Actually, to the extent permitted by economic conditions, the Bank of Greece sought a convergence of lending rates at a higher level. At the same time, it proceeded to abolish, simplify and rationalise credit controls.

Furthermore, it was necessary to put an end to the heavy reliance of specialised credit institutions on central-bank funding of their lending activities. This dependence was largely the result of administratively determined low lending rates, which made it unprofitable for these institutions to attract private savings by offering competitive rates on their liabilities. Following systematic efforts, these institutions have recently attained full financial autonomy. In addition, the refinancing by the Bank of Greece of certain categories of bank credit, in order to support low lending rates, was abandoned.

Finally, although the public sector borrowing requirement remains large and exerts pressure on available financial resources, considerable progress has been made as regards the methods of financing the PSBR. Under legislation enacted in 1982, a ceiling was imposed on central-bank credit to the Government, thus eliminating a major cause of monetary instability. It should be pointed out that central bank financing of public sector deficits has been reduced to around 10 percent in recent years, against more than 50 percent in the period 1981-1982.

. . .

I have referred to the prerequisites for implementing a programme of monetary reforms and to the progress that has been made so far in meeting these prerequisites. Changes were introduced gradually for the reasons mentioned before. In 1987 significant steps were taken by the Bank of Greece towards the liberalisation of bank lending and deposit rates.

Until a year ago, all interest rates on bank deposits and bank loans were administratively determined. Today, as a result of the measures taken, only few interest rates are still administratively determined, specifically those on savings deposits, on loans to small manufacturing firms and on mortgages granted under certain social housing programmes. In particular, the interest rates on more than 80 per cent of total commercial bank credit to the private sector are market determined, while in the case of investment banks interest rates are market determined on all categories of lending. As regards credit provided by the Agricultural Bank, lending rates on some categories of loans have been liberalised but for the majority of loans, minimum interest rates are still in effect. Lastly, mortgage banks have been permitted to grant housing loans at negotiable interest rates.

As regards bank deposits, interest rates on all categories of time deposits with a maturity of seven days or longer are negotiable.

Parallel to the initial unification of interest rates at higher levels and their subsequent liberalisation, the Bank of Greece took significant measures aimed at abolishing or simplifying the existing system of credit controls and regulations. This has provided more flexibility to the banks in managing their portfolios. The Bank of Greece intends to dismantle gradually the entire reserve/rebate system, so that

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the structure of lending rates will be determined exclusively on the basis of banking criteria. It should be noted, however, that reductions in reserve/rebate rates have monetary repercussions, and that they will therefore have to be reduced gradually, in a manner that would not undermine the effectiveness of monetary policy. In addition, a series of measures have been taken which enable banks to offer new services and adopt new methods of financing, along with abolishing credit restrictions and simplifying regulations on bank credit. Such measures, in conjunction with interest rate liberalisation, have strengthened competition in the banking system, and have contributed to a more efficient allocation of economic resources.

It should also be noted that significant changes were introduced in central-bank financing of the Agricultural Bank and mortgage banks. These credit institutions are currently financing their lending activities by attracting private savings or by securing funds from sources other than the Bank of Greece. Moreover, the Bank of Greece will make credit available to the Agricultural Bank and mortgage banks on the same terms and conditions as those applicable to commercial banks, while in the second half of 1987, the Agricultural Bank was included -for the first time - in the system of reserve requirements.

Parallel to the above measures, the proportion of the

PSBR financed directly from the money and capital markets increased substantially in 1987, especially in the second half of the year, reaching 19 percent compared with 4 percent in 1986. It is estimated that around 40 percent of the PSBR in 1988 will be raised from the financial markets. These significant developments are made possible by the issue of Government securities on market terms. Specifically, in 1987 there were three issues of Government bonds, while treasury bills continued to be sold on a regular monthly basis. The increase in the interest rates on treasury bills has stimulated demand by the public, thereby reducing the monetisation of the PSBR by the banking system, with a restraining effect on the growth of bank liquidity. In addition, the high interest rates offered on government securities have kept bank lending and deposit rates at high levels, thus enhancing the effectiveness of monetary policy.

Interest rate liberalisation and the abolition of a large number of selective credit controls have paved the way for the required adaptation and modernisation of the credit system. It should be noted that since the second half of 1987, following the liberalisation of interest rates, competition between banks has strengthened, although banks' adjustment to the new deregulated environment and their responsiveness to changes in monetary policy remain rather slow.

The slow response of the banks should have been expected. It can be partly attributed to the oligopolistic structure, especially of the commercial banking system. But most importantly, banks operated for a long period under a highly complicated system of credit controls and regulations, where interest rates were administratively determined, new initiatives were suppressed and to a large extent profitability was assured. It is therefore not surprising that banks are currently going through a transitional period of slow adjustment and adaptation.

In addition, a serious obstacle to the development of competition between banks is the absence of well-developed money and capital markets. Banks have essentially monopolised the financial intermediation process and have therefore become complacent to some extent. Thus the development of financial markets should be given top priority, because it could have widespread favourable effects on the economy. Resort by the Government to the market has already started exerting pressure on credit institutions to introduce more efficient methods of attracting savings, upgrade the quality of their services, expand into new banking operations and improve profitability. It appears that foreign banks operating in Greece have shown greater adaptability to the new deregulated environment, thus making a positive contribution to the development of competition and the promotion of financial innovations.

It is the view of the Bank of Greece that competition is the most effective means of speeding up adjustment of the banking system to the new conditions and requirements. Interest rate liberalisation and deregulation of the banking system provide banks with considerable leeway for expanding into new areas of financial activities which will enhance their profitability. Indeed, there is evidence that banks are moving in this direction by introducing new, more effective methods of operation and organisation. In fact, those financial institutions that adapt faster to the new environment will in all likelihood increase their returns and market share.

The Bank of Greece has pursued, and will continue to pursue, policies which are neutral and do not discriminate between financial institutions. It has ceased to extend preferential treatment to any category of credit institutions; in fact, all specialised credit institutions are treated on an equal basis with the commercial banks as far as financing by the central bank is concerned.

A major obstacle to the development of more competitive conditions in the banking sector is the requirement imposed on credit institutions to earmark a large part of their deposits for the financing of public sector deficits. If progress towards the development of money and capital markets continues, the public sector will soon be able to finance its borrowing needs through the financial markets. This will make the compulsory investment of commercial banks' funds in treasury bills redundant. To this end, it is also important for the Government to continue its present efforts to reduce the PSBR.

Modernisation and rapid adjustment of the Greek banking system, along with the development of efficient primary and secondary money and capital markets, are also essential, prerequisites for the Greek financial system to be able to cope with the intensification of competition stemming from the creation of a single financial market in the EEC by the end of 1992. The Greek banks have already begun adapting to the new conditions, taking advantage of the new opportunities. They are aware that any delay in adjusting and modernising will render the banking system unable to cope with competition from foreign banks, not only those operating in Greece, but also those operating in other member-countries, as these banks will be able from abroad to extend loans or provide other financial services to the domestic market.

Benefits of a more permanent nature will accrue to the banks and the Greek economy if banks take full advantage of the transitional phase to reorganise operations, improve efficiency, and expand and upgrade the quality of financial services they offer, parallel to the promotion of the money and capital market. Progress in these areas would provide savers with alternative portfolio opportunities, which would stimulate saving, and increase autonomous private capital inflows. Because in the case of Greece most of these inflows originate from Greeks living or working abroad, they do not increase the external indebtedness of the country. Moreover, business firms would be able to diversify the sources and means of their financing, while the methods and terms of borrowing by the public sector would significantly enhance the conduct and effectiveness of monetary policy.

In closing, I would like to emphasise that the Greek banking system has entered a new phase of substantial adjustments which, although difficult, are necessary for the development of an efficient financial sector that would be capable of facing the challenge of 1992. The Bank of Greece will continue its effort to adapt its role to the new deregulated environment and encourage and support the modernisation of our credit system.

GROWTH POTENTIAL, CAPITAL MOVEMENTS AND THE GREEK FINANCIAL MARKETS

Andreas Ch Boumis
Chairman
Commercial Bank of Greece

Dear friends and colleagues

Being a banker by profession, I would like to focus my presentation on what I consider to be the major issues of the greek financial system. I will argue and I believe convincingly, that the greek financial markets are going through radical changes with increasing dynamism leading up to an explosive stage, in the positive sense of the term.

The necessary and sufficient conditions which are satisfied for such a positive response to change are:

-the development potential of the greek economy especially in its regions.

-the underbanked condition of the greek economy

-the talent accompanied by the appropriate technical and managerial expertise of greek manpower, employed either at home or abroad.

-the global importance and dimensions of the greek shipping activities

-the stature, resources and power of four million greek expatriates living and prospering abroad.

-the long tradition of greeks in trade and financial intermediation

-the location of the country dominating the Eastern Mediterranean: also its geographic and historical and cultural links to the Middle East and Eastern countries

-the new role required of the greek banks for the radical acceleration of growth of the greek economy

-the challenge of international financial competition especially in view of the imminent full integration of the financial markets of the EEC in 1992.

I will now proceed with the supporting rationale of my proposition. I will begin by examining the growth potential of the greek econmy as a whole and move on to focus on the financial markets.

Having at times achieved very high rates of quantitative growth, the postwar pattern of greek economic development has led to an accumulation of structural problems. The full impact of these problems has been perceived only during the last decade with the serious slowdown in economic growth. A detailed analysis of these problems goes well beyond the confines of my presentation. For my purposes, however, I would like to focus on a few aspects which are relevant to my argument in the sense of adding depth to what might otherwise be taken as a theoretical exercise in comparative statics.

At the heart of the economic problems currently besetting Greece has been the overcentralization of economic power and activity. Strong linkages were developed between political power, the banking system, the top stratum of companies which set the direction and tone of economic development. This pattern resulted in and was reinforced by a substandard, distorted growth of financial markets. In fact, the overwhelming majority of the financing requirements of the private and the public sector was satisfied through direct banking channels, rather than being partially at least catered to through transactions at arm's length in the capital markets.

Among other things, this led to a serious dislocation of productive activities. For all intents, Greece was reduced to the Greater Athens Area. Creative entrepreneurial initiative was often stifled. A short-term-gain opportunistic mentality was fostered and set the tone of economic life. Last, but not least, the so called "informal economy" thrived.

Above all, the wealth generating potential of the country has been gravely underexplored and/or underutilized. For a number of years, it has been my firm belief that Greece has a large reservoir of untapped resources. By this I mean both natural and human resources and, also,capital. This belief has been substantiated by my experience at the head of the Commercial Bank.

My concern with the past is not derived from a negative attitude of idle criticism. Rather, I intend to use it in order to illustrate the potential dynamic of the greek economy. Especially given our current awreness of our gap from the EEC countries, of our growth potential, of the feasibility of bridging this gap and of the necessity of adjustment in the light of 1992.

More specifically,my point is that if the distorted pattern of economic growth has left us with accumulated problems, it has also bequeathed to us a backlog of unexplored and unexploited opportunities. After a protracted and often painful period of transition, Greece is currently moving in the direction of closing the gap between potential and actual performance. As this process gains momentum, in conjunction with other dynamic factors which will be considered further on, it is bound to have an explosive impact on the greek financial markets. Especially so, since, as already mentioned,the prospect of 1992 has played and will continue to play a catalytic role in speeding up institutional and economic modernization and adjustment.

Let me briefly indicate some of the areas which concentrate growth potential and which have been identified by the market experience of our group of companies:

-to begin with, in view of Greece's natural comparative advantage in quality products, there exists considerable room for improvement in the restructuring and upgrading of such traditional sectors of the greek economy as the food industry and most branches related to the processing of products of the primary sector. This has been more than corroborated by 3 special regional investment opportunity studies commissioned by the Commercial Bank of Greece discussed yesterday in the Bank's workshop.

-the services sector, with the exception of tourism has been virtually unexploited as a competitive, growth industry. I will have shortly more to say on the tremendous potential of the financial sector. But, also, with a proper mobilisation of its human resources, including scientists working abroad, Greece will reveal a comparative advantage in areas currently deemed the exclusive province of advanced countries such as subsectors of information technology and services and engineering consulting.

-the shipping sector with its allied manufacturing and service activities such as shipyards, sea transportation and marine insurance. The greek commercial fleet ranks first in terms of ownership and third in terms of flag in the world.

These should be viewed against the background of favourable factors such as:

-the location of the country in the heart of Eastern Mediterranean and in close geographical and also historical proximity to the Middle East.

