European Monetary Union

and an Analysis of Greece's Economic Efforts

to Meet the Maastricht Criteria

By

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Submitted in Partial Fulfillment of the Requirements
for the Degree of
Master of Arts
in the
Economics
Program

Youngstown State University
March, 2000

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Abstract

"European Monetary Union and an Analysis of Greece's Economic Efforts to Meet the Maastricht Criteria" is a thesis that mainly focuses on how an old European vision became reality.

More specifically the thesis is divided into two main axis. The first is the presentation of Europe's needs for coexistence and unification after WW2, and the illustration of the steps that different European countries took over the years towards the establishment of this unification under the formation of the European Union (EU). The second deals with the creation of the European Monetary Union (EMU) and the attempts by Greece (an EU member) to join the union.

By the end of this analysis every potential reader will have a better understanding of why the creation of EU was so necessary for Europe and more importantly how and why EMU is expected to lead to further unification and power.

Acknowledgements

I would like to thank Dr. Milley for his assistance and support as well as my committee for their encouragement in completing this thesis. I would also like to thank my beloved mother, Anastasia Fasoula, for being my inspiration. Last but not least, I need to dedicate this thesis to the two most important men in my life, my father Georgios Fasoulas, and my fiancé, Nikolaos Vasileiadis, as both are my source of energy and optimism.

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Introduction

The institutions of European Union and European Monetary Union that we all know today were not created overnight. On the contrary they are the results of years of economic programming and struggling that started immediately after World War II. This is the case since the conclusion of the war left Europe in a desperate economic and social situation. There were direct needs for unification and co-existence of the European countries. As we will discuss later on, the creation of a supranational organization that would bring the countries together seemed to be the only solution.

All of the above led to the creation of the first European Communities (European Coal and Steel - European Defense Communities) and others soon followed. As years went by and the communities started to enlarge, a vision of total unification among the member states became reality through the signing of the Maastricht Treaty and the creation of the current European Union and European Monetary Union.

The scope of this thesis is twofold, it will provide an analysis of all the steps that led to European Monetary Union. It also focuses heavily on what the EMU really represents, which is its importance for Europe. Secondly, it will show, in depth analysis of Greece's economic, social and political environment, in combination with the presentation and analysis of the macroeconomic policies used by the Greek government to meet the convergence criteria of EMU.

The Construction of Europe

In May 1945, a crucial chapter of the world's history came to an end, with the conclusion of World War II in Europe. Chaos and destruction were the basic elements of the European setting and it was then when many people realized that nationalism as well as racism should never be allowed to rule again and lead to another war. It was then people realized that France and Germany, the core of both wars, had to learn how to co-exist (Savage, 1970).

These moments of epiphany resulted in the beginning of another era for Europe. An era that is better described by an attempt to create a supranational organization that would make war materially impossible. As the term implies, this supranational organization would stand over the nations and would tie them economically and socially in a way that would be difficult for the nations to turn against each other again. This intriguing goal was the optimal choice for Europe, as its implementation would secure the following: rise against the USSR, gain the support of the USA, grow economically, and in the long run become a superpower itself, avoiding a third World War. So it seemed that only under the guidance of such a supranational organization all states would come together to support each other and united to stand above their problems (Nicoll & Salmon 1994).

All the above came as a confirmation at Victor Hugo's (1848) vision: "*A day will come when all nations on our continent will form a European* *brotherhood …A day will come when we shall see the USA and the US Europe face to face reaching out for each other across the seas.*" (Saisystems, 1999).

A direct result was the Treaty of Dunkirk in 1947. According to this Treaty Britain and France came together against possible German aggression. At the same time the United States was promising support to those threatened by Communist aggression. More specifically, Marshall stated that he was ready to offer economic aid to Europe, but only if the European countries cooperated towards unification and coexistence (Savage, 1970).

European Communities

European Coal and Steel - European Defense Community

In May 1950 a speech inspired by Jean Monnet and Robert Schuman proposed that France, Germany and every other European country wishing to join them, should pool their coal and steel resources together. In this way the basic cause of the constant ownership arguments between France and Germany would be eliminated. Therefore, a common path of collaboration in resources was proposed that would lead to a win–win situation as every participant was to be benefited. (Nicoll & Salmon, 1994). This collaboration took the form of a community and it was the first European Community ever created, the European Coal and Steel Community (ECSC). The establishment of this community occurred in 1951-1952 after the signing of the Treaty of Paris. According to this Treaty, the Six (Italy, Western Germany, France, Belgium, Netherlands and

Luxembourg) decided to collaborate for the common good. As a result this supranational organization (ECSC) was now in charge of coal and steel instead of the individual nations. It had high authority on making decisions about production, labor status, and other problems (Keesing, 1975; Kerr, 1983).

One step further towards unification was the creation of the European Defense Community in 1950-1951 (EDC). The Six signed an agreement in Paris and the goal of this community was to have a common army, thus creating one defense for the whole. Both Communities started to work in 1952, but in 1954 France declined the whole idea of EDC afraid it would have to give up too much sovereignty. This was the end of the EDC (Nicoll & Salmon, 1994).

European Economic Community-Euratom

The Six met later in Messina where plans for one market and a common effort to develop nuclear energy started. A direct consequence of this meeting was the signing of the Treaty of Rome in 1957. The European Economic Community and Euratom were created. Britain chose to stay out of the agreement (Savage, 1970; Vanthour, 1998).

To achieve the implementation of EEC and Euratom a timetable was constructed. Based on this time table short term goals were set in a chronological order so as to result in the long run the creation of a common market. These short-term goals were aiming towards free trade among members, customs union (common external tariff), and common market (free mobility of factors of production). The implementation of the EEC beat the deadlines and by 1968 was successfully carried out in most aspects. Although Euratom started as a very promising goal, it was boycotted later on by France. Conflicts rose over project allocation and France felt that since it was a nuclear power of its own, it should be the leader of Euratom and enjoy more benefits. France was against the supranational characteristic of Euratom. This attitude led to conflicts resulting in the fall of Euratom in 1962 (Nicoll & Salmon, 1994).

Single European Act: A New Phase for the Community

From that point in time and on, France continued to boycott the Community's institutions as well as attempts of EC's for further enlargement. In 1962, as well as at 1967, Denmark, Ireland, and UK attempted to enter the Community. These attempts were not successful as the Six could not reach an agreement because of France (Nicoll & Salmon, 1994).

In 1966, the Luxembourg Compromise took place. The Six decided that unanimity would no longer be the vote-passing requirement unless very important interests were at stake. This was a measure that the Community took against France's aggressive behavior. The above scenario led to a crisis in France. President De Gaulle was forced to resign in April 1969 as his beliefs were not compatible with those of the Community's. DeGaulle's successor, Pompidou, made clear from the beginning of his career that France would no longer object to every Community attempt for enlargement and that France would no longer stand against a possible UK's accession (Nicoll & Salmon, 1994).

The Community entered a new mature phase starting in 1969 with the Hague Summit. At this meeting the EC's heads of states started to talk about deepening (strengthening of institutions and policies), widening (enlargement) and completion of Common Agricultural policy. Also, it was then that discussions about the "future" European Monetary Union started. Finally, in 1972 part of the widening discussions and agreements were implemented as Denmark, Ireland, Norway, and UK were finally accepted, resulting in the first enlargement of the European Community. However, in September of 1972, Norway decided to withdraw its membership (Keesing, 1975; Nicoll & Salmon, 1994).

During the 70's, the economic status of Europe was not healthy as two consecutive oil-crisis led the Community to stagflation. Stagflation, stagnation (low demand, low growth) and inflation (increase in prices) occurred leading the Community to a dead end. Problems arose as members started to focus on national interests and not in supranational ones. To face that problem the foreign ministers of Germany and Italy, Gengher and Colombo, came up with the idea of deeper integration and more specifically they supported for the first time the idea of European Union (EU). As a result in June of 1983 the Solemn Declaration on European Union was signed in Stuttgart. Meanwhile, Greece managed to become a member of the Community in January of 1981 (Nicoll & Salmon, 1994).

The establishment of EU in 1983 and the plans associated with the whole idea, resulted in December of 1985 in revitalizing the process of European integration by drawing up a Single European Act. This act became official in February 1986 at Luxembourg right after Spain and Portugal joined in on January of the same year (Nicoll & Salmon, 1994).

The goal of a Single European Act was to change chaos into order. The act was accompanied by a five-year plan ending in 1992. According to the plan the following would be achieved by the deadline:

1. Completion of internal market by 1992.
2. Introduction of an emphasis on technology and environment (so as to achieve a progressive market).
3. Introduction of a qualified majority voting on most issues related to a single market.
4. Emphasis on cohesion that would bring countries to similar levels of development.
5. Strengthening of the European Parliament's role.
6. Emphasis on opening markets to competition.

All the above and especially the part of emphasis on cohesion, resulted in Delor's I package. This was financial assistance from the European Union to economically weaker countries enabling all members to reach the same level. Hence, by the end of 1992 goods and services were to be moved freely among members. Physical barriers were to be removed and substituted by governmental obligatory checks on quality and credibility of products as well as people that were to exit or enter a nation. In addition the pre-stated goods were to move around the European Union with fixed indirect taxation rates grouped into two categories, food 5%, and normal goods 15%. Free movement of capital and people communicated the idea of everybody being part of the same country, Europe (Nugent, 1994; Nicoll & Salmon, 1994).

