

Παρέμβαση του Διοικητή της Τράπεζας της Ελλάδος κ.
Α. Χαλικιά στην Επιτροπή των Διοικητών των Κεντρικών
Τραπεζών της ΕΟΚ στη συνεδρίαση της 12.11.1985,

On October 11, 1985, the Greek authorities announced a package of measures aimed at stabilizing the economy, in particular, at attaining a much faster deceleration of inflation and at drastically reducing the current account deficit.

I should perhaps remind that the difficulties facing the Greek economy stem to a very large extent from structural imbalances. The industrial base of the country is weak and accession to the EEC has increased the vulnerability of the Greek manufacturing industry. At the same time, the worldwide shipping crisis has had serious adverse effects on the balance of payments. If capital flows are included, the decline in foreign exchange receipts from shipping exceeds 1 billion U.S. dollars per annum.

But the difficulties facing the Greek economy stem also -to a large extent- from inappropriate economic policies. Not only has structural adjustment been delayed and inadequate, but imbalances have been accentuated by highly expansionary policies since the mid-70s. Especially in 1981, an election year, public policies led to a doubling of the public deficit to about 14.5 percent of GDP, a current account deficit of 6.5 percent of GDP and an inflation rate of nearly 25 percent. In the following two years, 1982 and 1983, some efforts were made, which resulted in a modest reduction in the fiscal and the external deficits. But the improvements were largely reversed in 1984 and 1985.

In the first eight months of 1985, the current account deficit was 55 percent higher than in the corresponding period of 1984, reaching the level of \$ 2.1 billion. The deterioration of the balance of payments continued in September and the first part of October, a fact that forced the authorities to decide on October

11 the devaluation of the drachma. There is evidence that market expectations of a devaluation of the drachma had contributed to the deterioration of the balance of payments. The current account deficit for 1985 may reach \$ 3 billion or 8.5 percent of GDP. Over the previous three years, this deficit ranged between 4.9 percent and 6.4 percent of GDP.

These unfavourable developments in the current account partly reflect a considerable loss of competitiveness and partly are a consequence of expansionary fiscal and monetary policies. The high PSBR -estimated at 18.5 percent of GDP this year- and its financing largely through the banking system have undermined the effectiveness of monetary policy, a fact which is reflected in the growth of monetary aggregates.

In order to tackle these problems, the economic stabilization program includes measures aimed at improving competitiveness, curtailing the public sector deficit, and restraining money and credit expansion.

Briefly, the measures that were decided are the following :

1. A devaluation of the drachma by 15 percent.
2. An advance deposit scheme on imports. The scheme requires importers to maintain a noninterest bearing deposit with the Bank of Greece for a period of six months, amounting to either 40 percent or 80 percent of the value of certain categories of imports.
3. A modification of the wage indexation system. Under the new system, wages and salaries will be adjusted every four months on the basis of an official inflation rate target for the following four-month period, adjusted to exclude imported inflation. The wage and salary adjustments thus determined will be the maximum legally permissible in 1986 and 1987. It is expected that the new wage

indexation system will result in a decline of real wages in 1986 by at least 5 percent.

4. Price increases for agricultural commodities will be maintained below the anticipated rate of inflation.

5. As regards fiscal policy, the Government aims at reducing the PSBR by 4 percentage points of GDP in 1986. A further reduction -not yet defined- is planned for the following years. Real government consumption, excluding debt servicing, and real public investment will be reduced. Tax revenues will rise as a result of :
(a) A one year surtax, ranging from 3 to 10 percent, on profits and incomes of the self-employed, (b) New legislation to make tax evasion a criminal offence, (c) Gradual elimination of tax exemptions and (d) Stricter enforcement of taxation on agricultural incomes. A considerable reduction of the borrowing requirements of public enterprises by over 20 percent in money terms is planned, mainly through an adjustment of the prices of goods and services they supply so as to reflect operational costs, and by imposing strict credit controls.

6. With respect to monetary policy, the aim is to have it play a supporting role in the disinflation process. In the first place, the reduction of the public sector deficit, together with an increase of sales of treasury bills to the nonbank private sector, is expected to lead to a tightening of monetary conditions. Although no monetary and credit targets have been set yet for 1986, the aim is to take all appropriate measures to bring domestic credit expansion progressively down. To this end, the Bank of Greece intends to employ a flexible monetary policy, especially as regards interest rates. Already, some measures have been taken. A minimum lending rate was set on short-term bank loans, which is 1 percentage point higher than the rate on savings deposits. This minimum lending rate, which is currently 16 percent,

replaced a number of preferential interest rates that ranged between 12 and 14 percent on loans to the agricultural sector and to small and medium-size firms. In addition, a number of measures have been taken by the Bank of Greece to absorb liquidity of the banking system, amounting to Drs. 35 billion (roughly 10 percent of the projected credit expansion to the private sector in 1985). The deposit requirement on imports would also lead to a decline in liquidity by at least Drs. 50 billion. Finally, the specialized credit institutions were required to withdraw their funds from the inter-bank money market. These measures have already contributed to a rise in the inter-bank market rates, while conditions of crowding out of public agencies are developing, which are expected to force these agencies to borrow less and lead to a rise in interest rates.

In concluding, I would like to say that these measures indicate a determined effort on the part of the Greek Government to tackle the severe problems facing the Greek economy. They amount to abandoning the "gradualist approach" that had been adopted in recent years, with very limited success.

An important feature of the package of measures is that the new incomes policy will eliminate the impact of devaluation on wages and costs. Thus, competitiveness should be maintained. This should help to restore profit margins, especially in the manufacturing sector, and thereby stimulate domestic production and business investment. These measures may not, however, be sufficient to deal with the deep-seated structural problems of the Greek economy. For this reason, the Government has stated its intention to take, before the end of this year, additional measures, aimed at improving the business environment and at promoting productive investment.

The decision to tighten fiscal policy and reduce the PSBR by 4 percentage points of GDP in 1986 is of crucial importance. It represents a very significant step in a difficult adjustment process. In our view, without a substantial reduction of the public sector deficit over the few years, inflation cannot be controlled, nor can the current account deficit be brought down to sustainable levels.