-the above also apply to countries of the Eastern Bloc, especially the Soviet Union, in view also of a millenium of religious and cultural ties.

-the benefits accruing to investors and customers from Greece's membership in the EEC.

-the talent coupled with the required managerial and technical expertise of greek manpower currently employed domestically or abroad.

-the economic.social and political stature of over four millions of greek expatriates.

Previous speakers, more competent in the area of macroeconomic analysis and policy have presented the recent developments in the greek economy. In their broad lines, they indicate a significant change in the economic climate. More importantly, as the Prime Minister has argued recently, during the last few years, we have achieved a degree of social and political stability and cohesion unknown in the past. These are indispensable factors for the economic transformations leading to growth.

If this process continues, our very distance from the main EEC countries which is currently considered our main handicap will be transformed into an engine of growth by the dynamic of catching up, of convergence which will gain momentum in the unified EEC market. And, more significantly, by the increasing awareness of the gap as well as of the steps required to close it.

The same combination of structural problems and latent opportunities is to an even greater extent characteristic of the greek financial system as it evolved in the postwar period. The end-result of this evolution has been a financial sector virtually monopolized by the banking system. In turn, the banking system has been highly oligopolistic: the three largest banks control over 70% of the market. With rare exceptions,it has operated in a protected environment and has been heavily regulated in most of its basic functions: interest rate level and differentials, rate of credit expansion,credit management and foreign exchange.

Greek banking has therefore developed into a highly centralized system. In terms of performance it has, in general, fallen well behind the current international standards especially in the areas of managerial structure and mentality and of the range and quality of banking products and services it offers to its clients. In the process, it has beeen a major contributing factor to the misallocation of resources and the underexploitation of valuable productive opportunities and initiatives noted above. Not least by downgrading the potential and needs of the greek regions outside the Greater Athens Area.

The above argument helps to explain the apparent paradox that a country with a relatively overgrown banking sector (in terms of its relative importance in the overall fianacial activity) is essentially seriously underbanked as far as its actual market needs and development requirements are concerned.

The identification of the problems and shortcomings of the greek banking system has a dual use: On one hand, it helps to determine the steps that need to be taken. On the other hand, however, it reveals the potential scope of achievable progress and, consequently, of profits for the financial intermediaries.

In fact,the greek financial system currently stands at the crossroads. As we approach the 21st century with the imminent prospect of a unified EEC financial market well in sight, the name of the game is modernization, deregulation and institutional reform.

I would like to suggest that the present challenge will be met and is, in fact being met. I would, further like to draw your attention to the synergistic effect of:

-the unexploited growth potential of the greek economy,

-the globalization of financial activity with actual direct presence of firms in the markets, rendered possible by the revolution in telecommunication services

-the scope for growth and progress in the greek financial system in conjunction with its institutional reform, already well under way and with the necessity to prepare for the full financial integration in the EEC market in 1992.

The combination of these factors is bound to lead in the medium term to a veritable explosion in the greek financial market. It is also clear that the changes of structure that have to be made as well as the pace of change required are of a different type and order of magnitude from markets in most other EEC countries.

Let me briefly indicate the scope of the challenge that the greek financial markets will be facing as an outcome of the economic and financial growth potential with special reference to the related capital movements:

-capital will have to be relocated on a great scale from the Greater Athens Area to the regions of the country. Such a relocation will concern practically every sector of the greek economy besides the primary.

-the market will have to attract and channel, mainly towards the regions the personal and corporate savings of the greek expatriates.

-especially it will have to attract the savings of greek shipowners on condition of developing the proper instruments and experience for servicing the specific financial needs of their business.

-out of a total of domestic savings of 4 trillion drachmas, about 1 trillion will have to be redirected from the banking sector where they currently reside to the capital markets at large.

-capital will have to be transferred towards industry and service sectors of medium and high technological content which are currently often being underfinanced.

-provision must be made for the profitable accommodation and use of the expected substantial increase in the traffic of foreign exchange.

Clearly all the above movements require a radical quantitative increase and qualitative improvement of financial intermediation in Greece. Add to this the intensification of international competition and the dismantling of the system of domestic protection by 1992. I think we are justified in speaking of an imminent explosion of the greek financial markets.

How will the greek markets and agents face up to this challenge?

My view is that we must face the future with a combination of guarded optimism and intensified alertness.

A number of developments since 1974 and especially in the last five years give us sufficient grounds for optimism:

-social and economic decentralization is well under way. For the first time greek regions acquire their own economic features and stature, rather than being mere appendages of Athens.

-in the last two years, we are witnessing a steady movement towards the institutional reform of the financial system focusing on deregulation and modernization. I should specially mention the in depth analysis of these issues carried through by the Ministry of National Economy which is gradually being implemented by means of practical directives.

-the mentality of greek business is changing in the direction of a more managerial and professional attitude towards its tasks

-the overall international exposure of our economy has significantly increased which leads to an emphasis on competitiveness and to a more rapid diffusion of modern technology and of modern managerial and work practices.

-we are gaining an increasing awareness of our unexploited resources and growth potential.

-we have succeeded in establishing a stable political environment and we are under way towards a significant improvement in industrial relations.

-in our modernization process we are profiting from the cooperation with experienced foreign counterparts and by avoiding the errors made by the more advanced countries.

This is not to say that mistakes have not been made or that all setbacks have been eliminated. But the broad thrust of improvement has been established.

Optimism, however, must not imply complacency. As I argued above we need to face developments with an increased alertness. The realization of the growth potential of the greek economy and financial system requires primarily a great deal of work. In the banking and insurance sector we are just beginning to adapt to a market which is being liberalized. We pay special attention to diversifying our products and services, in particular,venture capital companies, leasing, factoring etc. all indispensable instruments for development finance.We combine our conventional banking activities with a host of related services such as insurance, consulting etc. especially so as to respond successfully to the complex needs of customers as the greek shipowners.

These are necessary adjustments that we make in order to maintain our domestic market share. In other words, they are part of our defensive strategy. But we also formulate an offensive strategy. We embark on an expansion abroad, starting with our natural markets (greek expatriates,shipowners etc). We will also expand and upgrade our operations so as to establish Greece as the main financial center of the Eastern Mediterranean.

A similar challenge, though in an entirely different economic and historical context, faced the greek financial community at the beginning of the Sixties. For a number of reasons the opportunity was lost at that time.

Today we stand at the crossroads once again. Only now the stakes are higher.For it is not only the banking industry that is being challenged. Rather the resiliency and dynamism of the entire economy are being put to test.

The lessons have been learned. Human ability, knowhow and will for change all exist. The results, so far, have been positive and encouraging. Thus, our optimism that the the greek financial system will respond and develop is well justified.

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THE SPANISH ECONOMY TWO YEARS AFTER ITS ENTRY INTO THE EUROPEAN COMMUNITY

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1. HIGHLIGHTS ON BASIC DATA

Spain covers slightly more than 500.000 sq km, which is about 22% of the Twelve. Spain's total population is at present about 39 million, or 12.1% of the Community's.

In 1985, Spain's GDP at current prices and purchasing power parities, was estimated to be 293.000 million US$, i.e. about 9% of that of the Twelve. Spain's per capita GDP was about 7.600 dólars compared with an average of 10.500 dólars for the Community.

Table 1. A few basic data (1985)

	EUR-12	Spain	Spain/EUR-12
Area (mil sq km)	2256	505	22.4
Population (million)	322	39	12.1
GDP (bill.US $)(*)	3378	293	8.7
Per capita GDP (US $)(*)	10490	7596	72.4

(*) Expressed at current prices and purchasing power parities.

Source: Eurostat.

The present structure of Spanish GDP by main sector of origin is as follows: agriculture and fishing, 6.2%: industry, 30.5%; construction, 6.8% and services, 56.5%. As can be seen from the following table, this structure does not differ significantly from that of Community GDP.

As regards demand, private consumption accounts for a relatively large share of Spain's GDP compared with the Community, while the shares of public consumption and foreign trade are smaller (Spain's economy being less open to the foreign sector).

Table 2. Structure of GDP, 1985 (% of total)

	Spain	EUR-12
Supply		
- Agriculture and fishing	6.2	3.4
- Industry & Construction	37.3	37.1
- Services	56.5	59.5
Demand		
- Private consumption	64.5	61.3
- Public consumption	14.0	18.5
- GFCF	19.1	18.6
- Exports	23.2	31.9
- Imports	21.0	30.8

Source: Eurostat and INE.

The age structure of the Spanish population is slightly younger; the under-15 population accounts for 23.6% of the total and those aged 65 and over for 11.9%. The comparative figures for the EC are about 19.1% and 13.3%.

Basic data for the labour market show that the participation rate in the Spanish economy is lower than in the Community (the respective figures for 1984 were (35.8% and 43.3%).

As regards the structure of employment, the relevant figures for the Spanish economy show that agriculture accounts for a larger proportion of the working population 16.9% compared with 8.6% for the Community; this is balanced by the smaller employment share of the service sector.

Concerning the level of unemployment, the situation in Spain is markedly worse. In 1984, Spain's unemployment rate was slightly more than 20%, i.e. almost twice that of the Ten.

Table 3. Population and the labour market 1985

	Spain	EUR-12
Age structure (%)		
0-14	23.6	19.1
15-64	64.5	67.6
65 and over	11.9	13.3
Participation rate (%)	35.8	43.3
- Agriculture and fishing	16.9	8.6
- Industry	32.1	33.8
- Services	50.9	57.6
Unemployment rate(%)	2.9	11.6

Source: Eurostat and INE.

Despite the relatively rapid expansion of Spain's foreign trade in recent years, the Spanish economy is still less open than the Community average. Exports and imports each account for about 20% of Spain's GDP, against 30% in the case of the Community.

Spain is a country with a relatively high degree of dependence on energy: in 1986, energy accounted for more than 19% of the value of its imports compared with an average of 11% for the whole Community.

Raw materials also represent a significant proportion of total imports - 9.9% approximately, compared with 6.6% for the Community. Consequently, imports of manufactured goods, excluding capital equipment, account for a smaller proportion in Spain's case than in the case of the Community.

The structure of Spanish exports however, is much closer to that of the Community. In all, 43.5% of exports are manufactured goods.

Finally, as regards the geographical pattern of Spain's trade, somewhat more than one-half of imports come from the Community, a little over two-thirds from the OECD countries. As regards exports, approximately 80% go to OECD countries and a little over 60% to the Community.

Table 4. Foreign trade, 1986 (% of total)

	Exports		Imports	
Geographical pattern	Spain	EUR-12	Spain	EUR-12
* OECD	77.2	81.3	71.1	80.6
- EEC	60.3	57.1	50.3	57.1
- USA	9.2	9.3	9.9	7.3
- Other OECD	7.7	14.9	10.9	16.2
* OPEC	5.6	4.4	11.3	4.8
* Latin America	4.6	1.5	6.7	2.4
* Remainder	12.6	12.8	10.9	12.2
Breakdown by product				
* Food, drink and tobacco	14.9	10.4	11.2	11.9
* Raw materials, oils and fats	4.4	3.3	9.9	6.6
* Fuels, lubricants and related products	6.3	5.2	18.9	11.5
* Chemicals, manuf. goods and misc.	43.5	45.6	30.8	41.3
* Machinery and transport equipment	30.9	35.5	29.2	28.6

Source: External Trade Statistics, OECD.

2. THE SPANISH ECONOMY IN PERSPECTIVE

2.1. The Spanish economy in the pre-crisis period

After a long period of self-sufficiency starting from a very low level of development, the Spanish economy's growth and relative performance during the 1960s and the early 1970s were particularly satisfactory.

This made it possible to reduce substantially -but not to eliminate altogether- the large gap between the Spanish economy and other main industrialized countries.

Between 1960 and 1974 the average annual growth in real GDP was over 7%. At the same time, the unemployment rate was only around 1.0% of the labour force, and there were no imbalances of major importance in either foreign trade or the public sector.

Essentially, this period of high growth rates reflected such factors as the need to rebuild the infrastructure (transport, communications, housing and so on), the launching of basic industries (steel, shipbuilding, textiles, etc.), the gradual penetration of foreign markets, and the spectacular development of tourism. All this took place in the context of low labour and raw-material costs and easy export of surplus labour supply.

Nevertheless, even during the early 1970s this growth pattern was showing clear signs of strain.

2.2. The Spanish economy during the crisis (1974-82)

In these circumstances, the sudden economic crisis hit the Spanish economy particularly hard. In 1982, unemployment reached 16,2% of the labour force and the inflation rate was about 14,5%, while the current account deficit and the net public sector borrowing requirement amounted to 2,5% and 5,9% or GDP respectively.