Consequently, Europe started to prepare for the final target, European Monetary Union (EMU) while it communicated connotations of social, cultural and economic integration represented by one currency of this one country.

The Maastricht Treaty

The Community adopted the Single European Act in February 1987. Its nature was a group of actions necessary for the implementation of Europe's dream.... further unification and growth. The challenge that accompanied this Act was the one of "establishing a common economic and social area, creating the conditions for stronger economic growth, acting decisively and in concert on matters of foreign policy adopting the common agricultural policy to changing circumstances in the world and ensuring that the financing of the Community is placed on a sound footing" (Nicoll & Salmon, p277). Based on the above, within five years all goals were to be achieved. The creation of EMU would then be a reality.

In 1988, a step towards the Economic and Monetary Union occurred in Hanover's meeting of European Council. The president of the Commission

(Jacque Delors) was then asked to chair and generate a Committee that would later establish and present concrete steps to be taken towards Economic and Monetary Union. Delors presented the findings of this search on 14-16 June 1989 at the European Council's meeting in Madrid. He proposed the creation of a European system of central banks the nature of which would be federal and with the purpose of managing a single monetary policy. However, Delors did not directly recommend one currency but considered the above a natural consequence of Monetary Union. As a result, the Madrid European Council accepted the plan and decided that the first stage of EMU would begin on the first of July 1990 (Vanthour, 1998; Nicoll & Salmon, 1994).

During this time Europe had to face important political events including the fall of the Berlin wall and the unification of Germany. It was then (April of 1990), that President Mitterand and Chancellor Kohl issued a statement recognizing, due to the political instability in the European area as well as the goal of fulfillment of an internal market and plans for an EMU, the need to move rapidly forward and establish relations among member states under the concept of European Union (EU) (Padoa-Schioppa, 1994; Nicoll & Salmon, 1994).

Based on all the above, EMU's first stage started on July 1 1990, and was followed by full liberalization of capital movements among the eight member states. Spain, Portugal, Greece, and Ireland would join EMU at the end of 1992, since they did not initially progress financially as much as others. Finally, all the progress towards financial integration and the need of further unification led the Foreign and Finance Ministers of the Twelve to sign the Maastricht Treaty on

February 7, 1992. In this way, the European Community was finally transformed into something bigger and stronger, the European Union (EU) (Vanthour, 1998; Nicoll & Salmon, 1994).

The Pillars and Financial Affairs of European Union

The Maastricht Treaty, otherwise known as the Treaty of the European Union, was a step further from the Single European Act. It was composed by measures necessary to create Economic and Monetary Union as well as strengthening relations among the pillars of the Community. More specifically the building of the EU was resting on three main pillars: Economic and Monetary Union (EMU), Common Foreign and Security Policy (CFSP), and Common Justice and Home Affairs Policy (CJHAP or Europol). Goals within these pillars were the strengthening of previously existing policies as well as the creation of new policies for health, education, culture, tourism, consumer protection, establishment of a common legislation for workers, and the strengthening of common citizenship. Goals also included an enlargement of membership as well as increased economic support given to weaker member countries (Nicoll & Salmon, 1994).

The revenues of the Community came from the operation of its own resources. Own resources are defined as common customs and tariff duties, other duties collected from trade with non-member countries, levies on agricultural products and a tax on the GNP of each member. Ninety percent of the expenditures of the Community budget were on agricultural policy and the remaining ten percent on research and development and foreign affairs assistance. (Kerr, 1983) Part of all the above was the second Delors package.

Both Delors packages aimed an increase in member-government funding to help convergence and cohesion leading to a stronger EU. The packages also increased funding for foreign affairs and put an emphasis on technology. In this way the weaker members were economically assisted in the goal to succeed in being equal members within the EU. Later in time it was argued that the only way for Maastricht criteria to be met was through Delors packages (Nugent, 1994; Nicoll & Salmon 1994).

Maastricht Goals

The pre-existed need in Europe for unification; strength and independence led to the establishment of the Maastricht Treaty. The treaty was the only means to a stable monetary zone in Europe. It would secure the achievement of the following:

- true common market,
- creation of Euro, which would be the only one currency by the end of the twelve year plan (Maastricht),
- elimination of intra-EU transaction cost,
- boost of investment,
- boost of international as well as intra-regional trade,

- efficient supply of capital,
- further political integration,
- elimination of internal borders,
- intra-EU uniform standards

A combination of all the above will permit free movement of people, goods and services as well as capital within EU. In that way Europe will be transformed into one of the largest economic blocks of the world (Ramaprasad, 1999).

Hence, one currency will lead to stability and certainty for people and companies engaged in inter-European trade. "Certainty implies guaranteed prices when translating from one currency to another, and this brings increased trade which benefits all parties concerned" (Perry, 1994).

EMU Timetable

"The latest journey towards EMU follows the signing of the Maastricht Treaty with member states agreeing to increase gradually the coordination of economic, financial and monetary policies" (Ulsterbank, 1999). This treaty divides time into three stages and groups the corresponding short-term goals accordingly. Therefore we could refer to the Maastricht Treaty as a twelve-year plan which eventually leads to the creation of the United States of Europe.

This plan, as we have stated, started with Stage I on July 1, 1990. The goal of this particular stage was the strengthening of EMU by the completion of the single market. Stage II started in 1994. Its goal was the implementation of all the legal administrative and technical preparations necessary for the adoption of the single currency. A crucial year within this stage was 1998, as decisions were made about members who would be included in the first wave (first group of members entering EMU). Stage III started in 1999 and it will be completed in the middle of 2002. Here the goal is optimal unification since transformation will take place by the introduction of a single currency, the Euro. Towards the end of stage III all national currencies will be replaced (McKay, 1997;Ulsterbank, 1999).

The third stage towards the completion of EMU is divided into three Phases. The first Phase is 1998-1999. It is a transitional period between stage II and stage III. During that time, the participating member states were chosen. Whether a member state would participate or not was determined by the Maastricht criteria, which we will refer to later. Phase II occupies the years between 1999 and 2001. During this period of time the single currency (Euro) exists. While there is no prohibition in using it neither there is any compulsion. The euro exists in non-cash form only and is not a hard currency. Other characteristics of this phase are the locking up of exchange rates, the common interest rate (single monetary policy) and the operation of the individual counties' Central Banks in euros. The irrevocable conversion rates for the euro were adopted by the EU council on January 1, 1999 and are presented in the following table for the eleven original members of EMU (Oanda, 1999). The euro has the legal right to exist. Government debt is now expressed in euro terms and markets in general rapidly move towards using the euro. As we mentioned above, at the beginning of this phase the euro exists but not in cash form. It is towards the end of this second phase that the euro will be finally introduces in form of coins and notes. Throughout this phase members who did not make it at the first time (1998) have an opportunity to show progress and apply again for acceptance. Last but not least Phase III occupies the year between 2001 and 2002. This is the crucial final transition period since all currencies of the participating member states will be removed from circulation and substituted by Euro. Actually, for this year both the euro and local currencies will be accepted. Nevertheless by the end of 2002 the euro will be the only currency in Europe. Suggested Bank note designs are found in figure 1 (Billoud, 1998; Ulsterbank, 1999).

Table 1.

EURO Conversion Rates **1 EURO =**	
40.3399 Belgian Francs	40.3399 Luxembourg Francs
1.95583 German Marks	2.20371 Netherlands Guinness
166.386 Spanish Pesetas	13.7603 Austrian Sch.
6.55957 French Francs	200.482 Portuguese Escudos
0.787564 Irish Punts	5.94573 Finnish Markka
1936.27 Italian Liras	

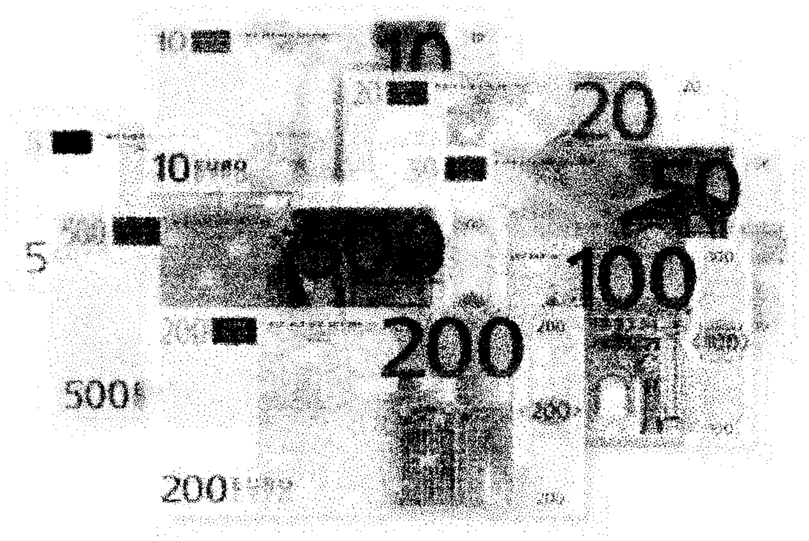

Figure 1. Euro Banknotes

Presently we are experiencing Phase II of the Third Stage of EMU. The first wave took place in 1998. This means that in 1998 all countries that met the Maastricht criteria entered EMU. Surprisingly, thirteen out of fifteen members qualified. These were Austria, Belgium, Denmark, Germany, Finland, France, Ireland, Italy, Luxembourg, The Netherlands, Portugal, Spain, and the UK. However, only eleven chose to participate as UK and Denmark decided to opt-out. Greece and Sweden were the only two countries left outside. Sweden failed to fulfil the conditions because it lacked independence in its central bank and was unable to meet the criteria for the exchange rate mechanism. In addition, the Danish and Swedish governments had also been discouraged by the hostile public opinion of the supporters of the governing Social Democratic parties. It is believed that the UK's opposition influenced both countries. It is anticipated that both will follow the UK when it decides to petition for membership. Greece, on the other hand, had more problems we will discuss later (Chance, 1999; Leonard, 1998).

