

BANK OF GREECE

MONETARY POLICY

1997-1998



APRIL 1998

BANK OF GREECE

REPORT ON
MONETARY
POLICY
1997-1998



APRIL 1998

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With the enactment of Law 2548/1997 regarding "Provisions relating to the Bank of Greece" and the corresponding amendment to its Statute, the Bank of Greece has acquired a modern institutional framework, compatible with the Treaty on European Union and the Statute of the European System of Central Banks.

Under the provisions of this law, the Bank of Greece is responsible for the formulation and implementation of monetary policy, with the primary objective of ensuring price stability. This task is performed by a new body, the Monetary Policy Council, which was established under the above-mentioned law.

The new law establishes the independence of the Bank of Greece from the government and other political authorities in the performance of its tasks. At the same time, to ensure the existence of democratic accountability and transparency in the conduct of monetary policy, Article 4 states that the Bank of Greece shall submit an annual report on monetary policy for the previous and the current year to the Greek Parliament and the Council of Ministers.

Athens, April 1998

This document is the first such report submitted in accordance with the above. It consists of two main chapters. The first describes monetary developments in 1997 and assesses the monetary policy pursued in relation to the objectives set. The second reviews developments in money and foreign exchange markets in January and February 1998 as well as the drachma's entry into the Exchange Rate Mechanism of the European Monetary System in March of this year. It then presents the objectives of monetary policy for 1998 and 1999 with regard to inflation and the drachma exchange rate, projections for the evolution of basic monetary and credit aggregates, an outline of the interest rate policy of the Bank and an examination of the necessary conditions for achieving monetary stability by the end of 1999.

In accordance with the above-mentioned law, this report focuses on matters directly related to the formulation and implementation of monetary policy. As in the past, overall economic developments and the prospects for the Greek economy are analysed and assessed in the annual Report of the Governor of the Bank of Greece.

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I. Monetary Developments and Monetary Policy in 1997

1.1 Monetary policy targets and outcomes

During 1997, monetary policy was the main component of stabilisation policy and its primary objective was the further deceleration of inflation. More specifically, its target was to reduce inflation gradually to 4.5 per cent by the end of 1997 and to less than 3 per cent by the end of 1998. At the same time, it aimed at supporting the projected growth rate of economic activity in a manner compatible with its primary objective.

In attaining its final objectives in 1997, the policy pursued by the Bank of Greece focused on two intermediate targets relating to the exchange rate of the drachma and broad money (M3), which comprises currency in circulation, private deposits and repos, as well as bank bonds. In addition, the Bank continued to set monitoring ranges for certain other monetary and credit aggregates which provide useful information on the future course of inflation.

More specifically, the framework within which monetary policy was conducted last year included:

- a broadly stable exchange rate of the drachma against the other currencies comprising the European Currency Unit (ECU);
- a target of 6-9 per cent for the growth of M3, with greater emphasis on the relationship between inflation and M3 over the medium term;—
- monitoring ranges of 8-11 per cent for the growth rate of the liquidity indicator M4¹ and of 4-6 per cent for total credit expansion to the private and the public sector;
- the monitoring of the core inflation trend, enabling policy instruments to be more

readily adjusted to the anticipated course of inflation.

Monetary policy targets were broadly achieved in 1997 and it is worth noting that this was done in an economic environment characterised at times, and particularly during the last two months of the year, by considerable market pressures linked to international monetary disturbances. As shown in Table I, consumer price inflation fell to 4.7 per cent at the end of 1997, the lowest level since 1972, compared with 7.3 per cent in 1996. At the same time, the growth rate of economic activity accelerated to 3.5 per cent in 1997 from 2.7 per cent in 1996, with the expansion originating mainly from increased investment.

The drachma remained stable or appreciated against the major EU currencies, while it depreciated by 1.7 per cent against the ECU. M3 grew by 9.5 per cent, i.e. at a slightly higher rate than the upper limit of the target range. By contrast, the rate of change in M4 fell considerably short of the projected lower limit (and, in fact, was negative), while total credit expansion overshot the relevant forecast. These deviations were largely due to changes in the methods and means of financing the central government.

1.2 Inflation

The twelve-month rate of change in the consumer price index (CPI) declined, as already mentioned, by 2.6 percentage points in December 1997, compared with December 1996, while the annual rise in the average CPI

¹ M4 comprises M3 plus government paper maturing in up to one year and held by the private non-bank sector.