Of course, during this period the economic situation in all Western countries worsened to different degrees, but everything seems to indicate that Spain suffered to a relatively greater extent.

Among the causes of this comparatively more serious deteriorations were:

(i) in Spain, the onset of the economic crisis coincided fully with the process of political transition;

(ii) there was no serious adjustment to the changed energy situation, with, as a result, an excesive use of energy inputs, a decline in the external balance and a deterioration in the terms of trade;

(iii) during this period the Spanish economy also experienced spectacular growth in wage costs, in real as well as nominal terms. The wage explosion added considerably to inflationary pressures, reduced Spains external competitiveness and encouraged the substitution of capital for labour;

(iv) In the same period, the public sector accounts also deteriorated significantly. Thus, the net general government borrowing requirement (which was practically nil before 1975) rose to 2,5% of GDP in 1980 and 5,6% in 1982;

(v) a last important factor was the lack of an industrial policy of positive adjustment to steer the productive base towards activities compatible with the change in demand, the international division of labour and competitive positions.

2.3 The process of adjustment, 1983-85

As formerly said, the Spanish economy in late 1982 was characterized by strong inflationary pressures, a worrying negative external balance and a tendency for the public deficit to grow rapidly, all of which was combined with a high degree of unemployment and a virtually stagnant level of activity.

In these circumstances, the fundamental priority objective of the Government was to correct the basic economic imbalances. This was essential if activity was to recover and more jobs were to be created.

The imbalances were corrected by applying a series of specific measures, which included an adjustment of the peseta exchange rate (December 1982), strict control of monetary aggregates, wage moderation, the containment and subsequent reduction of the public deficits, the application of industrial conversion measures in the sectors affected by the crisis, and the financial reorganization of public enterprises including reprivatisation of some of them.

From late 1982 to the year 1985, the adjustment policies applied had a positive effect on most of the imbalances.

There has been a turnaround in the external situation, the 1982 deficit on current account of 400 billion pesetas has given way to a surplus of 450 billion or 1,7% of GDP in 1985.

The inflation rate, as measured by the consumer price index, fell from 14,4% in late 1982 to 8,2% in late 1985. The moderation in the growth of wage incomes is apparent from the real wage per person employed, the average real growth for which in the three-year period from 1982 to 1985 was nil. Wage moderation has helped to give a substantial gain to gross operating surplus which, expressed as a proportion of GDP, went up from about 46,8% in 1982 to about 50,1% in 1985.

Table 5. Basic macroeconomic performance.

	1960-74	1975-82	1983-85	1986-87
- GDP(annual %)	7.1	1.5	2.0	4.2
- Gros Fix.Cap.Form.	10.4	-1.8	-1.3	8.5
- Employment	0.9	-1.8	-1.6	2.6
- Unemploy rate(%) (*)	(1.1)	(16.2)	(21.9)	(19.9)
- Inflation(GDP def.)	7.4	17.0	10.4	7.0
" (*)	(17.5)	(14.5)	(8.3)	(5.3)
- Bal.on c.acc.(% GDP)	1.8	-0.5	0.5	1.1
" " "	(-3.5)	(-2.5)	(1.7)	(0.3)
- P.S.Bor.Req.(% GDP)	n.a.	-2.0	-5.6	-4.6
" " " " (*)	(0.2)	(-5.6)	(-6.7)	(-3.6)

Source: Eurostat and INE. (National Institute of Statistics).
(*) Figures in brackets correspond to the situation at the end of the period.

Finally, it can be said that the above achievements were accompanied by moderate growth in the economy. The annual increase in GDP during the last three years (slightly more than 2% on average) was higher than in the previous. Much progress has been made in restructuring the industries worst hit by the crisis notably steel and shipbuilding.

Alongside the positive trend described, it is clear that certain imbalances persist, notably in such fundamentals areas as of unemployment and public sector deficit which remains too high.

2.4 The entry into the EEC and the expansion of the economy

Two years after joining the European Community, a first assessment of the impact this membership made on Spain is fitting, particularly as it relates to the effects of the introduction of VAT, accelerated restructuring, heightened investment and the marked worsening of the country`s trade balance.

As of day one of Spain`s entry into the EC, VAT, a comparatively simple system with three tax rates (6%, 12% and 33%) superseded a complex system of indirect taxation with more than 24 tax rates. The imppact of VAT`s introduction was limited in terms of tax collection, since a principle of equivalency between the old and new systems was respected; it was also limited in terms of prices, since its net impact is estimated ast two percentage points above the prevailing 8% rate of inflation.

It is also generally considered that Spain`s entry into the EC sped up the restructuring of the country`s system of production and stimulated investment, all because of the new economic framework of reference. This framework is characterized by sharper competition, new market prospects and more pronounced comparative advantages.

Foreign investment grew substantially during Spain`s first two years of EC membership as well. Direct investment in productive capital rose by 95.8% during the first two years, standing at 2,600 million dollars in 1987. This figure accounted for 4.4% of gross capital formation last year.

The most direct and significant effect of Spain`s new membership has nevertheless been the notable weakening of the country`s trade balances.

table 6.-FOREING TRADE BY GEOGRAPHICAL AREA

	Comm. Bal. (Mill. US $) 85	87	Cover rate 85	87
OCDE TOTAL	-28	-9128	99.8	74.9
- CEE	1628	-4988	114.7	81.4
. France	969	102	134.7	101.6
. RFA	-860	-3799	72.9	51.9
. Italy	329	-1299	123.9	70.0
. UK	127	-194	106.5	94.4
PVD	-6030	-5840	48.5	48.4
- OPEP	-4271	-3068	29.1	33.8
TOTAL	-5688	-14919	81.0	69.6

As is evident from the attached table, Spain`s overall trade deficit swelled from 5,700 million dollars in 1985 to 15,000 million dollars in 1987. This widening reflected primarily trade with OECD countries, in general, and EC member countries, in particular. In fact, Spain`s trade balance with the EC went from a 1,600 million dollar surplus in 1985 to a 5,000 million dollar deficit in 1987. This decline can also be seen in changes in the cover rate which, over the same period of time, fell by 11 points with respect to the world total and as much as 33 points with respect to the EC.

Of course, this marked decline cannot be wholly attributed to Spain`s entry into the EC. Other equally influential factors include the upsurge in domestic demand and the gap between the growth rate of Spain and that of Europe as a whole.

In this respect, 1986 and 1987 witnessed a sharp increase in the overall elasticity of imports with respect to total demand, which was registered at 4%, in contrast with 0.9% during the 1975-85 decade and 1.6% during the 1965-74 decade, a period characterized by an equally strong rate of growth. In light of the above figures, had the rate of elasticity remained at around 2% (a figure more in keeping with Spain`s economic experience, as well as that of other countries with a similar economic structure), nearly half of the upsurge in imports observed over the past two years would, at firts glance, have directly reflected new inroads made by foreign products in the domestic market.

The recent trends in economic indicators shows a progressive accentuation of the Spanish economy upswing in progress since the middle of 1985. The 1986 and 1987 balance sheet for the Spanish economy is clearly positive. According to the National Institute of Statistics`s (INE) estimates, Spain`s economic expansion raised real GDP growth to 5.2% in 1987, which is an all-time record since the start of the crisis and twice the growth rate registered by major world economies.

Factors fueling this upward trend include the healthy performance of Spain's various production sectors as a whole, growing domestic demand and, within domestic demand, investment.

As far as the country`s various economic sectors are concerned, the primary sector`s real product in 1987 was up 9.5% from 1986, that of the industrial sector, 5.7%, and that of services, 4.5%.

On the demand side, the real overall GDP growth rate of 5.2% mentioned above can be broken down into an 8.1% increase for domestic demand as a whole and the minus 2.8 percentage point contribution of foreign demand. The spectacular increase in domestic demand stems primarily from the sharp 5.2% rise in private consumption and, particularly, the 13.8% upsurge in gross fixed capital formation, with 10.5% reflecting investment in construction and 19.0% capital goods investment. This upturn in capital goods investment should be viewed as highly positive, for it ensures the expansion and modernization of Spain`s production capacity, heightened productivity and competitiveness and an adequate level of growth and job creation in the future.

It should be noted that the growth rate of exports was 2 percentage points ahead of the growth rate of foreign market imports. This means that Spain`s market share has actually grown.

The real overall 23.2% boost in imports in 1987 reflected a 12.3% increase in energy products and a 26.8% increase in non-energy products, figures which exceeded all early forecasts.

One of the highlights of the 1987 economic balance was, no doubt, the improvement in employment, raising to 814,500 (up 7.6%) the net total number of new jobs generated since the second quarter of 1985, a moment in which the labor market decidedly changed course. Nevertheless, the total labor force grew by an equally notable figure, practically cancelling out the improvement in employment. As a result, the jobless rate remained virtually unchanged.

Prices also followed a favorable pattern. Over the course of 1987, the general CPI hovered at around 4.6%, or 4 decimal points below the initial target. The inflation differential between Spain and other Western countries was narrowed to a little over one percentage point, in sharp contrast with the 5.6% gap existing at end-1986. Wage costs continued their descent last year, as evident from the 6.5% wage hike agreed-on in 1987, compared with 8.1% in 1986 and a 5.4% increase in unit wage costs for the economy as a whole, which is practically no increase at all in real terms.

Provisional estimates for Spain`s 1987 balance of payments show a pts. 23 billion surplus on current account, representing 0.1% of GDP and a decline compared with the pts. 574 billion posted the year before. The trade blance in 1987 stood at pts. -1.6 trillion (4.5% of GDP), nearly twice the 1986 figure. The favorable performance of invisible transactions made it possible to offset the trade deficit and even out the balance on current account. The long-term capital account balance turned around spectacularly in 1987. After posting deficits of over pts. 400 billion in 1985 and 1986, this account showed more than pts. 1 trillion surplus last year. This development, together with the vast influxes of short-term capital attracted by high domestic interest rates, heavily fueled reserves, registering over 30 billion dollars at end-1987, or twice the 1986 total.

Money markets showed some peculiar characteristics in 1987. Private sector liquidity (ALP) overshot earlier-programed targets, interest rates climbed and difficulties arose when trying to reconcile money supply controls and the inopportune upward pressure on the peseta in the foreign exchange market. Higher interest rates exerted upward pressure on the value of the peseta, a far from desirable result, given the gradual widening of the country's trade deficit and the need to avoid placing any sort of handicap on Spanish exports. In the second half of the year, the approach of monetary policy was considerably more flexible. Consequently, existing pressures eased up substantially, with the price of money gradually falling and the unwelcomed upward pull on the value of the peseta diminishing.

Turning to the public sector, 1987 can also be seen in a positive light. For the second year in a row, the General Government borrowing requirement in terms of GDP percentage was reduced, dropping to 3.6%. This notable decline was particularly favored by the strong growth rate of revenue -gaining 1.5% in terms of GDP- and the slight decline in expenditure- around .6% in terms of GDP.

3. ECONOMIC POLICY PRIORITIES AND MACROECONOMIC PROSPECTS FOR 1988/1989

After this basically positive balance sheet for 1987, a year in which economic progress was bolstered on all the country's major fronts, short-term prospects are shaped by the need to maintain current economic expansion (conditioned by a rather unfavorable international climate), to preserve and strengthen Spain's basic balances and to preclude the harmful effects of foreign sector bottlenecking, arising from far too wide a gap between the domestic growth rate of Spain and that of other industrialized countries.

In this regard, little support can be expected from the international economy, since forecast industrial growth worldwide is relatively low. Nonetheless, no pressure is expected to be exerted on the price of raw materials -crude oil, in particular- or on exchange rates or financial markets.

The main aim of current economic policy is to bolster a high rate of growth, which will generate new jobs and lower unemployment, to modernize the country's production system and to prepare the economy for its role in the 1992 single European market. Beyond a shadow of a doubt, the adjustment in foreign trade balances, inflation and public deficit accomplished in recent years has helped to achieve that aim and should ensure the continuance of the current economic upswing.

In order to atteint these objectives, economic policy will continue to be to strengthen the country's investment and export capacity. This, in turn, means maintaining and enhancing competitiveness and profitability, moderating unit production costs, gradually reducing the cost of credit, better allocating resources and fixing the value of the peseta that, without artifically supporting exports, does not obstruct the flow of Spanish goods and services abroad.