Maastricht Criteria

According to our discussion so far, we realize that today (1999) the EMU is working its way through Stage III. One of the most crucial elements at this stage is the function of the European Central Bank, as it will issue the European Currency Unit (ECU), which as we have already mentioned is a currency in its own right. Every country that participates in the EMU is obliged to let its own currency be fixed at a specific rate against the ECU (see table 1). This happens so that eventually ECU will successfully replace the European Union's national currencies.

However not all fifteen countries of European Union can automatically participate in this third stage of EMU. This is the case since not all fifteen countries fulfill the necessary conditions for economic convergence. These conditions are better known as Maastricht criteria and are the following:

- Inflation rate: It should not exceed the average of the three lowest countries (best performers) by more than 1.5%

- Long term interest rate: It should not be higher than 2% above the average of the European Union's three best performers
- Public debt: It should not be higher than 60% of GDP
- Budget deficit: It should not be higher than 3% of GDP
- Exchange rate: It must be within normal fluctuation margins of the ERM (European Monetary System) for two years without severe tensions.

(Pond, 1999).

There has been a first wave of countries that qualified entering the third stage towards EMU implementation. As we have said all countries qualified except Greece and Sweden, while the UK and Denmark chose not to participate. What is worth stressing though is that staying out of the EMU does not mean that the Euro will not affect these four countries (Pond, 1999). This is actually the case as 'several large multinational companies have already announced that they will invoice their customers in Euros rather than their national currency. The probability is that a dual currency system will be in operation in the same way that the US dollar is a parallel currency in much of Latin America'. Pressure for a dual currency will also come from tourism. European tourists arriving in Greece, the UK, Copenhagen or Stockholm, that will expect to pay hotels, restaurants and more in euros (Leonard, 1998; Pond, 1999).

Consequently, the whole idea for meeting the criteria can be seen as obeying the rules of a game. A game leading to the desirable outcome of total unification and growth of member countries. More specifically the effects of meeting the Maastricht criteria can be examined in the short-run and long run.

Short - Run Effects of Criteria

Starting with short run effects the EMU needs to prove that it exists and will be implemented. By doing so the Euro will become as stable as the Deutsche Mark and many benefits will be generated from then on. However this "story", although it sounds simple, can not generate stability overnight. On the contrary, it needs time to evolve. Therefore a measure of where EMU stands is the convergence criteria, as they provide all necessary information about the percent of convergence before Europe moves to the single currency (Vanthour, 1998).

We know that thirteen out of fifteen countries managed to meet the criteria by 1998 and came together. They reached desired levels as far as interest rates and inflation are concerned. The budgetary criteria might have been the hardest to meet as both France and Germany (founders of the whole concept of EMU and EU) had difficulty in achieving a budget deficit less than three percent of their GDP. At this point we should refer to the fact that public deficit was still more than three percent of GDP in 1996. However, both countries exercised additional fiscal policy measures and as a result of great efforts the budgetary criterion was met on time (Vanthour, 1998).

Exchange rate mechanism is another tool used in order for countries to have a standard while trying to qualify. To confirm that we should state that this mechanism was built to prevent exchange rate fluctuations between the euro and the currencies of countries that will join the EMU later. Every European

Union member is given a central rate both against the euro and every other currency within the mechanism. Member currencies are allowed to fluctuate by fifteen percent on either side of the particular rate. The direct result of using such an exchange rate mechanism is the promotion and achievement of coherence among members and the assurance that the European market will not have to suffer from fluctuations in exchange rates between either side of countries and the euro (Vanthour, 1998).

Long - Run Effects of Criteria

This section will examine the long run effects of meeting the convergence criteria and in general of implementing EMU. As discussed through this paper the optimal goals of the European Union is unification, power and growth. At the same time the optimal goal of the EMU, that also contributes to the goals of the EU, is economic and monetary unification.

There is more than economic and monetary unification and this is a political unification. It was believed throughout the history of European Union that the absolute unification would be one of not only currencies but people and politics too. Although this is a desired outcome of the whole attempt no one seems to really believe in it. The reason is that no matter how close members will come and feel as equal parts of the same supranational organization, national interests never seem to disappear (Vanthour, 1998).

A representative example is that Germany and France still have totally different beliefs about the Political Union. On one hand Germany supports political integration, especially after the fall of Berlin Wall, and it wishes for Europe to integrate even more. France, however, has always regarded European integration as a way to ensure its own influence in Europe. This is obvious, as France throughout the history of the building up of the EU, wanted to be the nucleus of the EU rather than being part of it (Vanthour, 1998).

However, entering the EMU and coexisting under the umbrella of a supranational organization secures that no member will dominate in the future. Achieving, in the long run, a political union should be one major goal. No monetary union is viable without political unification. In other words having one currency in the EU without a political unification will not lead to anywhere else but failure (Vanthour, 1998).

To summarize, the EU needs not only widening (more members) but also deepening (expanding the economic relations to political relations). "Building EMU is rather like building a house. Strict interpretation of the convergence criteria makes for solid foundations" (Vanthour, 1998). Therefore, more work is needed for further unification in the long run and this would be the political one.

Greece and the European Monetary Union

Political – Social – Cultural Environment in Greece

Greece is a southern European country between Albania and Turkey that borders the Aegean Sea and Mediterranean Sea. In terms of geographical size, as well as population, is among the smaller countries in the European Union. Greece occupies 131,940 square kilometers and has a population of 10,616,055 according to July 1997 estimates. The official language is Greek and official religion is the Greek Orthodox (98% of the population) (Greece World Factbook, 1999).

Greece has a great history of more than 5,000 years, which is cherished and respected by Greeks throughout time. This relatively small country constitutes one of the most ancient centers of civilization. Its history and fame – spread throughout the world – is considered to be disproportionate with its size and population. The immortal Greek spirit managed to survive through very difficult times and inspired Greek generations for many years.

During the last 15 years Greeks realized that in order to keep up with what happened in the modern world they had to permit external elements to penetrate and influence Greece's politics. Many suggested that the latter could signify an end for the whole notion of a "Greek nation". As an example a Greek journalist writes that when Greece decides to let modern civilization falsify its history, education and religion – its culture in other words – then in few years nobody will be able to recognize it (Marinos, 1991).

Of course, all the basic convictions that people have regarding what is right and wrong, good and bad, important and unimportant (values), as well as all the persistent tendencies to feel and behave in a particular way towards a belief (attitudes), demonstrate how the majority of Greeks felt over the years for their nation. In other words, Greeks used to strongly support the notion that their country should continue in the course of history as unaltered as possible. Their ethnocentric behavior was reinforced by their persistence on electing governments that did not account for change and kept foreigners away (Hodges & Rugman, 1995).

That is exactly what Mr. A. Papandreou, president of the socialist party PASOK, used as a base for his campaign when he was elected in the 1980s. He had been promising this to his voters for nearly 15 years. Papandreou wanted to get Greece out of NATO and EEC so that Greece would not be controlled or manipulated by western people (Glastris, 1996). We should note that Greece's political ideology and culture were almost inseparable during this time. The fact that most Greeks focused solely on what history had to present in the east – Constantinople, the old Byzantine Empire – made them unavoidably suspicious of the west. Greeks viewed westerners as people who wanted to get a foothold in Greece and after that destroy everything Hellenic that existed. Mr. Papandreou as a demagogic master grasped these old anti-western attitudes and beliefs and successfully turned them into the theme of his political campaign. In this way, Mr. Papandreou gained voters for a long time as he was telling people what they wanted to hear (Glastris, 1996).

Unfortunately for the Greek State, Papandreou's efforts to keep foreign capital outside Greece led the country's economy into recession. By adopting the well-known Ottoman system of "rousfeti" (hiring people on the basis of their political beliefs) he continued appointing unneeded personnel at different positions of the public sector. Consequently, an inefficient, huge, and bloated public sector was created that soon became the largest source of problems for the country's economy. On the one hand, Mr. Papandreou was able to please his voters as few political leaders could, while on the other hand he brought the country to a point that it could not survive without EC's assistance -- subsidies (A Gleam of Hope, 1996).

For as long as Mr. Papandreou ruled Greece, its economic position among EU member states was low. However, things started to change and attempts for economic progress started to occur after the Maastricht Treaty in 1992. It was at that point in time that Greece realized how important it was to be a part of European Monetary Union. The EMU became the center of public attention in Greece and Papandreou was "forced" to change his politics. The latter, in combination with the health problems he experienced at the time, resulted in the appointment of a new president for his party, Mr. Kosta Simiti (A Gleam of Hope, 1996; Kokkinaki, 1998)

Mr. Simitis appeared to be the only "gleam of hope" in the horizon for Greece when he was appointed Prime Minister. Kostas Simitis introduced commitment and guidance to Greece's entrance in EMU. People believed that he would manage to get rid of the populist image introduced by his predecessor of PASOK. Since Mr. Simitis was considered as "the businessman's choice for Prime Minister", he was expected to act as one of them. He would try to modernize Greece while at the same time preserve Greek cultural history. Mr. Simitis' primary goal was to help Greece to take all the necessary steps that would bring it closer to the economic and monetary union of Europe. However, before Mr. Simitis could succeed he had to accomplish another very difficult objective: he had to change people's attitudes toward politics while at the same time to restore the image of the Greek public (A Gleam of Hope, 1996; Greece, 1996).