Table 1
Inflation, exchange rate and monetary aggregates
(Per cent change December-on-December)

	1996		1997	
	Target/forecast	Outcome	Target/forecast	Outcome
Targets				
Consumer price index	5.0	7.3	4.5	4.7
ECU/drachma exchange rate	broadly stable	-1.0	broadly stable ¹	-1.7
Money supply (M3)	6-9	9.3	6-9	9.5*
Forecasts				
Broader liquidity indicator (M4)	9-12	12.0	8-11	-1.6*
Total credit expansion	5-7	5.9	4-6	9.6*

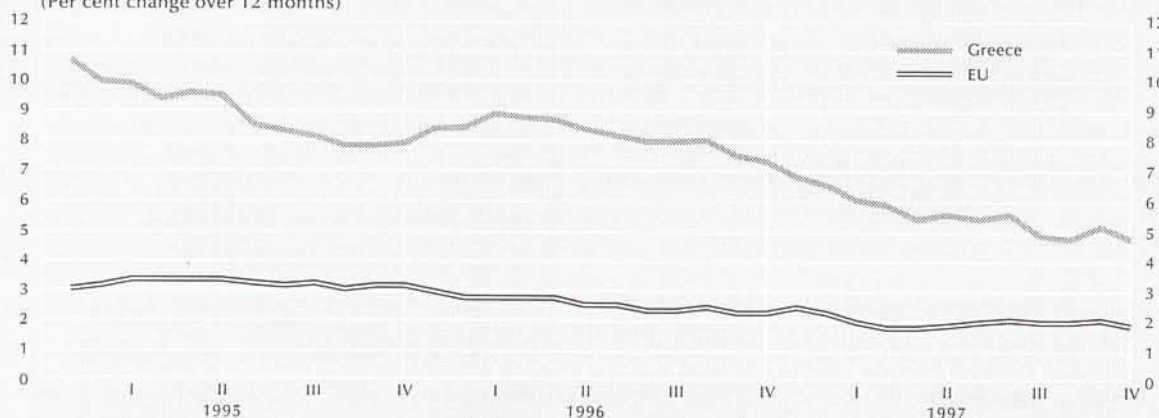
¹ The target for 1997 concerned the stability of the exchange rate against the currencies comprising the ECU and not the ECU/drachma parity (see Bank of Greece, *Economic Bulletin*, No. 9, March 1997).

* Provisional data.

Source: Bank of Greece.

Chart 1

Consumer price index in Greece and the European Union¹
 (Per cent change over 12 months)



¹ On the basis of national indices.

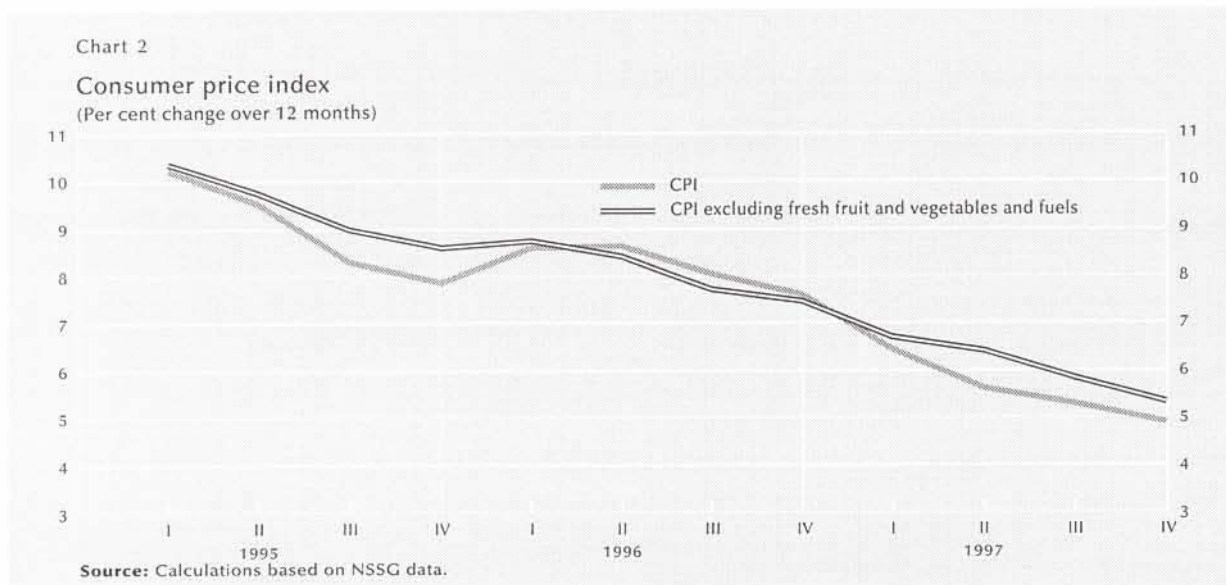
Source: National Statistical Service of Greece (NSSG) and EUROSTAT.

stood at 5.5 per cent in 1997, compared with 8.2 per cent in 1996.

The inflation differential between Greece and the European Union narrowed from 4.8 percentage points at end-1996 to 2.9 points at end-1997. According to data on the Harmonised Indices of Consumer Prices (HICPs) which are uniformly compiled to ensure comparability, the annual rate of increase in December 1997 was 4.5 per cent

for Greece against 1.6 per cent for the EU as a whole (figures for December 1996 were 6.9 and 2.1 per cent, respectively).