Nevertheless, attention should be given to the medium-term factors that could upset the self-sustained growth of production and, in particular, to keeping Spanish products competitive. In this regard, though the high level of reserves and the influx of foreign investment afford ample room to maneuver, the structure of Spain's economic growth should gradually be brought into balance by reducing the foreign sector's negative impact on the country's real growth rates.

Over the last three years, capital good investments rose by 46% in real terms, giving evidence that Spain's production system is quickly modernizing. Little by little, this process is helping to reduce the income elasticity of Spanish imports and to carve out a larget market share for Spanish exports. To ensure the attainment of both these objectives, unit labor costs must be kept down and measures must be taken to prevent the influx of speculative capital from exerting upward pressure on the peseta.

Indiscriminate wage moderation alone is not enough to guarantee low unit labor costs. The best way to ensure moderate costs must also take into account the basic components of labor market operations -vocational training, job mobility, the structure of wage bands and so on-.

The need to prevent the influx of speculative capital from appreciating peseta should be linked to the desirability of lowering Spain's high interest rates even further and to the problem of controlling both the growth of money supply and interest rates simultaneously through monetary policy.

For its part, 1988 fiscal policy, with the latitude afforded by automatic stabilizers set in motion when economic activity is high, aims to continue paring back the public sector borrowing requirement in terms of GDP, without reducing its role in the expansion of domestic demand.

Bearing in mind all of these considerations, if we turn our attention to short-term prospects, in 1988 the two main components of domestic demand are likely to grow at a slower pace. In any event, the expansionary inertia characterizing early 1988 and the above considerations regarding a supportive fiscal policy will significantly limit the scope of any possible deceleration.

Table 7

MACROECONOMIC PROJECTIONS
Percentage Change

	1986	1987(p)	1988(e)	1989(e)
Private consump....	3.7	5.2	4.0	3.5
Govt. consump......	5.1	9.0	5.0	3.5
Gross fix.cap.form.	9.6	13.8	11.4	9.1
- Construction.....	6.5	10.5	9.0	7.0
- Capital goods....	14.7	19.0	15.0	12.0
Domestic demand....	6.0	8.1	5.7	4.7
Export.goods & serv.	1.0	6.7	4.8	4.0
Import.goods & serv.	15.4	21.4	12.5	8.1
G.D.P.............	3.3	5.2	4.0	3.7
PRO MEMORIA				
GDP deflator.......	10.9	5.7	4.9	3.4
CPI Dec/Dec (2)....	8.3	4.6	3.0	3.0
Employment	2.2	3.1	2.6	1.7
Current acc.bal. %GDP..............	1.7	0.1	-0.8	-1.6
State cash deficit % GDP.............	-4.5	-3.8	-3.4	-3.0

(p) provisional
(e) estimates

Source: INE and Dirección Gral. de Previsión y Coyuntura.

Thus, the forecast rates of growth for private consumption (4%), investment in construction (9%) and capital goods investments (15%) are, barring any sudden changes in the world economy, clearly conservative. The slowdown in domestic demand and the foreseeable decline, compared with the past two years, in the income elasticity of imports point to a 12,5% increase in the volume of goods and services imported in 1988, down 9 percentage points from the 1987 growth rate.

The volume of goods and services exported will likewise slip from 6.7% in 1987 to 4.8% in 1988. As a result, the negative contribution of the foreign sector to GDP growth will fall from 2.8% in 1987 to 1.8% in 1988, realigning the structure of Spain`s economic growth and avoiding the excessive widening of the current account deficit, which will nevertheless hover around 0.8% of GDP. The real rate of GDP growth is so far estimated at 4%, nearly twice the rate forecast for other Western countries.

The decline in labor costs and the favorable prospects for the real terms of trade, heavily dependent on oil price assumptions, may reduce, with the aid of a vigilant monetary policy, the average annual growth of the deflator for domestic demand to 4.1% and of the deflator for GDP to 4.9%. These rates are consistent with a December-to-December CPI increase of 3%.

Lastly, 1988`s growth rate of employment, though slightly below that of 1987, should continue to be healthy. Nevertheless, if the high influx of new, mainly female, workers into the labor market continues, the reduction in the jobless rate will be curbed considerably.

The assumption regarding economic trends in 1989, summarized in the attached table, are subject to a greater degree of uncertainty and are based on a slightly more depressed international economy. In general, these forecasts point to a slight downturn in domestic demand and employment, though their respective growth rates will outdistance those of other Western countries, and a further reduction of the negative contribution of the foreign sector to GDP growth.

PANEL DISCUSSION:
COMPETITIVENESS AND THE EUROPEAN LABOUR MARKET

John Morley (Chairman)
Head of Division
European Economic Commission

PANEL DISCUSSION:
COMPETITIVENESS AND THE EUROPEAN LABOUR MARKET

Chairman's Introduction

John Morley
Head of Division
European Economic Commission

My principal task, and pleasure, this morning is to introduce to you two key Greek members of that population of people that we in Brussels like to call the social partners and to which my countrymen in Britain persist in referring as the two sides of industry. Whatever their title, however, their role remains the same, namely to guide the development of labour relations - whether at the level of the firm, the sector or the whole economy - and to negotiate on concrete issues such as conditions and terms of employment. As such, they are at the heart of successful businesses and economies.

But I have been asked, before giving them the floor, to make some brief introductory remarks about the state of the European labour market as a whole and about the prospects for its development as we move towards the crucial date of 1992.

First, I think I need to move a little onto the defensive. Image is something that is hard to acquire and equally hard to get rid of if you don't like the one you have and I think it is fair to say that Europe has had only a moderately satisfactory image in recent years as regards employment performance. In three significant respects it is commonly seen to compare less well with some other economies, notably that of the United States.

First, it is seen to compare less well in terms of total job creation - in aggregate macro performance. Secondly, it is seen to compare less well in terms of its flexibility and adaptability - its capacity to cope with change - micro level efficiency. Thirdly, Europe is seen to rely too heavily on centralised, government-led policies and insufficiently on entrepreneurial drive.

I think the first of these statements is misleading - and based on some misreading of the statistical evidence - and the second and third are frankly outdated assessments.

Job growth in Europe has been slow and insufficient to reduce what is widely recognised as an unacceptably high level of unemployment. But comparisons of Europe's job growth total of 2m to 3m over the last decade with the US growth of some 5m is not comparing like with like. Over that same period, the US population - and especially its population of working age - grew at a very fast rate. In effect, the employment growth was a counterpart, a corollary of that population growth.

In contrast, Europe's working population grew very little over that period so that, while we did fall short of our own employment targets, the shortfall was much less than crude aggregate comparisons with the US apparently suggest.

As regards the issue of labour market flexibility or efficiency, this concept is frequently measured by crude indicators such as the rate of job turnover - the rate of hiring and firing onto the labour market. Whilst this is one method of coping with change - and one much used in the United States - it is not the only one and it is not necessarily the most efficient. It has high costs - both directly and also indirectly through the loss of loyalty and team skills that it inevitably implies.

A truer overall measure of success is the speed with which the whole enterprise, including its labour force, can shift its operations in line with market demand and in that respect European-based businesses have shown a considerable capacity for internal change and development in recent years.

This is all the more remarkable because it has been achieved in a period of relatively low economic growth and it is normally much easier to bring about such changes in periods of high growth rather than low growth.

The third characteristic on which Europe is commonly unfavourably compared is in the extent to which entrepreneurial flair is allowed to drive the economic and job-creating system. In that respect again, major changes have taken place in recent years.

There is a new spirit of change which has affected government just as much as the private sector, especially at the local level. My colleague Jerome Vignon spoke yesterday about the Integrated Mediterranean Programmes and the way in which the local level had become the focal point for the conception and development of actions rather than just the point of final implementation. This concept of partnership at the local level - involving local industries, multinationals, the banking community, local and central government, trade unions and action groups of all kinds - is becoming commonplace and has led to the economic transformation of many areas that had been suffering from underdevelopment or serious industrial decline.

In this respect we owe a debt of gratitude to the United States, where such approaches have been pioneered, but we now feel that the pupil has caught up with the teacher and in certain respects, such as in the use of Local Development Agencies, we are actually ahead and attracting interest from the US.

I should now like to say a few words about 1992 and the European labour market.

The Treaty of Rome lays down the basic conditions for the free movement of labour, just as it does for the free movement of capital goods and services, but we need to turn these basic conditions, the potential of the market, into a reality.

At present, there are two sorts of obstacles to labour movement. There are the administrative ones - the Catch 22 situation where a person needs a residence permit in order to get a job and he or she needs a job in order to get a residence permit. Such problems are tiresome and wasteful but surmountable and the Community is actively seeking to outlaw those practices that remain.

More serious have been the obstacles posed by the unwillingness of professional groups in individual EC countries to recognise qualifications awarded in another, thereby inhibiting the free movement of qualified people within the Community.

Much has been achieved in recent years in this respect and the plan is to complete the process by 1992. We now have agreements covering most of the medical profession - for example, dentists, pharmacists and doctors. Other professions will follow, architects being the latest to join the list. And we have agreements covering many qualification areas in such varied activities as car repairs, hotels and catering, building and so on.

But it is not just a question of aligning national standards in existing sectors and occupations. The challenge lies in relation to new jobs and occupations, especially the technology-based ones, so that we have qualifications and skills that, from the outset, are recognised across Europe as a whole. In this respect the banking industry has already made great strides and this is an example that is being built on in other sectors.

All this activity is of growing importance since European labour mobility in the future is likely to be very different from that of the past. Mass migration of unskilled labour from the south of Europe to fill industrial workplaces in the north is most unlikely to return. Changing technology and changing patterns of production no longer require this and it has also proved culturally unsatisfactory. Nor are we likely to see the resumption of one-way brain drains.

What we are likely to see is much greater movement of skilled and trained personnel, moving along with other factors of production, to and fro across Europe, in ways that are already commonplace within individual countries and within the internal labour markets of some multinational firms.

Thus we have the prospect of developing a genuine European labour market that combines many of its traditional qualities and strengths - notably the high level of skills, experience and loyalty of the labour force - within a much more flexible overall system.

The social partners have done a great deal to transform their traditional relationships and provide a sound basis for expansion in the future and I believe that they, like we in the Commission, are waiting not a little impatiently for the counterpart effort by national governments within Europe to co-ordinate fiscal and monetary policies more closely in order to encourage a higher rate of economic growth so that we can derive the full benefits from all the structural improvements that have been put in place.

PANEL DISCUSSION:
COMPETITIVENESS AND THE EUROPEAN LABOUR MARKET

Theocharis Papamargaris
President
Greek Federation of Bank Employee Unions

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I shall limit my remarks to the Greek case rather than take a general, European view.

First, how do we define competition? It's a question of price and quality in relation to similar products. In the case of Greek products, in terms of both price and quality, at best we are near our European counterparts but we are lagging behind in many other respects.

Who is responsible for this situation? Who is to blame? I am not here to point a finger at any one factor and single it out as being the chief culprit in the story but I should like to offer the viewpoint that the question of Greek labour and its remuneration is not at the heart of the problem.

From 1985 to 1987, to take only the last two years, when by administrative action we had a freeze on labour earnings in Greece, we had a fall in the real income of wage and salary earners, at least to my mind, in the region of 15% to 20%. Of course we should bear in mind that labour costs in Greek manufacturing are a relatively small percentage. One estimate is that they are in the region of 15% to 20% of manufacturing costs.

The second factor relating to the price aspect of the competitiveness of Greek products is that, again in the last two years, we have had about a 15% depreciation of the drachma in relation to the main European currency basket.

That was the price aspect in the case of Greek versus non-Greek products and competition. Quality, at best, is near European levels but still lagging behind in many other respects. Greeks tend to prefer European products rather than Greek ones because the price is competitive and quality in many cases is better.

A fourth point. If, during the past two or three years we have indeed had a drop in the real incomes of wage and salary earners, as also the depreciation of the drachma, why have prices inside Greece been rising in the region of 15% to 20% annually, thus rendering Greek products even less competitive than they were?

Point number five. Public sector deficits have, to a certain extent, provided an underlying potential for sustaining inflationary trends, but the main point that I want to put forward is that in Greece we have the phenomenon of mark-up inflation, ie unbridled readjustment of consumer prices on the part of producers, sellers and intermediaries, without real reference to what usually is considered by employers as the chief culprit of rising prices, namely labour costs.