It is believed that Mr. Simitis' attempts have been successful as Greeks finally realized that their political culture had to be converted. Greeks accepted that political parties should not be responsible for finding them a job. They also became more open minded as they abandoned their beliefs about Greece being an underdog that was endlessly "betrayed" by powerful countries. As a direct consequence these changes allowed the Prime Minister performed his tasks properly. Simitis established a healthier public sector by undertaking heavy privatization efforts and providing for an unbiased judiciary and independent press. Therefore Greeks were no longer zealous patriots. They learned not to overemphasize the importance of their nation and they did not support the thesis that the "world is out to get them". Finally, after many years, one thing is clear in Greece: political life is distinguished from the cultural and social values. This attitude change was the only way that would allow Greece to be a part of future economic events (A Gleam of Hope, 1996).

Last but not least, it is quite obvious that Mr. Simitis brought the painful changes needed to bring Greece in line with its EU partners while at the same time he synchronized and modernized the Greek economy. His government applied a strict program in its 1997 budget in order to meet the economic convergence criteria that would enable Greece to join the single currency (see page 39-47). Direct results of these policies were increases in growth rates and decreases in inflation rates and budget deficits. However, these positive changes had short-term economic costs for citizens through a freeze on wages. All the above showed that Greeks finally changed their beliefs and were willing to face the strict economic consequences of attempting to enter the EMU (Kokkinaki, 1998).

This argument is supported by different public opinion surveys, one of which is Mrs. Kokkinaki's. Kokkinaki supports in her 1998 study that the mean attitude towards EMU was relatively positive 3.29 (SD = 1.03). This means that as a whole the whole Greeks are in favor of EMU; only 14.5% thought that EMU was bad idea and just 20.8% were against one currency. At the same time the majority of respondents 57.1% considered EMU a good thing and 55.1% were in favor of a single currency. Furthermore while the study shows that "respondents were slightly pessimistic about the consequences of EMU on their personal income, value of their savings and prices of goods, they were optimistic about the consequences of EMU on job security and the inflation rate. They did not expect to loose money from the introduction of EURO" (Kokkinaki, 1998).

Economic Environment in Greece

In the first two decades of the postwar period, Greece was growing at rates much higher than the European average. This was the case as it had the lowest per capita income among the 16 OECD countries from 1950 to 1972 but had the highest output growth (an average rate of 6.2%).

Table 2. Real GDP Annual Changes.

YEAR	GDP	YEAR	GDP
1971	7.13	1985	3.12
1972	8.87	1986	1.62
1973	7.31	1987	-0.46
1974	-3.64	1988	5.36
1975	6.07	1989	3.8
1976	6.35	1990	0
1977	3.44	1991	3.1
1978	6.68	1992	0.7
1979	3.87	1993	-1.6
1980	1.74	1994	2
1981	0.06	1995	2.1
1982	-0.53	1996	2.4
1983	-0.78	1997	3.2
1984	2.75	1998	3.7
1984	2.75	1998	3.7

However, during the two decades that followed the process was reversed and this led Greece to diverge from the other European economies in terms of economic activity. Greece still had the lowest per capita income but the average growth rate was reduced to only 1.5% until 1994 (see table 2 & figure 4). It is strongly believed that if the initial high rate of growth had continued it would have led the economy to converge with European economies earlier (Christodoulakis & Kalyvitis, 1998; IMF, Nov 1999).

Nevertheless, several changes occurred in the Greek economy, especially during the last 10 years, in a way such that the attempt for participation in EMU later in time would be achieved. In an effort to describe the basic elements of the Greek economy during the last years we should refer to the following:

The Greek economy is divided into two sectors, the private (55% of GDP) and the state (45% of GDP). Out of the approximate 10.6 million of population the workforce is about 4 million. The per capita GDP as of 1998 was $11,398 and it was the lowest in EMU. However, with GDP growth above the average the gap is steadily but slowly closing. The largest and fastest growing sector of the Greek economy is services (70% of GDP) with tourism, shipping, trade, banking, communications, construction, and transportation the largest services' sub-sectors (National Trade Databank, 1999; Bureau of Economic Analysis, 1998).

Greece is an import dependent country since exports are less than its imports (see table 3 & figure 2). A representative illustration is the one of 1997 when 7,590.6 billions drachmas were imports while exports were 2,355.4 billions drachmas (IMF, 1999).

Table 3. Export & Imports in Billions of Local Currency Units.

YEAR	EXPORTS	IMPORTS
1986	790.0	1587.4
1987	881.0	1773.4
1988	776.4	1758.0
1989	1231.0	2629.4
1990	1281.0	3137.9
1991	1584.6	3921.9
1992	1817.7	4442.3
1993	1934.2	5051.6
1994	2276.6	5207.6
1995	2539.2	6010.2
1996	2281.8	6593.6
1997	2355.4	7590.6

The basic reason behind the low exports is the lack of investment especially in the last 10 years (see table 4) (IMF, Nov 1999). Greece exports mainly agricultural products and light manufactured products and it imports more sophisticated ones like medical equipment, telecommunication equipment, computers, all types of air-conditioning and more (National Trade Databank, 1999; Bureau of Economic Analysis, 1998).

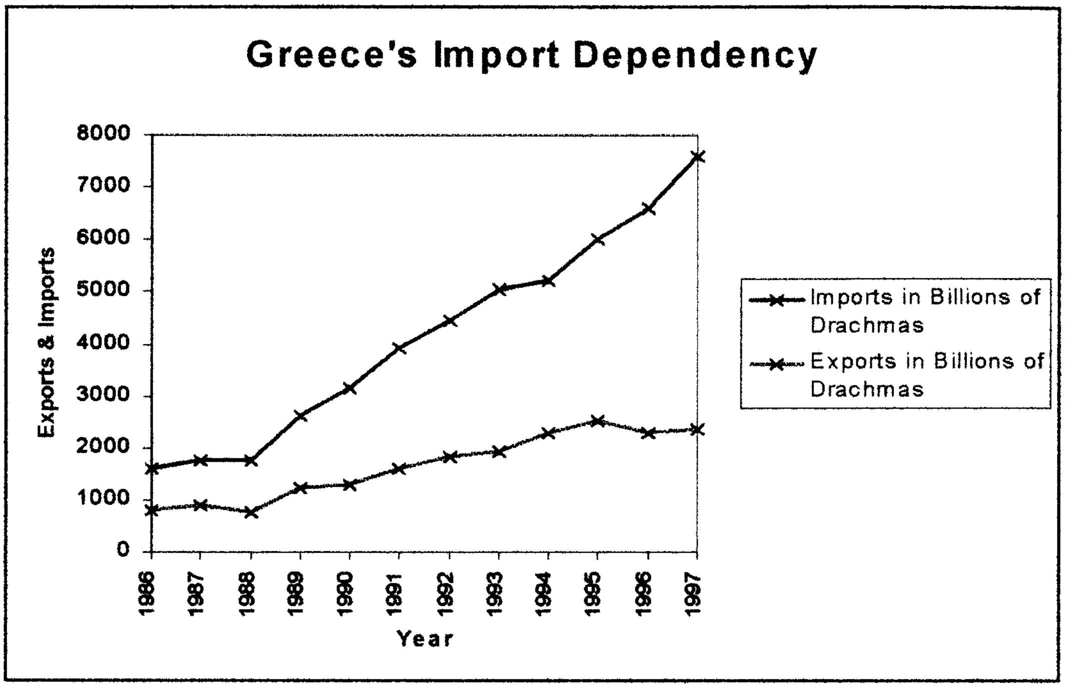

Figure 2. Exports & Imports in Local Currency Units.

Table 4. Inward Foreign Direct Investment & Other Investments (% of GDP).

YEAR	INVESTMENT
1991-1994	1.9
1995	3.7
1996	4.2
1997	2.6
1998	2

As discussed so far 'in the context of the European Union, the process of real convergence is viewed as a prerequisite for the cohesion and long run sustainability of the Economic and Monetary Union. In an effort to promote growth and cohesion among member states, the EU has put particular weight on remedying structural deficiencies in less developed countries such as Greece. The basic policy instrument for achieving this target is the inflow of structural funds, which aim at increasing the physical and human capital of each country" (Christodoulakis & Kalyvitis, 1998).

Consequently, funds from EU to Greece were allocated basically for major infrastructure projects and they were up to $20 billion for the period of 1994-1999.They were allocated under the condition that a majority of projects were to be built by given deadlines. Greece managed to utilize about 70% of these funds to date. There is a possibility of another structural fund beyond 1999 (Bureau of Economic Analysis, 1998).

However the structural funds, and in general the idea of the convergence program, does not only concern infrastructure projects but also promotes privatization. Greece's progress in this area is limited, since it managed to primarily privatize a few small banks and Hellenic duty free shops. Later in time the government sold minority of stakes in the Hellenic Telecommunications Organization (35%), the National Bank of Greece, and in the Hellenic Petroleum (state petroleum distributor). Also, it created a plan of further privatization of organizations like the Ionian Bank, the Olympic Airways Catering, and the Athens Stock Exchange (Bureau of Economic Analysis, 1998).