Core inflation also decelerated significantly. The annual rate of change in the CPI excluding fruit/vegetables and fuels — the prices of which are influenced by exogenous or conjunctural factors such as supply and demand in world markets and weather conditions — fell by 2.3 percentage points



(from 7.4 per cent in December 1996 to 5.1 per cent in December 1997).²

Factors which contributed to the deceleration of core inflation include the monetary policy pursued, the slowdown in unit labour cost growth and the decrease in the public sector borrowing requirement (PSBR) as a per cent of GDP.

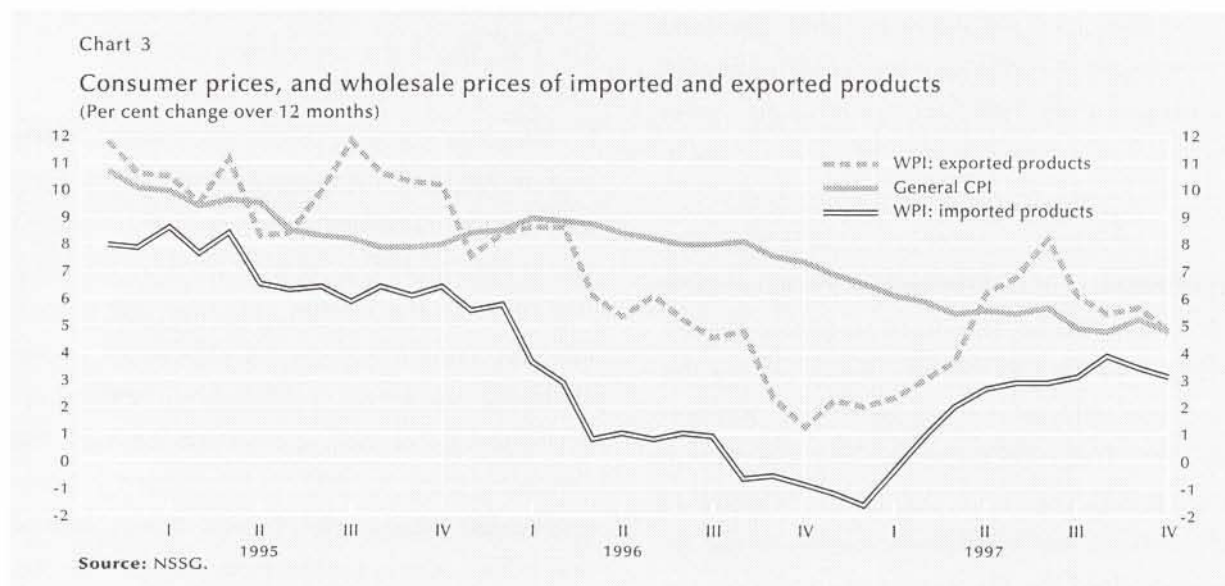
Monetary policy and, in particular, the policy of the stable drachma exchange rate, had a favourable impact on the prices of imported goods (final products and raw materials) which rose only slightly. At the same time, it dampened inflationary expectations and exerted pressure on firms to contain domestic product price rises so as to remain competitive. Indeed, the average annual rate of increase in the wholesale prices of imported goods (in drachmas) remained low (1997: 1.8 per cent; 1996: 1.6 per cent), even though it accelerated in the closing months of the year in comparison with the corresponding months of 1996.

The annual rate of increase in the wholesale prices of domestic industrial products for home

consumption fell from 6.8 per cent in December 1996 to 3.1 per cent in December 1997. This development can be attributed *inter alia* to the lower cost of borrowing for enterprises resulting from the approximately 2 percentage point decline in drachma interest rates in the ten months to October, a decline that was in line with the drop in inflation. The monetary turmoil which broke out during the last two months of 1997 contributed to a reversal of the downward trend in these rates, but the cost of funds at average annual levels remained lower than in 1996. The containment of the average cost of funds also reflects the significantly lower interest rates on foreign currency loans.

An additional factor underlying the decrease in inflation was the 2.7 percentage point slowdown in the growth rate of unit labour costs in the economy as a whole between 1996 and 1997 according to Bank of Greece estimates (a drop from 9.6 per cent to 6.9 per cent). How-

² The corresponding rate of increase in the CPI excluding food and fuels dropped by 2 percentage points to 5.8 per cent in December 1997.



ever, this growth rate remained higher than inflation, hindering the latter's faster decline (the exception was manufacturing, where it is estimated that unit labour cost growth fell to less than 5 per cent in 1997, from 7.5 per cent in 1996). The evolution of unit labour costs reflects in part the fact that average gross earnings in the public sector increased less than in 1996 (13.3 per cent, compared with 14.9 per cent in 1996), although their growth rate was still high. Primarily, however, it reflects a faster rise in productivity in the private sector, a result of much increased business investment in recent years, and, in certain cases, of a decrease in employment. In any case, nominal earnings continued to rise much faster than inflation. This increase, as mentioned above, was due to the significant rise in nominal earnings in the public sector (roughly 13 per cent, mainly because of the adoption of the new pay-scale for civil servants). The increase in private sector nominal earnings was smaller, but still high (around 9 per cent on average). These developments are similar to those of 1996. As a consequence of the deceleration of inflation, real average gross earnings in the economy as a whole grew faster than in 1996 (4.5-5 per cent

in 1997, compared with 3 per cent in 1996); they also rose faster than productivity.