Sixth, if labour costs are at not at the heart of the rising spiral of final prices, leading to less competitive Greek products inside the European Community, what is to blame? A gamut of factors is responsible for the situation: poor technology, qualitatively and quantitatively; managerial and organisational weaknesses, and bureaucratic impediments. All these factors, coupled with the fact that over the past 10 years we have suffered a general unwillingness for investment, make up the present Greek scene concerning competitiveness in terms of price and quality.

If this is the essence of things, what do we do? One does not have to be enamoured of seeing things always from the labour point of view, or of the idea or ideal of European integration, in order to be realistic and try, inside the present framework, not only to better the lot of the workers, the salary and wage earners, but also to have an overall view of where the Greek economy is going and try to improve things there. There are 10m Greeks. It is somewhat unrealistic to think that we can transplant 5m to Sweden and bring 5m Swedes here. We have to make do with what we have. Consistently, patiently and methodically - admittedly not Greek virtues! - and accepting foreign contribution, under controlled rules, of course, we have to find capital, expertise and know-how. This is the main problem for all of us, both labour and the other social partners, and we should not single out Greek manpower as being the only culprit.

In conclusion and independently of whether or not we are in favour of European integration, in the vast challenge ahead of us of 1992, not only in the banking system but in the overall anatomy and structure of the Greek economy, we have a very limited time horizon within which to speed up the rate of change. If we do not make these changes, both social partners and employers and employees will suffer from the outcome. We must therefore develop mechanisms for dialogue and participation in all the decisions that are being taken in relation to this challenge.

Greece, which is in a transitional stage at this phase of its history, must adapt, quicken the pace of improvement and adaptation, and face, hopefully in 1993, the challenge of a united European market. As I said at the beginning, one does not have to be either a fan or a devoteee of the European Community to accept realities. Whatever one's dreams and ideals, here and on the part of the labour movement, social realities mean that we will have to fight inside established forms of machinery providing for dialogue and consultation with other social partners.

PANEL DISCUSSION:
COMPETITIVENESS AND THE EUROPEAN LABOUR MARKET

Nicolas Analytis
Member of the Board of the Federation of Greek
Industries in charge of Social and Labour Affairs

N. ANALYTIS

EUROMONEY CONFERENCE

19 - 21/4/1988

I. I WOULD LIKE FIRST TO THANK THE ORGANIZERS OF THIS CONFERENCE, FOR THE HONOR TO INVITE ME AS REPRESENTATIVE OF THE PRIVATE SECTOR OF THE GREEK ECONOMY TO PARTICIPATE IN THE DISCUSSION OF LABOUR RELATIONS IN OUR COUNTRY.

PERHARS, A GENERAL STATEMENT OF QUALIFICATION, RIGHT AT THE OUTSET, WOULD BE USEFUL IN HELPING US CONFRONT THE SUBJECT IN ITS PROPER DIMENSIONS.

I WOULD NOT ASSERT AND I PRESUME NO ONE COULD CLAIM THAT, LABOUR RELATIONS IN GREECE CONSTITUTE A "HAVEN" IN EUROPE. BUT NEITHER DO THEY CONSTITUTE "HELL". GREECE IS NOT AN ISLAND IN THE WIDER EUROPEAN SPACE. IT FORMS A PART OF THE EUROPEAN ENTITY GEOGRAPHICALLY, CULTURALLY, AND ECONOMICALLY. THUS, IT MOVES ALONG WITH THE OTHER COUNTRIES OF THE EUROPEAN COMMUNITY: IT FACES THE SAME MORE OR LESS PROBLEMS, THAT THEY FACE; PERHARS AT A DIFFERENT STAGE OR SCALE, BUT, ESSENTIALLY IT MOVES IN THE SAME GENERAL DIRECTION.

GREECE HAS EMBARKED ON ITS OWN DIFFICULT COURSE TOWARDS THE EUROPEAN INTERNAL MARKET. AND, WITHIN A RELATIVELY SHORT PERIOD OF TIME. IT MUST MODERNIZE. SOCIALLY AS WELL AS ECONOMICALLY. IN ORDER TO SHORTEN THE DISTANCE AND NARROW THE GAP SEPARATING IT TODAY FROM THE COMMUNITY "AVERAGE", AND HENCE TO BE ABLE TO WITHSTAND THE TEST OF 1992.

WITHIN THIS BROAD FRAMEWORK OF "MODERNIZATION", WE MUST CHART THE CHANGES WHICH ARE NECESSARY TO OCCUR IN THE FIELD OF LABOUR RELATIONS IN SUCH A WAY THAT WILL ENSURE A SMOOTH TRANSITION.

IT IS EVIDENT THAT ALL SOCIETIES OF THE WESTERN WORLD -BUT EVEN THOSE OF THE EAST-, TEND TO DEVELOP A DIFFERENT LEVEL OF LABOUR RELATIONS AS THEY ARE ENTERING AND GOING THROUGH THE POST-INDUSTRIAL ERA. A LEVEL WHOSE MAIN FEATURE WILL PROBABLY BE A CONTINUOUS AND OPEN DIALOGUE WHICH WILL ENABLE THEM TO MAKE A QUICK AND SUCCESSFUL ADJUSTMENT TO THE REQUIREMENTS OF AN INFORMATION AND ROBOTICS ECONOMY WHILE MAINTAINING SOCIAL BALANCE.

I BELIEVE THAT GREECE ALSO IS AT THIS PHASE NOW.

II. HOW DO THE SO-CALLED "SOCIAL PARTNERS", WORKERS, EMPLOYERS AND THE STATE, FACE UP TO THIS CHALLENGE?

LET ME START WITH THE STATE:

IN GREECE, GENERALLY AND HENCE IN THE AREA OF LABOUR RELATIONS SPECIFICALLY, WE SUFFER FROM A VERY PERVASIVE AND EXTENSIVE STATE INTERVENTIONISM. SUCH INTERVENTIONS BY THE STATE ARE NUMEROUS AND VARIED. THEY ARE NOT LIMITED TO THE DETERMINATION OF THE FRAMEWORK OF LABOUR RELATIONS (THE RULES OF THE GAME IF YOU WILL) -SOMETHING EXPECTED AND NATURAL-, BUT OFTEN, OR I WOULD DARE SAY MOST OF THE TIME, THEY GO RIGHT ON DOWN AND THROUGH MINUTE DETAILS.

WE HAVE, NONETHELESS, MANY INDICATIONS THAT THIS SITUATION IS BEGINNING TO CHANGE: IT IS BECOMING INCREASINGLY UNDERSTOOD THAT, FOR MANY INSTITUTIONS, THE ROLE OF THE COMMUNITY AND ITS INSTRUMENTS WILL BE INCREASING AT THE EXPENSE OF THE NATIONAL GOVERNMENTS. THE GREEK GOVERNMENT, AT A POLITICAL LEVEL, IS EXPRESSING FREQUENTLY THE INTENTION TO REDUCE ITS OWN ROLE IN THIS CONTEXT. THUS, WE HOPE THAT WE HAVE ENTERED A ROAD LEADING TO THE REDUCTION OF INTENSE STATE INTERVENTIONISM AND TO A CORRESPONDING RISE OF CONFIDENCE IN THE EFFECTIVENESS OF ACTION BY THE SOCIAL GROUPS.

AS FAR AS THE SECOND SOCIAL PARTNER IS CONCERNED, THAT IS THE WORKERS, I MUST NOTE HERE THAT THE FOUNDANENTAL PROBLEM OF THEIR OFFICIAL REPRESENTATION -THE TRADE UNION MOVEMENT- IS ITS SUBMISSION TO AND ITS HEAVY-HANDED "GUIDANCE" (MANIPULATION) BY THE POLITICAL PARTIES.

MIND YOU, I AM NOT REFERRING TO THE IDEOLOGICAL AFFINITY TO POLITICAL PARTIES, BUT, TO THE ABSOLUTE CONTROL EXERCISED ON THE UNIONS BY THE PARTIES AND THE USE OF THE TRADE UNION MOVEMENT FOR SHORT-TERM PARTY MANEUVERS AND EXPEDIENCIES.

AFTER 1974, THE LABOUR MOVEMENT SPREAD RAPIDLY WITH SUCH DOMINANT FEATURES AS: THE CHALLENGE OR NEGATION OF EVERYTHING; CONFRONTATION; THE REFUSAL TO CONDUCT A REAL DIALOGUE, AND CLASS-CONSCIOUSNESS DOMINATING ITS IDEOLOGY. HOWEVER, SINCE 1986, WE WITNESS A PERIOD OF ADJUSTMENT TO THE "FACTS OF LIFE", WITH EVIDENCES OF REALISM AND ACCEPTANCE OF THE ECONOMIC NECESSITIES. THIS IS MUCH MORE VISIBLE IN THE UNIONISM OF THE PRIVATE SECTOR.

IN FACT, A SHIFT IN MENTALITY HAS STARTED TO TAKE PLACE AMONG WORKERS AND MANY UNIONS OF THE FIRST LEVEL -THOSE THAT WE CALL ENTERPRISE OR PLANT UNIONS-. THIS DIFFERENTIATED ATTITUDE RELATES TO THE ECONOMIC PROBLEM GENERALLY, AS WELL AS TO THE SPECIFIC PROBLEMS OF THE INDIVIDUAL COMPANY. IT IS

ONLY THIS SHIFT OF ATTITUDE AND MENTALITY WHICH COULD REASONABLY EXPLAIN THE REMARKABLE TOLERANCE DEMONSTRATED BY THE WORKERS DURING THE "STABILIZATION PROGRAM", WHICH LASTED MORE THAN TWO (2) YEARS AND RESULTED IN A REAL AND SUBSTANTIAL REDUCTION OF THE WORKERS PURCHASING POWER.

LET ME ADD HERE THAT IN THIS CONTEXT THE CONCEPT OF "PROFIT" IS ACQUIRING MORE AND MORE SOCIAL "LEGITIMACY" AND ACCEPTABILITY. ITS SOCIAL VALUE IS INCREASINGLY RECOGNIZED WHILE ITS INTENSE CHALLENGE, PREVALENT UP UNTIL 2 YEARS AGO, IS GRADUALLY LOOSING STEAM.

THE THIRD PARTNER, THE EMPLOYERS, ARE BECOMING CONSCIOUS OF THE NEED FOR THE CHANGES THAT THEY MUST FACE AND SUSTAIN EVEN MORE RAPIDLY THAN THE OTHER SOCIAL PARTNERS, MAYBE ON ACCOUNT OF THE VERY NATURE OF ENTERPRENEURSHIP WHICH BY DEFINTION MEANS INCREASED FLEXIBILITY AND ADAPTABILITY.

MOST EMPLOYERS/ENTERPRENEURS ARE AWARE THAT, ALONG WITH THE INVESTMENTS AND THE TECHNOLOGICAL AND ORGANIZATIONAL UPGRADING, IT WILL ALSO BE NECESSARY FOR THE INSTITUTIONS REGULATING LABOUR RELATIONS TO BE RESTRUCTURED AND UPDATED. THEY HAVE BECOME CONSCIOUS THAT THEY, THEMSELVES, MUST CONTRIBUTE TO THE ESTABLISHMENT OF A STEADY AND HONEST DIALOGQE WHICH IS AN ESSENTIAL CONDITION FOR IMPROVED LABOUR RELATIONS.

I WOULD NOT LIKE TO GIVE THE IMPRESSION OF A UNIVERSAL PHENOMENON PREVAILING IN THIS AREA AND WHICH, IN FACT DOES, NOT EXIST. THIS BEGINNING OF A CHANGE OF ATTITUDE I REFERRED TO, APPLIES TO A LARGE SEGMENT OF GOVERNMENT; OF TRADE UNIONS, AND OF EMPLOYERS. BUT, BY NO MEANS, DOES IT APPLY TO ALL. THERE ARE STILL A NUMBER OF REPRESENTATIVES, IN ALL THREE SECTORS, WITH DOCTRINAIRE THINKING, NEBULOUS SCHEMES OF MANAGEMENT, OLD-FASHIONED OPERATING HABITS AND MODES, E.T.C. THERE ARE STILL A NUMBER OF PEOPLE WHO, I AM AFRAID, HAVE NOT EVEN BEGUN, TO SUSPECT THE TOUGH CONDITIONS AS WELL AS THE NEW OPPORTUNITIES WHICH WILL BE FORTHCOMING, IN THE CONTEXT OF THE FREE COMPETITIVE ARENA OF THE INTEGRATED EUROPEAN MARKET.

WE SHOULD NOT FORGET THAT THE CENTRAL ELEMENT OF LABOUR RELATIONS IS THE WORKER HIMSELF AND A FEW WORDS ON HIS QUALITIES AND ATTITUDE TOWARDS HIS WORK ARE REQUIRED.