In an attempt to demonstrate what the EU financial assistance plan tries to promote and achieve, we should refer to the following five main axis: (Christodoulakis & Kalyvitis, 1998).

1. Promotion of domestic integration by large scale expenditures on the infrastructure: Aiming at the reduction of regional isolation and promotion of connectivity between Greece and the rest of the world and of different geographical areas within Greece.
2. Improvement of the quality of life: Improving the systems of health and welfare, urban development and environment protection.
3. Growth and competitiveness: Aiming at improving competitiveness of the production sector, as 44% of the funds will be used for industrial investment and 42% will be used for R&D, agriculture and fishery.
4. Upgrading of human capital and promotion of employment: Aiming at the improvement of the quality of the education system, finance training and retraining of employees into new skills and technologies.
5. Reduction of regional inequalities and isolation: Aiming at the improvement of the living conditions at 13 different regions in Greece.

As we have already said, despite the financial assistance that Greece received from the Union, it failed to meet the criteria for the European Monetary Union in the first wave. The next attempt will be to join on January 1 of 2001, based on the economic performance of 1999. So far the results of all the policies taken have been positive. Inflation has decreased from 5.41% in 1997 to 4.5% in 1998. Private investment became stronger and is growing. GDP increased from 10700.6 billions of drachmas in 1997 to 11096.52 billions of drachmas in 1998. Finally, the ratio of the budget deficit to GDP has fallen by 4% in 1998. At this point we should refer at the fact that "Greece's huge government debt of 108.9% of GDP in 1997, stemmed to a great extend from government acquisition of failing enterprises and a bloated public sector. Greece's social security program has also been a major drain on public spending, while deficits are financed primarily through issuance of government securities." However the government managed to decrease the debt to 106.1% of GDP on 1998 (Bureau of Economic Analysis, 1998; IMF-Greece staff report, 1999).

As far as it concerns the exchange rate policy, medium and long-term capital movement has been fully liberalized and Greece's foreign exchange market is compatible with the EU's requirements on free movement of capital. The stable drachma policy is the policy that the Greek Government applied so as to prevent the drachma from depreciating against other EU currencies and it was applied from 1994 to March 1998. The results were positive as the drachma managed to be included in the Exchange Rate Mechanism on March 16 of 1998, after 12.3% devaluation on March 14 of 1998. It was then that The Greek Government made a promise, to the EU monetary committee, to meet the EMU criteria by the end of 1999. According to all the above drachma now participates in ERM from January of 1999 at the central rate of 3 drachmas = 1 euro, and it is allowed to fluctuate ±15% of the central rate (Bureau of Economic Analysis, 1998).

To conclude, Yannos Papantoniou, the Greek minister of national economy and finance feels very confident about Greece's attempt to enter the EMU at the next wave. More specifically he claims that " the economic climate in Greece has improved substantially over the recent years and especially during 1998. We want to fulfill the criteria for joining Europe's economic and monetary union by the end of 1999 so that we apply for membership in the year 2000 and join EMU by January 1, 2001. We shall meet this objective" (Papantoniou, 1998). Papantoniou's opinion is also shared by others. Phyllis Reed, government bond economist at Barclays Capital, said: "The Greeks are the best value as their spreads are high in relative and absolute terms and they are the most likely to join the euro next" (Dyson & Lee, 1999).

How Close is Greece to EMU?

In an attempt to meet the Maastricht criteria and become member of EMU, Greek governments struggled over the last ten years to bring the economy at desired levels. The different macroeconomic policies that were applied throughout these years are going to be analyzed in depth at the section that follows. However, our scope at the particular thesis segment is to provide visual representations of the economy so far and therefore a hint of how close the economy is to convergence. At this point it should be mentioned that all necessary data used for the illustrations that follow were taken from the

European Commission Data Books as well as from the database of the International Monetary Fund (IMF).

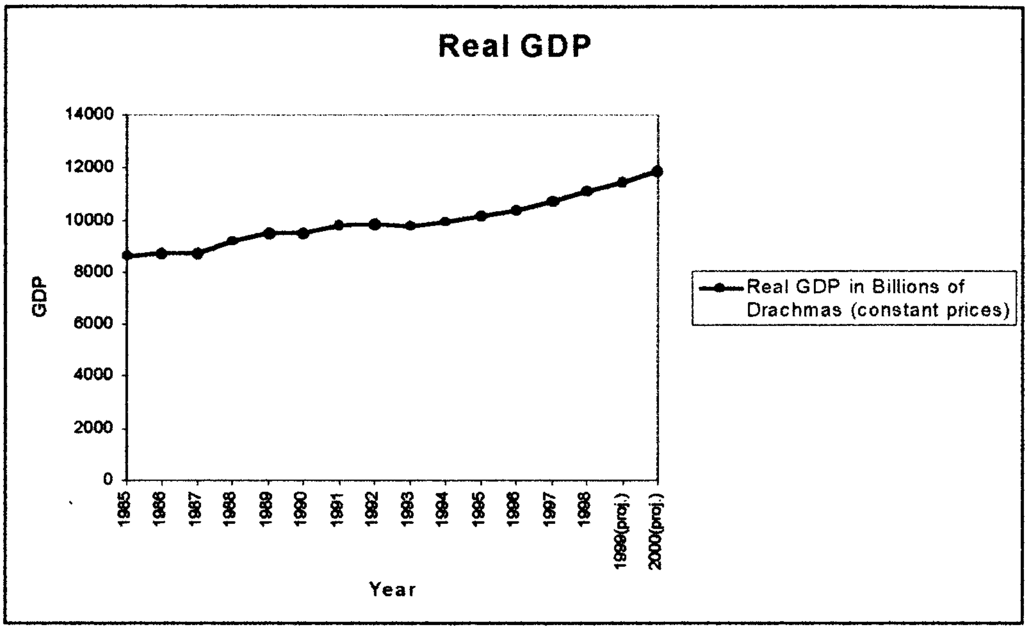

Figure 3.

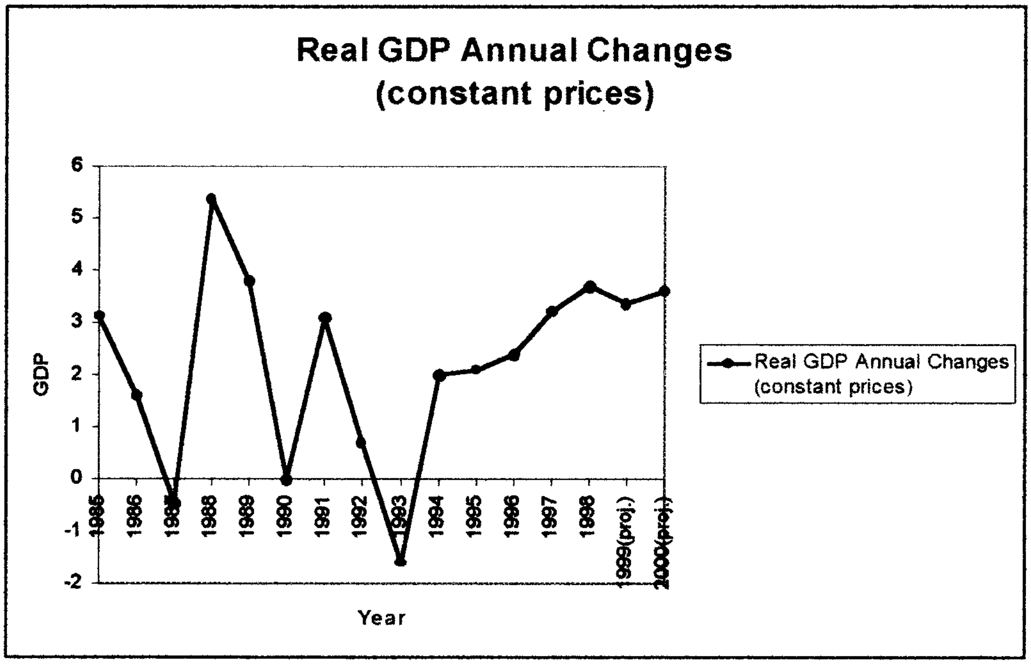

Figure 4.

From the above figures it is obvious that since 1994-1995 the Greek economy steadily and continuously performs well. Even in years 1998-1999 when the two main events of the war in Kosovo and a destructive earthquake in Greece took place, the growth was unabated. High investment rates, brisk consumer lending that sustained the level of consumption, and more exports also contributed to this growth. In 1999, GDP increased at approximately 3.4%, holding it in the fourth successive year of faster growth than the EU average. Percent growth is anticipated for the year 2000 at 3.6% and 2001 at 4%. All the above signify that convergence is not far away for Greece (IMF, Nov 1999).

Indeed, due to this growth, EMU is not a distance dream any more. By 1999 Greece met four out of five criteria: exchange rate, fiscal deficit, long-term interest rate, and debt. Greece met some of the criteria by a large margin. For example the fiscal deficit, which in 1993 was 13.8% of GDP was in 1999 1.5% of GDP against a target of 2.1% and a Maastricht requirement of 3%. This decline is also anticipated to continue in 2000, with a predicted value of 1.2% against the target of 1.7%. It is argued that, despite the plans for tax relief and social security improvements, the decline will not be altered. All additional expenditures will be counterbalanced by an increase in the tax on stock market transactions. The result will bring the net cost down to 6% of GDP (IMF, Nov 1999).