The drop in the fiscal deficit also contributed to the deceleration of inflation, by lessening the expansionary effect of the deficit on total demand and prices. However, the direct effect on inflation of the pricing policy of public utilities was not, on the whole, favourable.

The decrease in inflation, as already mentioned, was achieved under conditions of accelerating economic growth and rising real incomes. Total demand is estimated to have exerted only a limited pressure, if any, on prices, given that available evidence suggests that the margins for the increased utilisation of productive capacity have not yet been exhausted and unemployment remains high. More specifically, the degree of capacity utilisation in industry, according to a survey conducted by the Foundation for Economic and Industrial Research (IOBE), decreased slightly in 1997 in comparison with 1996. This reflects increased investment in equipment over the last three years combined with the fact that manufacturing output did not increase

at a similar pace. At the same time, the total unemployment rate (10.3 per cent) remained unchanged from 1996, according to data from the National Statistical Service of Greece (NSSG).

Certain exogenous or conjunctural factors also contributed to the deceleration of inflation in 1997. In particular, the drachma prices of fuels included in the CPI fell by 2.2 per cent in the course of 1997, after rising by 8.2 per cent during 1996. This reflects the fact that the drop in world fuel prices (in US dollars) in 1997 and *ad hoc* cuts in the special consumption tax on fuels enacted by the government during the year more than offset the effect that the appreciation of the US dollar had on drachma fuel prices. Additionally, the retail price of olive oil fell by 18.2 per cent in 1997 (owing to excess supply in the world market), following a rise of 29.7 per cent in 1996 because of excess world demand.

The new system for the pricing of pharmaceuticals, introduced by the government in October, together with the abolition of certain earmarked taxes levied on pharmaceuticals in December, also contributed to the slowdown in the annual rate of inflation in December 1997, compared with December 1996.

Finally, mention must be made of a technical factor. To achieve uniformity in the statistical treatment of goods in the CPI, it was decided to regard heating oil as a seasonal good, starting from April 1997. The new methodology affected only the average annual rate of inflation for 1997, which at 5.5 per cent turned out to be half a percentage point lower than it would have been under the old method.³ This change, however, did not affect the twelve-month rate of inflation for December 1997, which was 4.7 per cent under both methods.