I TRULY BELIEVE, THAT THE GREEK HUMAN RESOURCE, IS ONE OF THE MOST SIGNIFICANT COMPARATIVE ADVANTAGES THAT THIS COUNTRY OFFERS FOR EVERY INVESTMENT. I AM CONFIDENT, THAT ON THIS ISSUE I NOT ONLY CAN CALL AS WITNESSES A NUMBER OF WELL-ORGANIZED GREEK ENTERPRISES BUT ALL THE FOREIGN AND MULTI-NATIONAL

COMPANIES WHICH OPERATE IN GREECE FOR MANY YEARS, AS WELL.

THE MOST EVIDENT CHARACTERISTIC OF THE GREEK IS HIS EXCEPTIONAL ADAPTABILITY. IT IS THANKS TO THAT QUALITY THAT THIS NATION WAS ABLE TO SURVIVE. MORE THAN 4.000 YEARS IN THIS GEOGRAPHICAL AREA WHOSE NATURAL RESOURCES ARE LIMITED. IT IS, IN FACT, THIS ADAPTABILITY THAT GREEK IMMIGRANTS DEMONSTRATED IN THEIR NEW ADOPTED COUNTRIES, WHICH ENABLED THEM TO DISTINGUISH THEMSELVES NOT ONLY AS HONEST AND HARD-WORKING EMPLOYEES BUT AS SCIENTISTS, ACADEMICS, ARTISTS, ENTERPRENEURS AND EVEN POLITICIANS. THIS IS ALSO TRUE OF MANY GREEK STUDENTS WHO GO ABROAD FOR STUDIES AND EVENTUALLY STAY ON TO MAKE A CAREER IN THOSE COUNTRIES. THUS, THE GREEK IN HIS OWN COUNTRY, MAY BE MEDIOCRE, OR EVEN INEFFECTIVE IN THE PUBLIC SECTOR OR IN INEFFICIENT ENTERPRISES OF THE PRIVATE SECTOR. BUT, IN ENTERPRISES WITH GOOD ORGANIZATION, PROPER POLICIES, CLEAR CORPORATE OBJECTIVES AND DEDICATED AND SENSITIVE MANAGEMENT, NOT ONLY DOES THE GREEK WORKER PERFORM BETTER THAT SATISFACTORY BUT ADDS HIS NATURAL INTELLIGENCE, INITIATIVE, VITALITY AND LOYALTY PLUS SOMETHING ELSE: THE UNTRANSLATEABLE GREEK QUALITY OF "FILOTIMO" (PRIDE TO GO THE EXTRA MILE AS ONE MIGHT SAY, TO DO "ONE BETTER", NOT TO

BE LEFT BEHIND -THESE ARE JUST FRACTIONS OF THE MEANING OF THAT WORD-).

A <u>SUMMARY</u> OF THE POSITIVE AND THE NEGATIVE ELEMENTS WHICH FORM THE BALANCE SHEET OF THE GREEK LABOUR RELATIONS SCENE IS THE FOLLOWING:

ON <u>THE PLUS SIDE:</u> THERE IS THE COMPREHENSIVE REVISION OF THINKING ON THE PART OF GOVERNMENT AND TRADE UNIONS, WHICH LEADS TO MORE REALISTIC APPROACHES TO THE ECONOMIC PROBLEM. AS EXAMPLES, I WILL MENTION THE FULL AWARNESS OF THE NEED TO REFORM AND MODERNIZE, AND TO IMPROVE COMPETITIVENESS, AS WELL AS THE ACCEPTANCE OF THE LINKAGE OF COMPENSATION TO PRODUCTIVITY AND PERFORMANCE.

FURTHERMORE, THE REDUCTION IN GOVERNMENT INTERVENTIONISM, IF IMPLEMENTED, SHOULD ADD UP ON THE PLUS SIDE OF THE LEDGER.

<u>ON THE NEGATIVE SIDE,</u> THE POINTS WHICH REALLY ACT AS CONSTRAINS HOLDING BACK A DYNAMIC EFFORT FOR INDUSTRIAL RESTRUCTURING ARE:

(A) A GENERAL CONCEPT, OF THE "OLD SCHOOL TYPE" SURELY NOT RESPONDING TO THE NEW CONDITIONS. A CONCEPT TRANSCENDING BOTH THE LAWS AND THE PRACTICE, THAT THE WORKERS ARE THE WEAKER SIDE AND THUS IN NEED OF SPECIAL PROTECTION. THE PRACTICAL

RESULT OF COURCE BEING THE UNEQUAL TREATMENT OF THE TWO SIDES.

(B) THE LACK OF SUBSTANTIVE DIALOGUE WITH THE TRADE-UNION LEADERSHIP. WHICH CAN BE SEEN IN CONJUNCTION WITH THE CONTINUED POLITICAL PARTY INTERVENTION ON THE UNION MOVEMENT.

(C) THE HESITATION OF PUBLIC AUTHORITIES TO ENFORCE THE LAWS, WHICH UNDOUBTEDLY EXIST, WHEN THE ISSUE IS TO PROTECT THE RIGHT TO WORK AND NOT THE RIGHT TO STRIKE.

(D) A SERIOUS PROBLEM IS THE SYSTEM PREVAILING IN COLLECTIVE TERMINATIONS (LAY-OFFS) WHERE, IN PRACTICE, ENTERPRISES ARE NOT PERMITTED TO ADJUST THE NUMBER OF THEIR WORKFORCE TO THEIR PRODUCTION AND BUSINESS NEEDS.

A SPECIAL POINT SHOULD BE MADE REGARDING THE BASIC LAW REGULATING COLLECTIVE BARGAINING AND RESOLUTION OF INDUSTRIAL DISPUTES. THE PERTINENT LAW IS PRESENTLY UNDER REVIEW AND THERE IS IN FACT AN ONGOING DIALOGUE BETWEEN THE SOCIAL PARTNERS AND THE MINISTRY OF LABOUR FOR THE PURPOSE OF SHAPING THE DRAFT OF THE NEW LAW. I AM SORRY THAT, I AM NOT YET IN A POSITION TO INFORM YOU AS TO WHICH SIDE THE EVENTUAL TEXT WILL LEAN, WHETHER IT WILL BE THAT OF "DEVELOPMENT" OR THAT OF IDEOLOGY.

HOWEVER, WE BELIEVE THAT THE IMPORTANCE OF THIS

BASIC LAW FOR ECONOMIC DEVELOPMENT AND FOR THE CREATION OF AN "INVESTMENT CLIMATE" WILL PROBABLY LEAD ALL SIDES TO DEMONSTRATE RESPONSIBILITY AND CAUTIOUSNESS.

IN CONCLUSION, I WOULD LIKE TO LEAVE WITH YOU AN OVERALL IMPRESSION, WHICH I BELIEVE GIVES THE TONE, THE COLOUR, TO OUR CURRENT SOCIAL ENVIRUNMENT. DESPITE THE DIFFERENCES THAT CERTAINLY EXIST BETWEEN THE POLITICAL PARTIES AND THE IDEOLOGIES THEY REFLECT; OR THE DIFFERENCES BETWEEN EMPLOYERS AND EMPLOYEES, THERE ARE CERTAIN PARAMETERS EMERGING, ON WHICH, THERE SEEMS TO BE CONCENSUS THAT THEY ARE ESSENTIAL FOR OUR ECONOMY AND SOCIETY IF IT IS TO FACE SUCCESSFULLY THE CHALLENGES LYING AHEAD!

A MINIMUM OF CONCENSUS EXIST ON:

- THE NEED TO MOBILIZE **ALL** OUR SOCIAL RESOURCES.
- THE NEED FOR CONTINUOUS TRAINING OF OUR WORKFORCE AND FOR EMPHASIS ON EDUCATION.
- THE NEED FOR LESS INTERVENTION BY THE STATE AND MORE CONSIDENCE IN THE SOCIAL DIALOGUE.

IT IS ON THESE FOUNDATIONS THAT A NEW MODEL OF LABOUR RELATIONS WHICH IS ALREADY EMERGING MAY BE FULLY DEVELOPED.

WE ARE HOPEFUL THAT THE DYNAMIC IMPACT OF OUR LINK TO THE EUROPEAN COMMUNITIES WILL ACCELERATE THE TEMPO OF THIS DEVELOPMENT.

THANK YOU.

INSTITUTIONAL INVESTMENT IN GREECE AND OTHER MEDITERRANEAN COUNTRIES: AN OVERVIEW

William Richards
Executive Director
Sun Life Investment Management

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It is an honour for me to be here today in the cradle of European civilisation and to speak to such an illustrious audience on the topic of investment opportunities in Greece and in the Mediterranean region from the institutional investor's point of view.

In my presentation I shall endeavour to put Greece and the Mediterranean region into an international context. Then I shall comment on certain capital market themes and this will lead into the questions of the weighting of these areas in our portfolios as well as our general decision-making process.

Over the past few years we have come a long way in raising the entrepreneurial spirits in Europe. Factors in the renaissance of the European stock markets include:

- Entrepreneurial spirit
- Budget deficits cut
- Marginal production units removed
- Excess capacity eliminated
- Share incentive schemes
- Funded pensions

These factors may be summarised as follows:

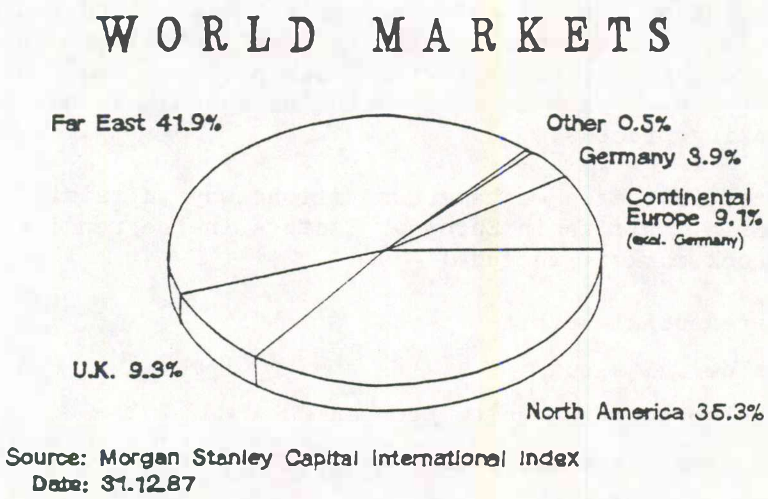
- A rekindling of the profit mentality
- Governments committed to improving efficiency (eg cutting budget deficits)
- Share incentive schemes
- Rationalisation measures, including the shedding of labour which was previously very difficult to implement
- More responsible attitude of trade unions
- Removal of marginal production and elimination of excess capacity, obsolete plant and machinery
- Some reduction in interest rates, made possible by strong government
- Efforts to be more competitive in international markets and to increase value added of the product mix

- Internationalisation of stock markets, spurred on by US pension fund interest
- Move towards funded pensions in Europe

The resulting upsurge in profitability led to the phenomenon of bringing GDP to the markets. Europe is certainly no longer a minnow in stock market terms. Its economic strength is well represented in the bourses and will continue to grow as countries take measures to cut public sector deficits, perhaps through privatisation.

At Sun Life we believe strongly in the globalisation of stock markets.