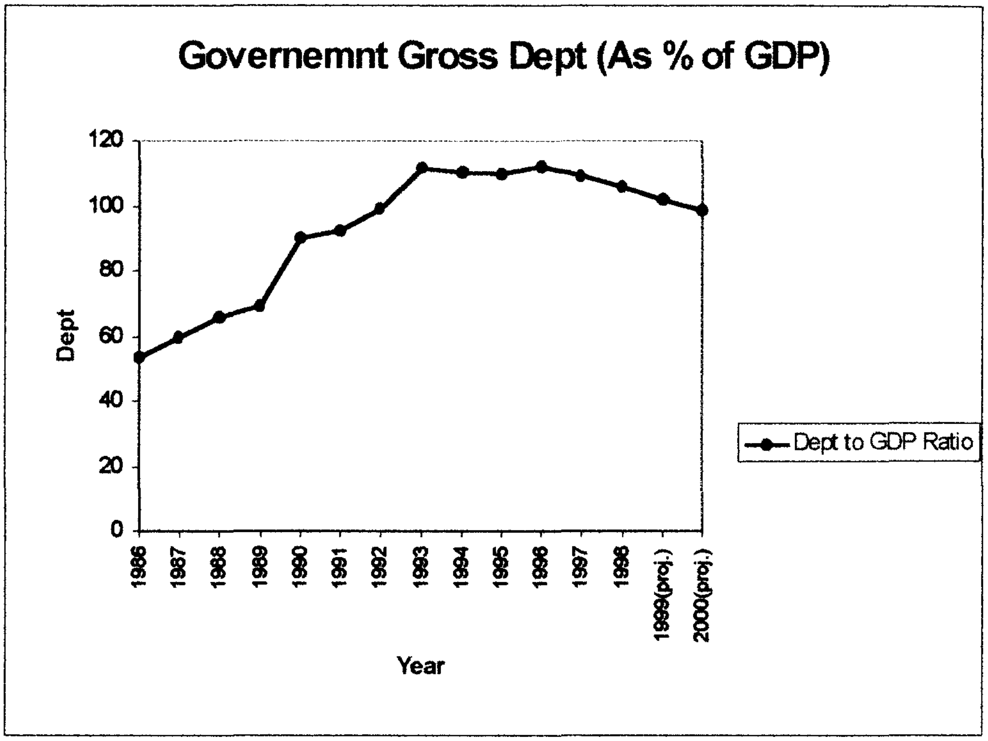

Figure 5.

High privatization and partial flotation programs were parts of Greece's structural reforms that were announced in March of 1998 and were implemented by the end of 1999. These in combination with a low fiscal deficit, managed to decrease the debt to GDP ratio by 3.4% points in 1998 and an additional decrease of 1.5% point has been anticipated by the end of 1999. The level of gross national debt in the middle of 1999 was still high (104.5% of GDP) but Greece's government has been optimistic about a continuing fall due to the opening of competition in large areas of the economy like shipping, electricity and more (IMF, Nov 1999).

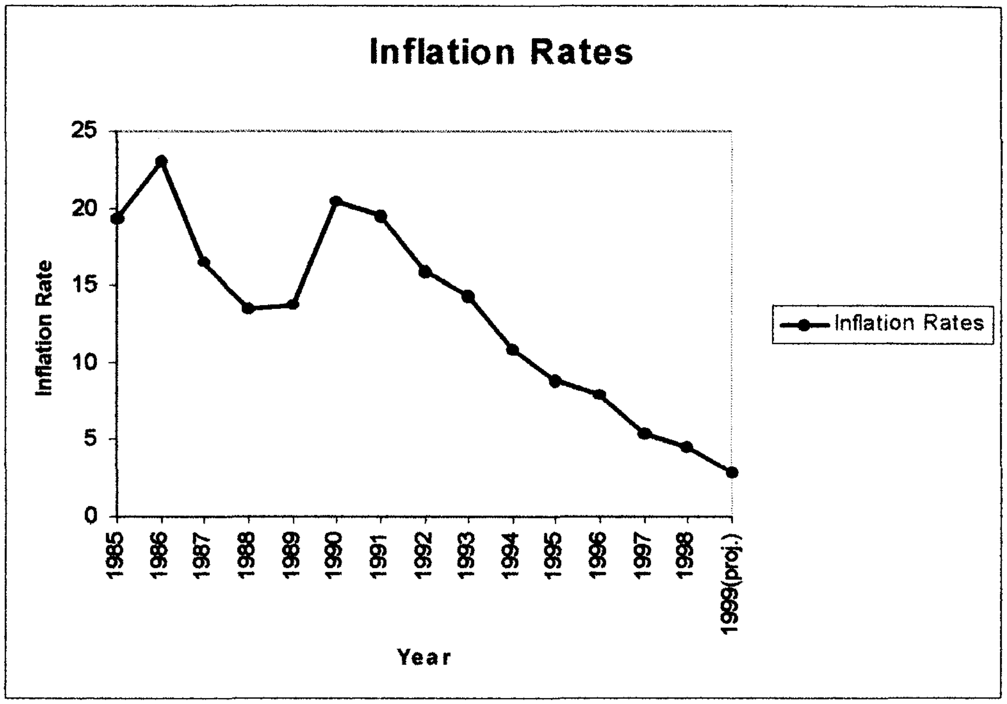

Figure 6.

Although anti-inflation progress has been substantial over the years, it still does not satisfy the reference value of 2-2.1% in terms of the harmonized index as required by the Maastricht criterion. This criterion was the most difficult to meet even by member countries that already are part of EMU. We should note here that Greece entered the ERM in March of 1998 while that period a devaluation of Drachma also took place. As expected, given Greece's reliance on imports, this resulted in a persistent inflation rate at relatively "high" levels over the summer of the same year. Nevertheless, Greece took action by introducing indirect tax cuts and other offsetting income policies in 1998. Greece is hoping that the inflation criterion will be met by 2000 despite the anticipated pick up of inflation in late 2000 and 2001 due to indirect tax cuts (IMF, Nov 1999).

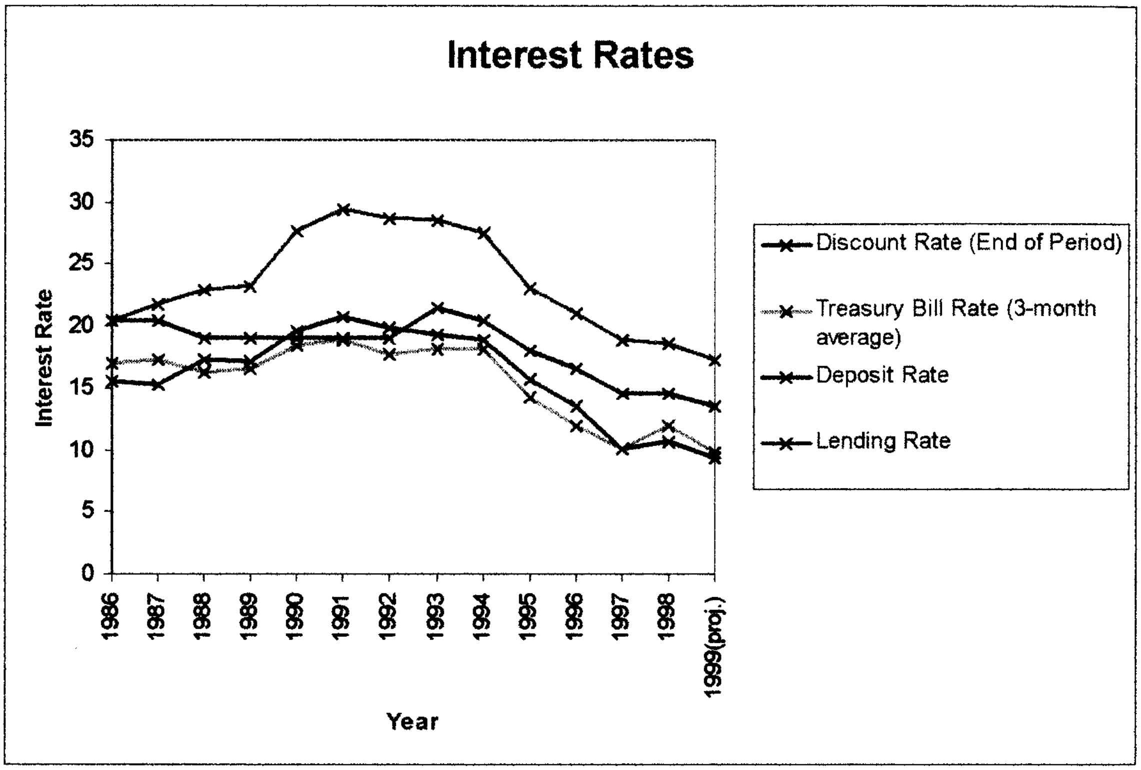

Figure 7.

As we have already mentioned, the Drachma was devaluated in 1998 while Greece entered the ERM on March of the same year. Over the years and due to tight monetary policies the government managed to reduce the interest rates. These policies were centered on high interest rates and a strong Drachma within ERM, assisting anti-inflationary efforts in this way. Later in time a very sharp decrease in long-term interest rate and an increase in equity market activity caused favorable reactions by the financial markets. However, as it is also analyzed in the next section, the effectiveness on monetary policy decreases as Greece approaches to convergence (IMF, Oct 1999).