1.3 The drachma exchange rate

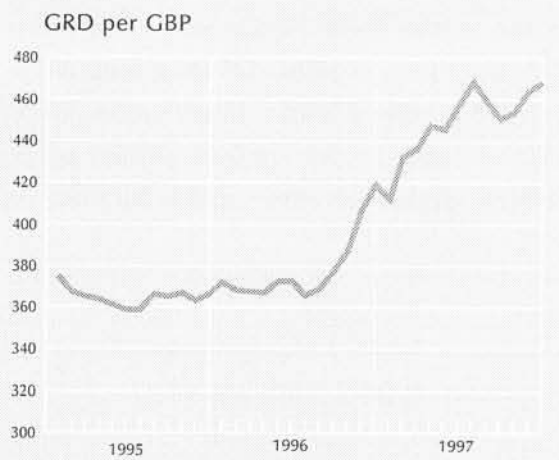
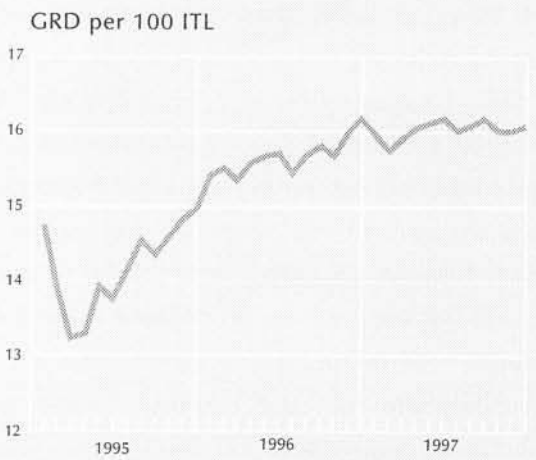
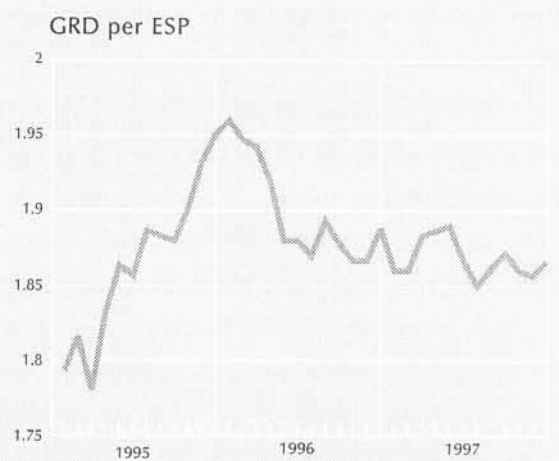
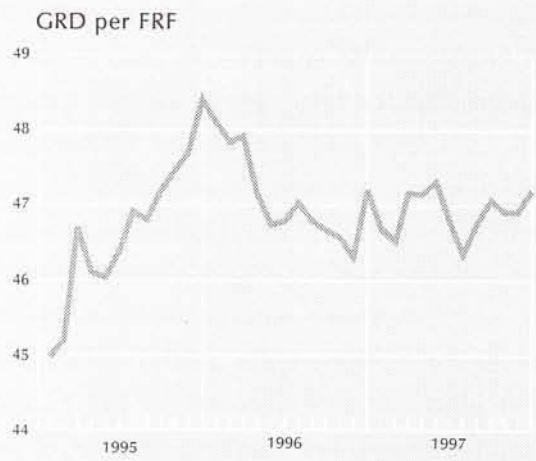
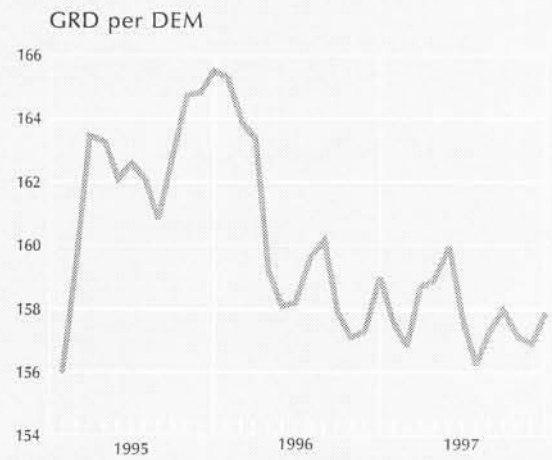
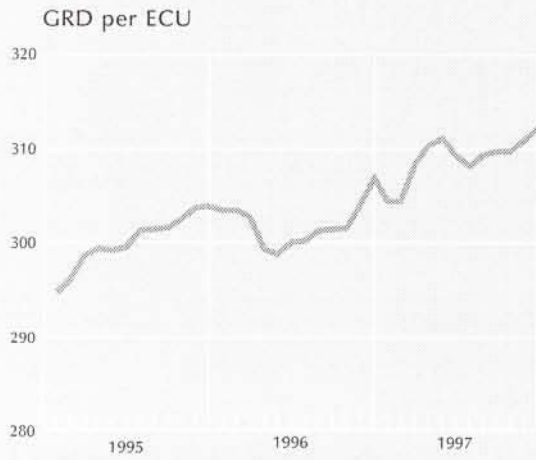
Exchange rate policy, as already noted, continued to be the main component of the anti-inflationary monetary policy in 1997. Interest rate policy, as well as interventions by the Bank of Greece in the foreign exchange and money markets, contributed to the attainment of the exchange rate target. Indicatively, the drachma appreciated by 0.7 per cent against the Deutsche mark in 1997 and remained virtually unchanged against the French franc. Against the other currencies participating in the Exchange Rate Mechanism (ERM), the drachma appreciated by 0.2 to 2.8 per cent (see Table 5 in the Statistical Appendix). The drachma depreciated against the pound sterling by 10.6 per cent, in line with the substantial appreciation of sterling against all European currencies. As a result, the drachma also depreciated by 1.7 per cent against the ECU (1996: 1 per cent). The effective drachma exchange rate (weighted on the basis of transactions with Greece's main trading partners, including those outside the EU) fell by 1.5 per cent in 1997, compared with a rise of 0.4 per cent in 1996.

There were considerable net inflows of foreign currency in the first quarter of 1997. Hence, the drachma remained appreciated against the ECU until end-March, compared with end-1996 levels. The highest rate of appreciation, 1.3 per cent, was recorded in mid-January. As a result of outflows of foreign currency during the period of turmoil in the Central European and SE Asian markets, the drachma depreciated against the ECU in April and May and by the end of May was 1.3 per cent lower than at the

³ See also Bank of Greece, *Economic Bulletin*, No. 10, December 1997.