WORLD MARKETS



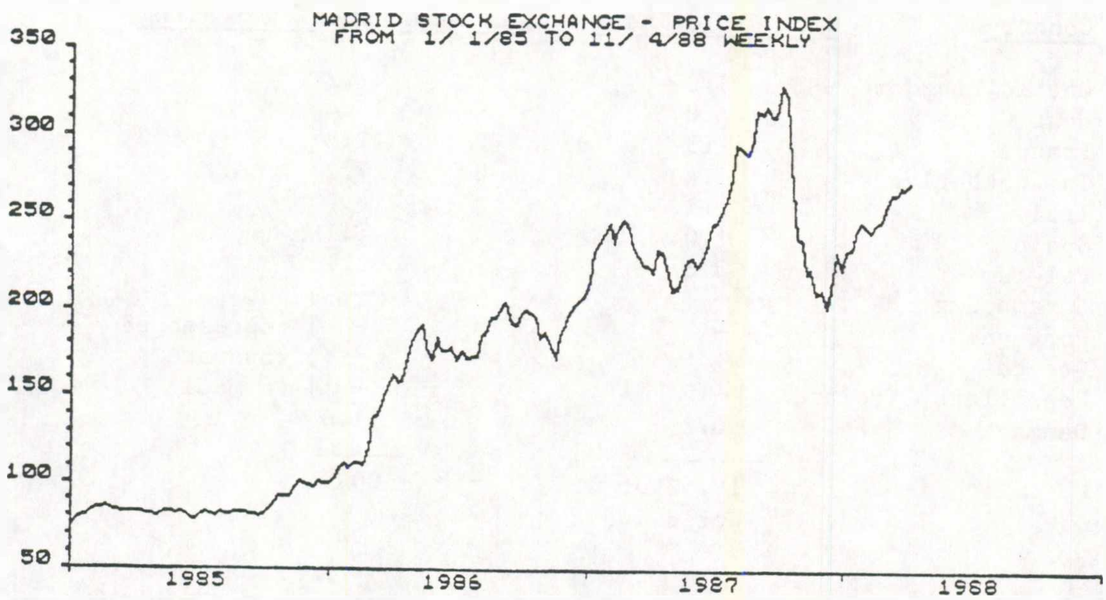
No global investor can afford to miss out on investment opportunities in Europe and, increasingly, Mediterranean Europe where growth rates are faster than in the traditional heartland of northern Europe. For example, from a miniscule weighting in the Morgan Stanley Capital International index a few years ago, Spain now accounts for some 5% of the European Community index. Further examples are Italy with 8.7% and France with 11.8%, although the United Kingdom accounts for nearly 50%!

Percentage Weightings in Common Market Growth

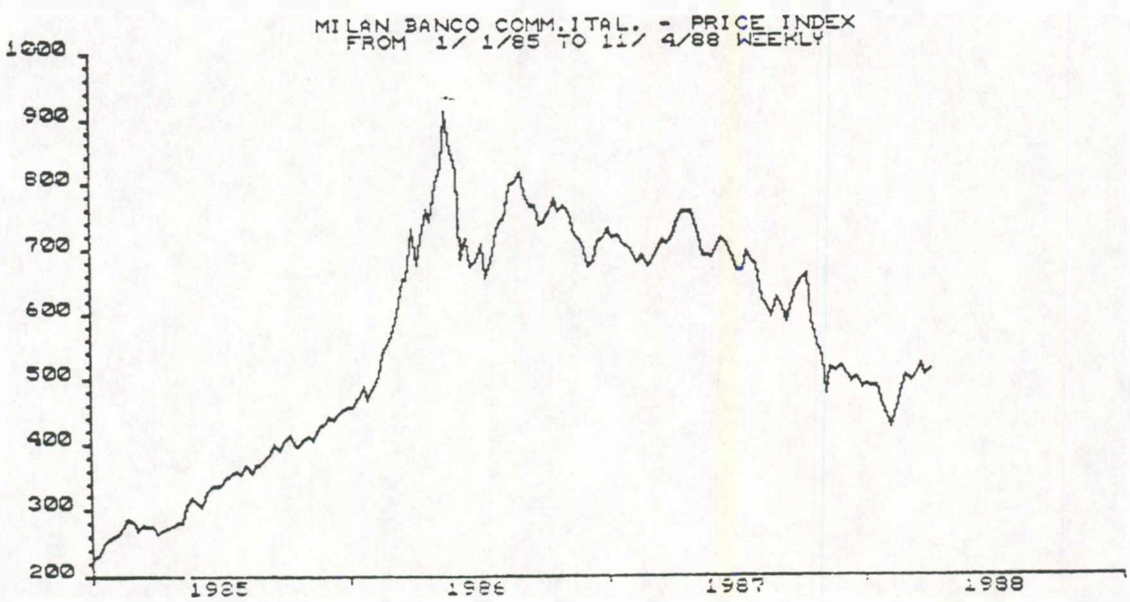
Country	% Weighting in MSCI World Index	% Weighting in EC Fund assuming index weighting	
United Kingdom	9.3	47.7	
West Germany	3.0	15.4	
France	2.3	11.8	
The Netherlands	1.4	7.2	
Italy	1.7	8.7	
Spain	1.0	5.1	
Belgium	0.6	3.1	
Luxembourg	-	-	] not
Portugal	-	-	] represented
Greece	-	-	] separately
Republic of Ireland	-	-	] in MSCI
Denmark	0.2	1.0	
	19.5% of World Index	100%	

Up till now Greece and Portugal have not been represented in this index ... but for how long? How long will it take before these countries follow? This would surely be the catalyst to spark off the attention and potential in _your_ country.

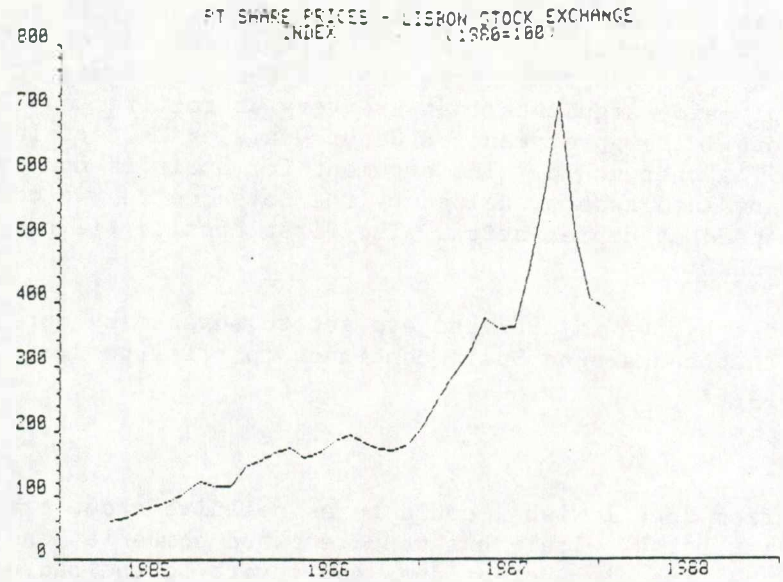
STOCK MARKET PERFORMANCE : SPAIN



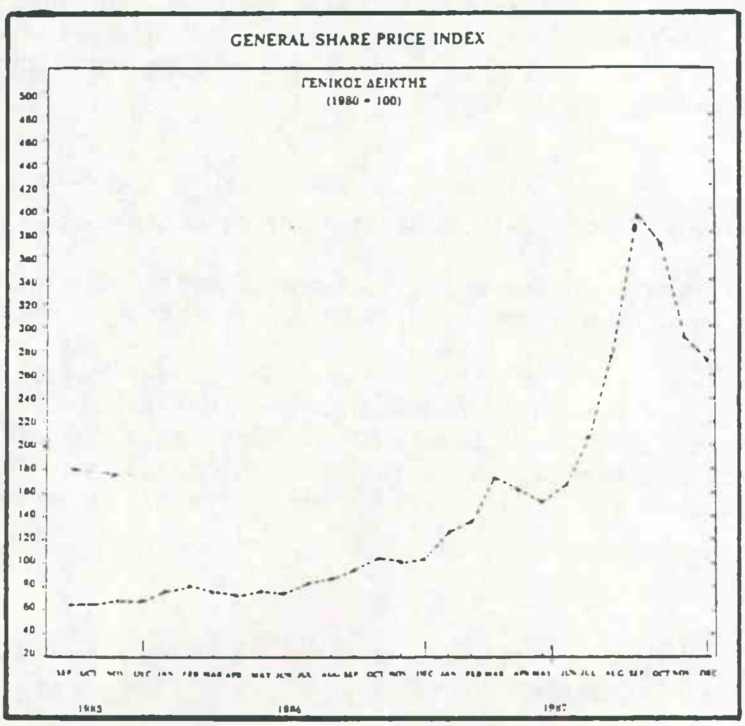
STOCK MARKET PERFORMANCE : ITALY



STOCK MARKET PERFORMANCE : PORTUGAL



STOCK MARKET PERFORMANCE : GREECE



I should now like to talk about the stock market performance and outlook for Spain, Italy, Portugal and Greece.

Spain

The Spanish "bolsa" has been one of the world's success stories in recent years and this buoyancy has continued through the first quarter of 1988. Whether the initial catalyst was the entry into the European Community, Spain does offer supply-side arguments that are very attractive to international investors. The government of Senor Gonzalez is certainly laisser-faire in the Thatcher mould. The argument for Spain is now moving into the area of undervalued assets, helped by the Boyes decree which allows companies to speed up depreciation. The first hostile bid has emerged - Torras for EBRO!

Corporate earnings rose by 30% in 1987 and are set to advance by more than 12% in 1988. Given that background Spain continues to offer good investment opportunities.

Italy

Having just arrived from Rome I wish I could be as positive about the outlook for the Italian borsa. Italy has many renowned companies and it is to be hoped that the financial set-up does not revert to the bad old ways. Recent developments concerning Ferruzzi, Pirelli and Standa, for example, have left small shareholders out in the cold. Outside of market rumours the major preoccupation is with the finances of the public sector and complying with EC directives.

The budget deficit forecast is now 122 trillion lira for 1988, up from 113.7 trillion lira in 1987, over 11% of GDP. Can the new coalition of de Mita come to grips with this imbalance? Earnings momentum remains intact but if bond yields do not fall a sustained rally in equities is not likely. However, Italy does, in principle, offer exciting opportunities and we monitor the situation very closely.

Portugal

I hope that I can include Portugal in a Mediterranean context.

Fuelled by foreign investors the emerging Portuguese market did well up to 19 October but after that it plummeted to two-thirds of the October peak.

Banco Totta e Acores index rose by 450% in the first 10 months of 1987. However, confidence may be returning and new issues such as Corticleira and Amorin have captured investors' imagination. The Social Democrat government may introduce new measures to rebuild confidence, such as exempting share deals from stamp duty, and to encourage private asset management companies.

Greece

I shall restrict myself to a few general comments on the outlook before developing the main capital market themes and opportunities.

For the international investor the main risk is associated with lack of liquidity due to the limited supply of shares. Events of the past 12 months have shown this clearly, leading to sudden and sharp price movements. Any move by a large institution can drive up share prices, as happened up to the crash of 19 October. On the other hand, potential rewards are there due to undervaluations and low levels of share ownership. It is these factors which prompt us to include Greece in the emerging markets context. It has first-class companies in many sectors such as textiles and we are willing to become involved. As 1992 looms on the horizon Greece should integrate fully in the EC financial market.

The 1992 deadline for establishing the EC internal market is a major talking point and is potentially one of the most exciting eras in recent European history - the creation of a single market in Europe of 320m people, a market that will be larger than the USA. In addition, impetus is being given to the relationship between EFTA and the EC and already a number of companies have begun to position themselves, for example ASEA of Sweden and Brown Boveri of Switzerland.

GDP/GNP - 1985 (US$)

Austria	66.1	Belgium	79.1
Finland	54.0	Denmark	57.9
Iceland	2.7	France	510.3
Norway	57.9	Germany	625.0
Sweden	100.2	Greece	32.8
Switzerland	92.7	Ireland	18.2
		Italy	358.7
	373.6	Luxembourg	3.6
		Netherlands	125.0
		Portugal	20.7
		Spain	164.2
		UK	449.7
			2445.2

There is considerable interest on behalf of international investors in those sectors that are seeking to benefit from the rationalisation and restructuring of Europe in the build-up to 1992 and those that will gain most from a liberated market. This will be an ongoing theme and keep interest in European stock markets at a high level.

Within our international strategy there is every likelihood that we will place a growing emphasis on the emerging markets such as Greece, Spain, Italy and Portugal where the benefits of corporate rationalisation and restructuring are still coming through. These developing markets with their exciting growth prospects complement the maturer aspects of major European markets. The risk reward ratio in emerging markets, which is higher than in major Europe, will be constantly and carefully monitored.

The major caveat is the liquidity in these markets and the fact that the bourses are very much at the whim of the international investor and domestic support is negligible. However, we are encouraged by the moves of several governments to promote equity investment, which is a slow but sure way of giving depth to the market. This in turn will encourage further foreign participation.

Next a few words about our approach and strategy towards European investment.

Sun Life believes strongly in the internationalisation of markets and that this development will continue over the coming years.

Let us examine how this works in practice, using continental Europe as an example. The major economies of Europe, ie Germany, Switzerland, the Netherlands and France, have been characterised in the past year by slowing economic growth, currencies that have strengthened against the US dollar and export sectors that have been pressurised by that strength. Economic fears on an international level have been the major contributors to a lacklustre performance by Europe's major bourses. However, the economies of other European nations (Scandinavia, Belgium, Italy, Spain, Greece and Portugal) have exhibited more growth and dynamism, with Spain in particular performing well against a background of increased foreign investment, a developing internal infrastructure, growing demand and improving economic performance. Companies in some of these countries are still experiencing the benefits of rationalisation and reconstruction, which have only during the past year begun to show in financial results. Growth in earnings has exceeded that of stocks in major European markets. However, higher rewards entail higher risks.