The detailed presentation of the policies that the Greek government has taken during the last four years follows, in order to provide a better understanding of the way the above results have been achieved.

Greece's Macroeconomic Attempts to Meet the Criteria

As it has already been mentioned the Greek economy was in a very bad shape during the 1980s. High levels of spending and lack of fiscal controls during that period resulted in an inflation level above 20% in 1990. The economic recovery in Greece started right after and it has been driven mainly since by EU funding and private consumption. More aggressive economic reform programs were applied having as a goal the gradual recovery of the economy and the country's eligibility to join EMU. It is argued that Costas Simitis, who was elected Prime Minister of Greece in 1996, was the person that tried the most to bring Greece closer to EMU membership. He believed in the EMU and the benefits associated with a future membership for Greece. He "prioritized preparations for membership of the single currency and argued strongly in favor of rigorous policies to reduce the budget deficit and the rate of inflation" (Greek Economy, 1997). Let us now explore the economic policies that the Greek government applied over the last years.

Until 1996, the burden of fiscal consolidation fell mainly on taxes, and more specifically, on indirect taxes. However, in 1997 this burden of adaptation to the Maastricht criteria was focused more on the reduction of interest payments as well as on the curtailment of primary government expenditures. Hence, this was the result of changes in the fiscal policies that eventually would lead Greece inside EMU. Nevertheless we should keep in mind that while a country attempts to become a member of EMU and takes on different policies the problems and struggles of that economy do not stop there. This is the case as, within EMU, economic efforts will not be relaxed. On the contrary, they will become more aggressive as fiscal competition among members will be "the case". By that we mean that since members will be obliged to sustain low government deficits the national governments will try to maximize tax their revenues for the implementation of different fiscal policies. Competition between member countries will result, "since any measures increasing the tax burden rather than the tax base will make this country non-competitive given that the capital and labor will be free to move from country to country" (Christodoulakis, 1997).

Hence, all members will exercise such policies so as to reduce the fiscal burden on their tax payers and attract local as well as foreign capital, enlarge the tax base and consequently increase the level of states revenues. Greece realized this around 1997. This is why Greek policies from that point on were aimed to fight tax evasion, increase efficiency and ensure reduction of fiscal disincentives to enterprises as well as employees. More specifically the above policies reinforced the main objectives of Greece's fiscal policies. In order for these goals to be implemented or achieved, the government attempted to "decrease the expenditures that caused distortions to economic activity such as interest rate payments of public debt". By reducing these expenditures funds were made available for job creation or other kinds of investment. (Christodoulakis, 1997).

Consequently in 1997, the Greek government started to monitor expenditures more carefully while it set up an evaluation procedure for these expenditures. A closer examination of operational costs of various ministries and the way subsidies were used also took place. The new approach was more focused on the level and quality of social benefits provided by government expenditures. A representative example of a change in budget policy is the one of the revised social policy. The revised policy was targeted more towards those with maximum needs, like low-income pensioners. Concerning the institutional changes, the government introduced new salary scales and new pension laws in order to transform the ineffective previous system by providing new criteria for eligibility. With these policy changes also came new hiring methods for civil servants as well as new methods of evaluating subsidies and more. (Christodoulakis, 1997).

The 1997 policy adjustments and applications were followed by similar ones in 1998. In March of 1998 the government followed an alternative strategy of devaluation to achieve entrance into the exchange rate mechanism. The expected reduction on interest rates and the nominal wage restraints were necessary to support the fiscal consolidation.

Additionally, during that year, Greece's economy started to approach the European Monetary Union reality as growth increased. The fiscal deficit was decreased below 3% of GDP, the debt to GDP ratio decreased and more importantly the devaluation in coordination with reduction in indirect taxes and other administrative measures resulted in the moderation of inflation. However, post-devaluation inflation proved persistent (5.3% in May of 1998), forcing the government to take a series of administrative measures so as to reduce inflation to even more desirable levels (IMF, Nov 1999).

As a result, in the fall of 1998 the government "reduced indirect taxes on a range of products, limited adjustment in administrative prices, entered into a series of "gentlemen's agreements" to cap price increases" (IMF, Nov 199). A direct consequence was the decrease of inflation to 2% in August 1999. This was a rate that was actually lower than the rates of other member countries. This rate did not satisfy the Maastrich criterion. It was one and one quarter percent above the differential allowed in calculating the reference limit. Nevertheless, this differential was on a declining path and would continue to be so, as it was supported by additional indirect tax cuts in August and September of 1999 (see figure 6) (IMF, Nov 1999).

A tight monetary policy stance also contributed to the anti-inflationary efforts. The main goal of the Bank of Greece was price stability (an inflation rate that not to exceed 2%) to be achieved by the end of 1999. The Bank maintained high official interest rates and allowed drachma to appreciate within the Exchange Rate Mechanism (ERM) margins that were 8 – 8¾% after ERM entry and ±15% after January of 1999 (ERM2). However, the effectiveness of monetary policy is diminishing as Greece comes closer to join EMU. This is the case since high interest rates generated capital inflows that were followed by build up of foreign exchange reserves which resulted in a credit expansion above the 6-9% range. Also, the growth of mortgage and consumer lending stimulated worries about an inflationary impact. As a result in April of 1999, the Bank of Greece imposed temporary credit controls and by the end of July 1999 the penalty for excess lending was doubled (IMF, Nov 1999).

In 1998, the Government supported a tighter fiscal policy that would increase uncertainty as to how much the inflation rate would be decreased. Because of this the government decided to focus on remedying the direct impact of devaluation on fiscal accounts and to retain a deficit target of 2.4% of GDP. The target was met despite an overrun in primary spending (that was offset by an over-performance of revenue). In addition the debt to GDP ratio further decreased to 106.1% of GDP, mainly through high privatization revenues (IMF, Nov 1999).

Last but not least, progress on structural reforms was also achieved for that year. This was the case since privatization and partial flotation programs were followed and successfully implemented. Representative examples are the steps towards privatization of Bank of Macedonia - Thrace, General Bank, Bank of Crete, Bank of Central Greece, Athens - Piraeus Electric Buses and more. However, there were still major sectors and organizations that continued to be dominated by public enterprises and this proves that many more steps towards privatization were to be taken. Social security and labor market reforms were on hold for that period (IMF, Nov 1999).

It has been clear that the most challenging criterion to be met was the one of price stability. During 1999, attempts to meet the criterion were continued while within this economic year the main problem was the inflation in private services and certain retail sectors. These were indications of demand driven pressures and lack of competition in these sectors. The government undertook new macroeconomic policies to achieve a low and sustainable price performance. The first step was taken in early September of 1999 and was the decreases in excise taxes on gasoline, heating oil and car purchases. Later the proposed post devaluation tightening of the fiscal stance left the government without a lot of alternatives to choose from. However, indirect tax cuts had undesirable short-term effects on inflation that unavoidably led to loss of control over price stability as required by the Maastricht criterion. The Staff projected a rise in inflation in late 2000 and the whole 2001. These tax cuts affected the fiscal accounts while at the same time they risked fueling increases in consumption. The Greek government was positive about the ultimate effects of the actions taken and counted on high revenue performance to balance any alterations of fiscal targets caused by the indirect tax cuts (IMF, Nov 1999).

In 1999, the policy of Bank of Greece was to maintain a tight monetary stance. It was aware of the waning effects of such a policy given the approaching EMU membership. It was felt that the implementation of such a policy was constrained by a combination of the traditional capital inflows dilemma faced by exchange rates based disinflation and the EMU convergence process that largely predetermined expectations regarding interest rates. In this setting, the ability of monetary policy to curb credit growth was eroded. This was the result since, on the demand side, the public had a widespread perception that interest rates would per force decline while on the supply side, banks' stood ready to effect reductions in lending rates in their vigorous pursue of market shares (IMF, Nov 1999, p8). All the above circumstances led the Bank of Greece to apply the measures of April 1999 that we referred to previously, in order to restrain credit growth.

During the same year the fiscal plans were the following: According to the convergence program of 1998-2001 the government deficit was targeted to fall from 2.4% of GDP in 1998 to 0.8% of GDP in 2001, while the expectations for the surplus were an increase of 6.7% to 7% of GDP for the same period. The plans for deficit targets aimed to steady and slow improvement in the overall balance which improvement would be more rapid than the one anticipated by the exercise of the program used so far. Hence, deficit targets for the next two years were considered no more than 1.5% of GDP in 2000 and 0.5% of GDP in 2001. Less than the convergence rates of 1.7% of GDP and 0.8% of GDP respectively used until then (IMF, Nov 1999).

Another goal was the achievement of fiscal balance by 2002, since this is an indication of observing growth and stability of an economy. To achieve the above suggestions were made about the primary need of evaluating the long term and medium term assets and liabilities of the public sector. This was the case as the problems of the economy were “high government-debt ratio (that even a surplus of 7% of GDP would not counterbalance), contingent liabilities, highest unfunded pension liabilities in OECD, large debt accumulated by chronically loss making public enterprises” (IMF, Nov 1999, p12). One way that Greece was planning to proceed was through large privatization and the other course of action was the establishment of a medium term fiscal target. The fiscal plans were expected to ease with inflationary pressure that other policies brought in the economic environment. The latter performance showed over-performance on the revenue while the tax administration remained the same. Another part of these revenues was due to tax on share transactions. The government proposed the use of a substantial part of revenues the for deficit reductions and a smaller part for financing additional indirect tax cuts (IMF, Nov 1999).