Chart 4

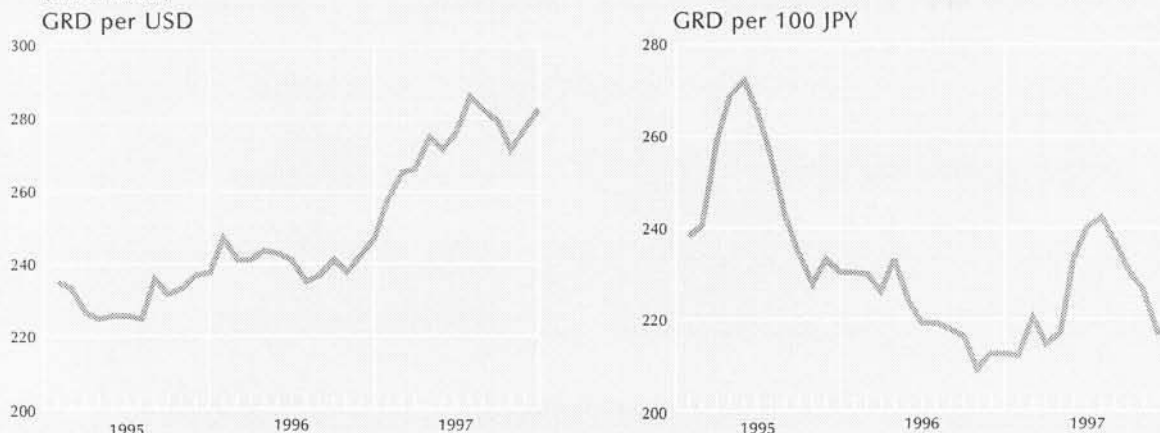
Exchange rates of the drachma against the major EU currencies
(End of month)



Source: Bank of Greece.

Chart 5

Exchange rates of the drachma against the US dollar and the Japanese yen
(End of month)



Source: Bank of Greece.

end of 1996. Subsequently, it remained roughly stable until October 1997, at a level that was 0.8 per cent lower relative to its end-December 1996 level.

During the periods of monetary turmoil in the second half of July 1997 and more particularly at the end of October, the drachma came under strong pressure and there were outflows of foreign currency. During these periods, the Bank of Greece intervened substantially in the foreign exchange market, as well as in the money market, to contain the fluctuations of the drachma against other European currencies. On the whole, these fluctuations were somewhat larger than in 1996, reflecting a modification of the central bank's intervention policy, which widened the range within which drachma exchange rates could fluctuate in 1997.

1.4 Money supply and liquidity

The rate of growth of broad money (M3) rose to 9.5 per cent in 1997, slightly above the

upper limit of the annual target range (6-9 per cent). It was nonetheless characterised by considerable volatility over the year. In particular, the twelve-month growth rate of M3 rose to high levels at the beginning of the year (around 13.5 per cent) and accelerated further from April onwards, reaching a maximum of 17.9 per cent in October. This development was associated with the restructuring of investors' portfolios, as Treasury bills maturing between January and October 1997 were partly replaced by other assets, mainly deposits, an M3 component. This trend was due to a number of factors. First, interest rates on government securities dropped faster than those on deposits, thereby reducing the yield differential. Second, as from 1 January 1997, a 7.5 per cent tax was imposed on interest from government securities, further squeezing the net yield differential between government securities and deposits. Third, Treasury bill issues were smaller in number during the year in accordance with debt management policy, which aimed *inter alia* at extending average debt maturity. Finally, the volume of transactions on the Athens Stock Exchange grew considerably, leading to increased holdings of liquid assets.

Chart 6

Money supply (M3) and liquid assets (M4)
(Per cent change over 12 months)

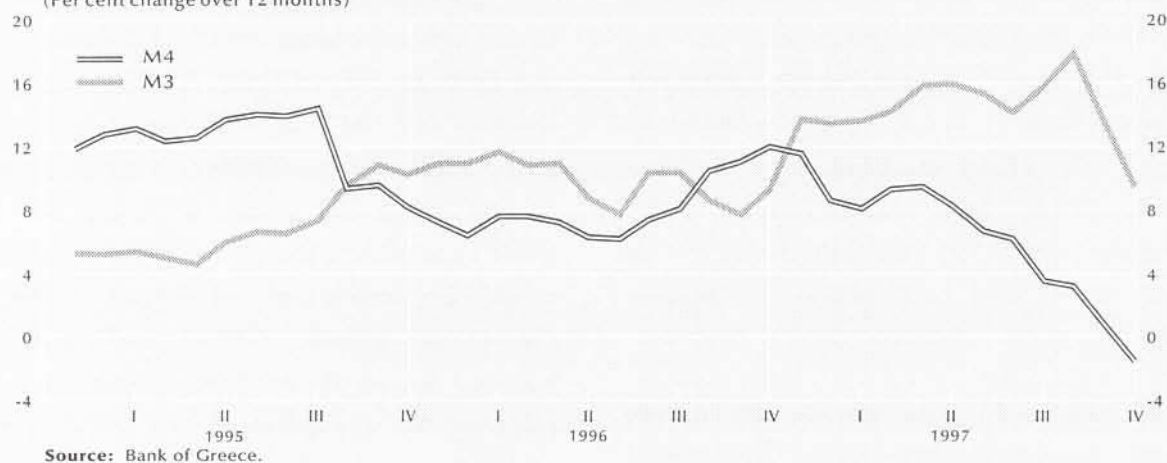


Table II

Monetary aggregates

(Changes in billion drachmas and per cent change in outstanding balances)