Despite the exceptional returns generated by the minor markets, Sun Life adhered to - and still adheres to - the 70:30 policy. This policy specifies that a minimum of 70% of all holdings must be kept in liquid stocks and liquid markets. In addition, we had become increasingly cautious about the minor markets during the summer, reasoning that precipitate rises would be followed by swift falls, and had already begun to take profits. Hence, on 19 October we were considerably better placed than other institutions that had not been as prudent and our presence in liquid markets and stocks afforded us maximum flexibility to respond to events.

We show below the main criteria underlying our stock selection process using the continental European market as an illustration.

CRITERIA FOR SELECTION OF CONTINENTAL EUROPEAN SHARES

MAJOR FACTORS INVOLVED IN SELECTION PROCESS	BROAD CATEGORIES		
	QUALITY	CYCLICAL	NICHE
1. Earnings Improvement - current	X		
2. Earnings Improvement - forecast	X	X	
3. Dividend growth			
4. Technological excellence	X		X
5. Management openess	X	X	X
6. Excellent management	X		X
7. Normal P/E		X	
8. Average relative performance		X	
9. Good marketability	X	X	
10. Reliable shareholder structure			

REQUIREMENTS FOR SELECTION

(i) QUALITY - Factors marked x(6) plus at least two others - minimum 6
(ii) CYCLICAL - Factors marked x(5) plus at least one other - minimum 6
(iii) NICHE - Factors marked x(3) plus at least one other - minimum 4

Our underlying strategy of:

1 concentrating on strong/liquid stock markets around the world

2 maintaining a high proportion (70% to 80%) in good-quality/liquid stocks

3 searching for latent potential within smaller company growth stocks in emerging markets

is applied to all the major geographic groupings of world stock markets.

I have endeavoured to put Greece and Mediterranean Europe in an international context. There are many exciting possibilities in the new, emerging markets, especially in the run-up to 1992.

We intend to take advantage of these and hope that you will help our efforts by liberalising your capital markets and easing your exchange control restrictions.

EVOLUTION IN WORLD BANKING

Hans H Angermueller
Vice Chairman
Citicorp/Citibank

THE EVOLUTION TO THE WORLD BANKING

by

Hans H. Angermueller

Vice Chairman

CITICORP/CITIBANK

An Address before the Euromoney Conference

"Greece in the World Economic Community"

Athens, Greece

April 21, 1988

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In Europe these days, the number 92 looms larger and larger for today's bankers. That year is the start of European banking. Similarly, in the United States, the number 91 has a great significance. That year is de facto the start of nationwide banking. Bankers in both areas are already planning to take advantage of the opportunities that larger markets will bring.

My purpose here today is simple. It is to suggest that the trends toward European banking and nationwide banking in the U.S. are but part of a larger trend - an evolution to world banking - and that world banking will be as different from national banking as Athens, Greece is from Athens, Georgia.

I

The forces propelling us toward world banking are strong. The first is the growing intergration of world economy. As we all know, the world is basically composed of about 160 nations, about two dozen of which constitute the OECD nations or what might be called the "first world". Then there are about a dozen or so developed countries who operate centrally planned economies or what might be called the "second world". The remaining 125 developing countries who operate their economies from highly free-market orientation to very centrally planned are what is generally called the "third world".

The aggregate value of the goods and services produced by those 160 countries that comprise the first, second and third worlds currently runs at about 12 to 13 trillion dollars per year and is growing at about 2 to 3% per year in real terms. The earnings that result from that vast and increasing production of a surprising $2.5 trillion/year. Those retained earnings of $2.5 trillion/year constitute the world's annual savings. They are the source or fuel for the world's growth.

Most of the world's income and savings is concentrated in the "first world". About 75% of the world's production, consumption, savings and trade occur in the "first world", even though it has only about 20% of the world's population. Increasingly, this first world is a single marketplace, whether for cars, computers or capital. National borders mean less and less; the quality and cost of a product or service mean more and more. Consequently, companies cannot ignore either consumers or competitors in other lands. Nor can governments or participants in financial markets. For proof, one need only look at the market's anticipation of and reaction to the U.S. trade deficit each month or to calculations of how much Japanese demand there will be at each auction of U.S. Treasury bills.

A common theme running through the first world is an increased reliance on markets to propel economic growth. Policy changes have included reductions in marginal tax rates, the privatization of state owned companies and the reform of domestic financial regulations - a subject to which I will return later. The results have been dramatic: six uninterrupted years of prosperity, a marked decline in inflation rates,a substantial growth in employment in each of the major industrial countries, and a substantial increase in the efficiency of business corporations.

This economic transformation has not been easy. It has required a basic restructuring of production and distribution and a basic restructuring of the way corporations are owned, managed and financed. The hostile takeover, the leveraged buyout, two tier wage scales, and junk bonds grab the headlines. But the result has been an increase in productivity, and a drive to keep productivity growing, if only to pay down the vast increase in debt that has usually accompanied restructuring.

Before turning to the implications of this increasing economic integration for world banking, let me digress a moment to discuss the challenges that this record of capitalist prosperity poses for the second and third worlds.

The "second world," the developed, centrally planned economies dominated by Russia, was seriously considered in the late 1940s and early 1950s (when I began my professional life) to be that world which was likely to dominate the other two worlds. Central planning, it was assumed, was the system which in the long run would provide the solution to the better generation, and more equal distribution, of the world's wealth. In the early post-war period, Russia, China, the Eastern Block all seemed to have found the right solution. Many of the then recently decolonized nations of Africa and Asia saw enormous attraction in the centrally planned economy. Indeed, in those early post-war years, countries like England, France, Italy and even Germany flirted with those ideas. Today, however, the "second world" seems to be stagnating, and its leaders seem tobe looking at free market solutions to revitalize their economies. How they can do so while preserving their type of political system poses a grave challenge to these regimes, and, by implication, a foreign policy issue of great significance to the governments of the first world.

The "third world" also faces the challenge of responding to the capitalist successes of the first world. This third worldcontains, by far, the largest number of countries, some 125, and also has the largest variety of economic systems, the most diverse cultures, and the widest range in standards of living. It is the world which has grown accustomed to supplementing its own savings by attracting savings from the first world. Those local and imported savings were used - with a variety of degrees of success - for productive local investment and improvements in standards of living. In the early post-war years, the imported savings were preponderantly supplied by the multilateral development agencies like the World Bank and by multinational investor corporations. In the oil-shock years from 1973 to 1980, the imported savings were predominantly supplied by private commercial banks like Citibank.

For about half of the "third world" nations - 60 to be exact - servicing their external borrowings has proven difficult, but do-able. For the other 65 "third world" countries crisis has followed crisis involving extending maturities, altering repayment schedules, reducing interest and borrowing more money. The reasons why these 65 countries have stumbled while the other 60 haven't are as many and as varied as the countries themselves, but three common themes seem to weave themselves into the economies of these 65 countries:

- The economies are largely government dominated;
- The economies discourage foreign equity investment, allegedly to prevent "foreign domination", but in reality to protect local enterprises - whether public or private - from competition; and
- The economies, through overvalued exchange rates, high taxation, and controls on investment and savings foster the export of local savings to the "first world".

However, politically attractive these policies may be to the 65 troubled third world countries, they will not succeed in attracting new capital. Yet new capital will be the commodity that all three worlds (first, second and third) will be competing for as the advantages of cheap labor and government subsidies give way to private enterprise and productive efficiency.

As the supply of the world's capital is limited, but as the demand for it inceases, it seems to me that the "third world" countries must play the economic game essentially by the same rules as have the more successful "first world" countries. Debt repudiation, confrontation, nationalization and isolation are not, in my judgment, the way to attract new capital.

II

Let me now turn to the second force driving us toward world banking. That force is technology. Advances in technology are changing the way capital is raised, distributed, and invested - and therefore changing the way in which banks must operate if they are to remain competitive.

For centuries banks were the institutions which received savings, distributed them, and invested them. They were the custodians of capital because they had a unique, and therefore extremely valuable store of financial information. They knew the source, the quantity and the quality of savers who are the ultimate providers of capital - whether those savers were households, businesses, or governments. That unique store of financial information kept bankers alive, flourishing and profitable for hunderds of years.

However, as information technology developed - particularly in the last 20 years - the costs of acquiring, processing and transmitting information, including financial information, dropped enormously. Today virtually anyone can acquire and use the information that used to be available only to the bankers.

And today virtually everyone has. In the U.S. some 200 professional money managers manage pension, mutual and money market funds that have an aggregate value of about $2 trillion. That is about two thirds as much as the total assets of the U.S. commercial banking system. And, the differences in operating efficiencies between banks and money managers are very marked. One well-known U.S. pension fund manager employs 20 professionals and a high-powered computer to run a $10 billion pension fund. A $10 billion commercial bank, on the other hand, employs between 5000 to 7000 people. A professional money manager can quite profitably operate portfolio investments at a cost or spread of 25 basis points. A bank operating itsbusiness encounters a pre-tax cost or spread of 250 basis points - ten times as much.

Information technology has also fostered the development of the so-called "derivative instruments" - the puts, calls, options, indexes, futures and the like - that are designed to segregate the rate, liquidity, exchange and credit risks that used to have to be bundled together in the single bank loan or bond issue.

I therefore believe that the long-term tide is running worldwide against the traditional <u>banking function</u> - that is to say, deposit taking and lending - but not necessarily against <u>bankers</u>. It would seem to me that bankers are moving away from the unique relationship (and, as I said earlier, information) links on which they so long depended and profited and more toward the impersonal markets, bitter competition, and shorter product cycles that are part of the process of change.

Thinner spreads from traditional relationship borrowers is simply incompatible with a declining deposit base, more expensive equity and the higher capital demand by regulator. If bankers are to survive, they will have to change.

III

The forces of change that I have described, namely, the integration of the world economy and the advances in financial information technology, are driving the evolution from traditional banking to world banking. What will this new world of banking look like?

It will of course be global. Banks will increasingly operate throughout the first world, and, to the extent that the second and third worlds respond to the capitalist challenges of the first, tomorrow's global banks will also operate in the second and third worlds as well. In the coming years, banks will have to position themselves for the opening of the European and U.S. markets, and Japan will have to consider opening its doors more widely to foreign banking institutions, if its banks are to retain access to foreign banking markets.

More significantly, world banking will differ from traditional banking. The global bank will not simply make loans and hold them on its balance sheet. Nor will the global bank simply underwrite securities and place them with investors. Instead, the global bank will be a financial engineer. It will originate financial instruments that meet the needs of issuers. The global bank will then reconfigure the instrument, via credit guarantees, swaps and other derivative instruments that I mentioned earlier, to meet the needs of investors. In this manner the instrument sold to investors will differ markedly from the instrument purchases from the issuer.

The advent of financial engineering blurs the lines between traditional forms of financial intermediation. Investment banking and commercial banking, long separated by law or custom in many countries, are now being united. In the United Kingdom, there was the Big Bang; in Canada, the Little Bang; and in France, le petit bang. In the United States Congress isconsidering the repeal of the Glass-Steagall Act, and in Japan, the Ministry of Finance is reforming Article 65. This would bring the financial systems in these countries much closer to the universal banking system that is the norm in most of Europe.

Similarly, insurance is blending into banking. Whether on the asset side or the liability side, insurance has great similarity with banking, and there is an increasing amount of cross fertilization among banks and insurance companies. In the United States many of the leading insurance companies own investment banks, and in the United Kingdom, the leading banks have insurance subsidiaries. More integration of banking and insurance stands ahead, for both activities are fundamentally the same - the pricing and management of risk.

To prosper in the age of world banking, a bank will therefore have to understand how to price and manage risk - not just credit risk, but also interest rate risk, exchange rate risk and liquidity risk. And, since the global bank will be heavily involved distributing and dealing in the instruments it creates, the global bank must understand how to price and manage the risks inherent in the clearing, settlement, servicing and custody of those instruments, even if they do not decide to perform all of those functions for themselves.

And, today's banks will have to do so quickly, if they are to make the transition to world banking. Technology continues to advance at a rapid pace, and banks must keep pace, if they are not to become obsolete. Only those banks that do keep pace will be able to survive when 91 and 92 arrive.