In September of 1999 the government announced tax cuts and benefit increases starting in January 2000. The part of increases in benefits was an attempt to show the public some tangible benefits from the whole pursuit of stability and the cost associated. More specifically the new attempts would include increase of the tax exempt income level, increase in tax allowances for families with children, decrease in corporate tax for small businesses, decrease in social security contribution of new hired individuals as well as increase in unemployment and specific pension benefits. The financing of the above plan will be generated mainly from the doubling of taxes on stock sales (IMF, Nov 1999).

Concerning wage moderation, the two-year national wage agreement concludes at the end of 1999. The early signs of renewal indications are considered encouraging while it is said that the 2000 budget will probably include wage moderation for civil servants and public enterprises. Banking wage moderation will be extended in 2000 and will enjoy moderate awards. However, since the wages in Greece have to become compatible to the European rates more understanding in negotiations is expected from both sides of employees and employers (IMF, Nov 1999).

Lastly, a lot of steps are planned to be taken on structural reforms that will greatly contribute to disinflation and growth. Main targets are the strengthening of competition and increases in productivity. This will be done .through even higher privatization, public enterprise restructuring, liberalization of product markets and labor market reforms. It has been shown that privatization in past years had contributed to 3.5% growth in GDP through the first quarter of 1999. Therefore, more privatization is anticipated to bring about more economic benefits, such as reduction in prices and input costs, and reduction of the burden allocated mainly on macroeconomic policies (IMF, Nov 1999).

The Pros and Cons of EMU

The EMU is now a reality and a desired long-term goal of the past is almost fully achieved. We realize that the origins of EU go back to the end of

World War II when the needs for political and economic integration in Europe were first identified.

The EMU is the final step towards total integration in Europe, with one currency (euro) being the main characteristic. Today, eleven out of fifteen EU countries are participating in the EMU, and by the end of 2002 it is anticipated that all fifteen will be included. Therefore, by 2002 one market, one currency, one Europe will exist. From this several advantages will be generated for the members as well as several disadvantages. At this point we should mention that all members would not face the consequences (both good and bad) of EMU membership in the same degree since the size of their economies and financial systems differ. Prior to the presentation of the advantages and disadvantages, we will refer to the requirements for a successful single currency area and we will try to identify how many of them the EMU satisfies.

There are three main characteristics of every single currency area. The first one is the elimination of differences in competitiveness and living standards among the participants. . The second one suggests that the government of this area should have sufficient taxation and spending power to be able to even out economic differences from member to member, due to better economic performance in some areas. The last characteristic is a continuation of the second and supports that the moving of people within EU from a depressed country to a less depressed country should become easier. Unfortunately, the EMU does not yet fulfill these requirements. Differences in competitiveness and living standards among members do exist, while due to linguistic, cultural and legal reasons the movement of people from one area to another is still difficult. However, the EMU 's main goal is the implementation of the above characteristics (Labor Euro, 1998).

Advantages of EMU Membership

The advantages that a country will enjoy by being part of EMU are the following:

- "Exchange rate stability with the euro. Exchange rate instabilities will cease to exist and fluctuations between the currencies of EMU countries will no longer occur, as all countries will have the same monetary unit (euro). As a result exchange rate risk will be eliminated for companies that export/import goods and services within EU. This stands true for Greece as Greek importers and exporters will be able to predict future markets with greater certainty. Risk elimination will lead to higher growth. More specifically in the case of Greece, exchange rate risk reduction will be of great value since Greece is an import dependent country (see figure 2).
- The euro will be a reserve currency. It is anticipated it will oust the dollar in its role as accounting unit in the international trade. Hence the EU will not be as dependent on the dollar as it now is. Furthermore, the adoption of Euro secures two main benefits for European businesses. One benefit is the cost of managing cash will

be reduced for all businesses that operate across national boundaries in Europe. In this way Greek companies that contact business within the EU zone will no longer need to convert drachmas into another currency and vice versa. Medium sized companies will be benefit more due to their usual lack of money and expertise for proper cash and foreign exchange management (Currie, 1997). A second benefit is that Greek companies will do business in a larger and more integrated market across the EU zone. Their customers will enjoy easier and quicker access to Greek products and services.

- The euro will allow interest rates, especially those in Greece, to decrease. This follows since countries who join the EU and the EMU will be forced to decrease their governments, budget deficits and remove restrictions on capital movements between members, both of which keep interest rates artificially high. As has been mentioned, this is also the case for Greece. The application of different monetary and fiscal policies by the government managed to decrease the interest rates over the last seven-year period (see figure 7). Also, more investors will be attracted to Greece.
- Tourism within EU will be facilitated, as travelers will not need to change their money when moving from one country to another. In this way the expenses of travel will be reduced and time will be saved. It has been estimated that a traveler visiting the twelve members states of the EU would loose 40% of the value of his or her money in

transaction charges alone (BBC, 1997). In addition, consumer prices may fall due to competition" (Mainero, Ricchuto, Shank, Wilmot, 1999). As far as Greece is concerned tourism is the largest and one of the faster growing sub-sectors of the economy. Tourists from all around the world, and especially Europe, visit Greece every year and are forced to exchange their national currencies for drachmas. The single currency will result in a reduction in the cost that every EU tourist pays from exchanging, for example, francs and pounds for drachmas. Consequently, more tourists within the EU zone will have the stimulus to visit Greece. Hence, tourism will further increase resulting in a parallel increase in Greece's income.

- Finally, the move to one currency will facilitate long term planning since interest rates will be standardized and cross-country price comparison will be easier to make.(Chand, 1999). This will be beneficial not only for companies but for individuals too. For example, as it has already been stated, Greek importers and exporters will avoid risky situations because of the single currency and the stability of exchange rate. They will be able to better conduct business within the EU. As far as it concerns individuals, the benefit of the single currency will be reflected in the increased capability of organizing long-term goals. Individuals will find it easier to move into or out of Greece country in search of a job or to purchase a cottage within EU by thinking in terms of the same currency.

Greece will enjoy all these anticipated benefits after entering EMU. However, due to the Single European Act, Greece already enjoys many benefits:

1. Its products and services have unrestricted access to a market of 350 million consumers (approximately total EU's member states population).
2. Agriculture benefits by the provision and regulations of Common Agricultural Policy.
3. Subsidies from the Community's funds are given to Greece for economic support.
4. Last but not least all Greeks have a right of moving and working within EU (Business Economics, 1999).

Disadvantages of EMU Membership

Single currency era will not only result in beneficial situations but it will also be accompanied by disadvantages. Such as:

- "The cost of introducing EMU /euro is a major disadvantage. This is costly since administrative and legal systems will have to adjust to the new currency, national currencies have to be taken out of circulation, teller machines will be replaced, labels will be changed and staffs will be retrained. This major drawback will affect not only Greece but also all members of EU.

- There is also the implicit cost of social adjustment to the euro. People will have to adjust to the new concept of the euro and stop converting euro prices into the previous local ones. For a time there will be confusion and uncertainty. Concerning Greeks, confusion and uncertainty will definitely be the case due to the nature of the Greek society and culture itself. We should not forget that in general Greeks fear everything that attempts to change their way of thinking and living. Therefore, getting used to a new currency will be a source of uncertainty and anxiety for Greeks. Greeks will feel a threat of not able to preserve their culture unaltered. There is hope that the Greek society will mainly focus on all the advantages of the euro and in that way the mixed emotions of fear and confusion will not prevail.
- Austerity measures are another problem. Governments will need to proceed into expense cuts so as to meet the Convergence Criteria of Maastricht. In the case of Greece, the government already exercises policies that attempt to reduce distortions to economic activity, such as interest rate payments on public dept. Thus, for Greece, the burden is more on investments, job creation and production.
- Surrender of national economic policy instruments is another disadvantage of EMU membership. With the introduction of the euro, national instruments for exchange rate policy and national interest rate policy will disappear. Countries will no longer be able to engage in independent monetary policies. They will need to put their national

budget in order to support the economy at difficult times. The same stands true for the government of Greece as well as the bank of Greece. However, the Greek public seems to have confidence in the government since the level of interest rates offered by the latter is lower than the those offered by private banks. Previously it was supposed that savers and investors trusted private banks more than the state and hence required higher interest rates to invest in government securities. "In December of 1991 this difference was 4.5% points higher that what the private banks were offering to their depositors. Today the difference is 0.4%, meaning that the trust in government and in the credibility of its economic policies has been increased in addition to the reduction in the cost of borrowing" (Christodoulakis, 1997).

- A government deficit in country A might lead to increases in interest rates in country B. 'Therefore countries need to comply with the budgetary criterion before entering EMU since after entering EMU negative changes in budget deficit will lead to severe penalties'. (Mainero, Ricchuto, Shank, Wilmot, 1999). This is why the long-term policy plan of the Greek government is focusing not only on preserving what it has already succeeded but also in increasing growth and compliance with the criteria after EMU entrance.
- All EU members either have different economic cycles or experience different stages within their cycles (boom / recession). Thus,

coordination of all members in a common economic policy will be difficult.

After all that it is obvious that EMU is a desired goal with great advantages but also undeniable disadvantages for every member.

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