	Year			
	1994	1995	1996	1997*
1. M0 (Currency in circulation)	176 (11.6%)	175 (10.4%)	78 (4.2%)	244 (12.6%)
2. Private deposits	2,546 (24.6%)	1,939 (15.0%)	2,065 (13.9%)	1,544 (9.1%)
2.1 Sight deposits	394	180	321	211
2.2 Time and savings deposits	2,152	1,759	1,744	1,333
3. M1 (M0 + private sight deposits)	570 (25.6%)	355 (12.7%)	399 (12.7%)	455 (12.8%)
4. Repos	-1,576	-222	-7	-47
5. Bank bonds	135	-267	-511	61
6. M3 (= 1 + 2 + 4 + 5)	1,281 (8.8%)	1,625 (10.3%)	1,625 (9.3%)	1,802 (9.5%)
7. Private investment in Greek government securities with a maturity of up to one year	1,302	115	1,122	-2,225
8. M4 (= 6 + 7)	2,583 (13.9%)	1,740 (8.2%)	2,747 (12.0%)	-423 (-1.6%)
9. Total private investment in Greek government securities	1,622	2,088	3,113	650

* Provisional data.

Source: Bank of Greece.

In the last two months of 1997, however, the twelve-month growth rate of M3 slowed considerably and, as pointed out above, was con-

tained to 9.5 per cent by the end of the year. The slowdown was related to the interest rate policy and money market interventions of the

Bank of Greece during this period, which resulted in the movement of funds from M3 components to government securities, financial derivatives and mutual fund units. In this respect, it is worth noting that the total assets of money market mutual funds increased by roughly 930 billion drachmas over the two-month period November-December 1997, compared with 2,150 billion drachmas for the whole of 1997 and 1,040 billion drachmas for 1996.

In contrast to M3, the growth rate of the broader liquidity indicator M4 throughout 1997 remained at levels considerably lower than that of end-1996. Specifically, the twelve-month growth rate of M4 fluctuated from February through June 1997 within the range projected for 1997 (8-11 per cent), gradually slowing further in the second half of the year, to stand at -1.6 per cent by the year-end. This evolution of M4 was caused by the fact that part of the Treasury bills maturing in the course of the year was not substituted with deposits but with government securities of a maturity longer than one year or with other financial products. It should be noted that private investment in government paper maturing in up to one year decreased by 2.2 trillion drachmas in 1997, compared with an increase of 1.1 trillion in 1996. As mentioned above, this development was related to the government's policy of extending the average maturity of public debt in 1997. This policy involved offering new types of government paper, such as drachma-denominated zero-coupon bonds and fixed interest rate bonds, which are not components of M4.

1.5 Credit expansion

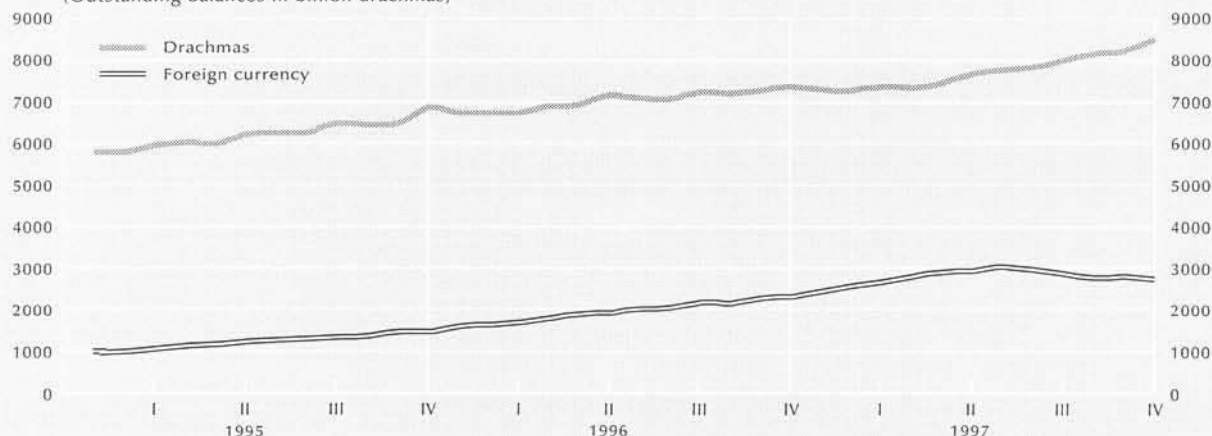
Total credit expansion accelerated to 9.6 per cent in 1997, compared with 5.9 per cent in

1996, because of a correspondingly faster increase in bank credit to the public sector. More specifically, credit expansion followed a steady upward course from the beginning of the year to the end of October, when it reached 13.2 per cent. This can be attributed to the substantial acceleration of credit expansion to the public sector, while the rate of credit expansion to the private sector remained roughly unchanged until the end of October. In the last two months of 1997, total credit expansion slowed down considerably, thereby reversing the upward trend and reducing the twelve-month growth rate to 9.6 per cent by the end of 1997, as already mentioned. This development was related to bank sales of government securities to the public, following the significant increase in the yields that prevailed in the secondary markets and in the financial derivatives markets after the monetary turmoil that broke out at the end of October 1997 and the measures taken by the Bank of Greece to deal with it.

Credit expansion to the public sector rose to 6.4 per cent in 1997, compared with 1 per cent in 1996. This is accounted for by the fact that, even though the PSBR was much lower than in 1996, a considerably smaller share of it was financed by the non-bank private sector. More specifically, central government borrowing requirements on a cash basis fell to 2,581 billion drachmas in 1997, i.e. 33 per cent less than in 1996. In spite of this decrease, however, only 25 per cent of central government borrowing requirements were covered by the non-bank private sector, compared with 80 per cent in 1996 and 68 per cent in 1995. Consequently, the percentage covered by the banking system and foreign sources increased. Thus, the way in which the PSBR was financed in 1997 contributed more than in previous years

Chart 7

Bank lending in drachmas and foreign currency
(Outstanding balances in billion drachmas)



Source: Bank of Greece.

to the creation of liquidity, accounting for 75 per cent of the increase in M3, against 12 per cent in 1996.

Credit expansion to the private sector decelerated to 16.3 per cent in 1997 from 17 per cent in 1996. The twelve-month rate of increase in bank lending to the private sector was around 17.5 per cent until end-October 1997. In November and December 1997, however, it slowed slightly as a result of higher interest rates on drachma loans, as well as uncertainty in the foreign exchange markets after the monetary turmoil at end-October. It should be noted that, because of the appreciation of the US dollar and the Japanese yen and the foreign exchange turmoil at the end of May 1997, foreign exchange loans were substituted with drachma loans from April 1997 onwards. As a consequence, the outstanding balance of loans in foreign exchange began to decrease in August and in the five months through to December 1997 fell by roughly 290 billion drachmas.

As far as the sectoral breakdown is concerned, a slowdown was recorded in bank credit to

industry, housing and consumers, although credit expansion to the last two sectors remained relatively high. Financing of other sectors of the economy (small-scale industry, farming, domestic trade) accelerated (see Table 10 in the Statistical Appendix).

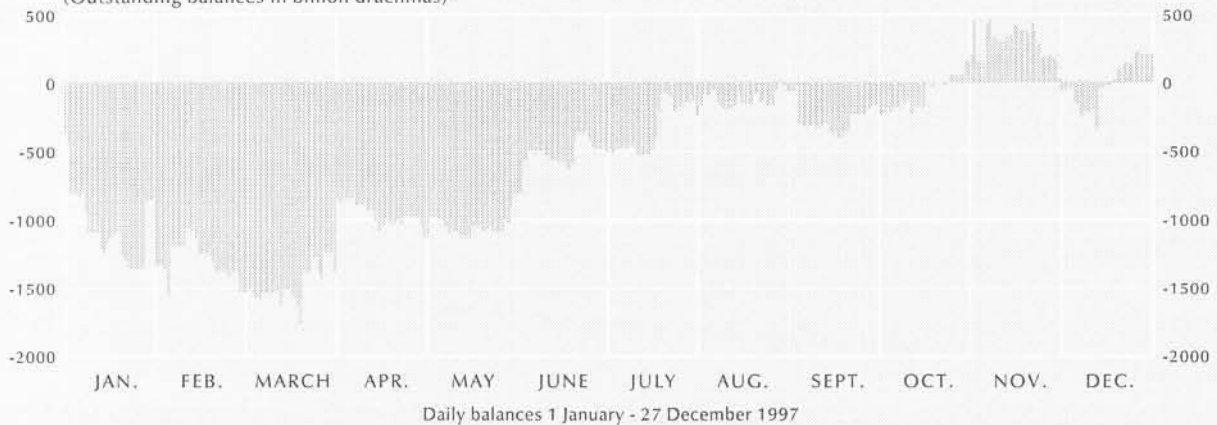
1.6 Interest rates and the interbank money market

Throughout 1997, the primary means used by the Bank of Greece to achieve the final and intermediate targets of monetary policy was interest rate policy.

Interbank money market

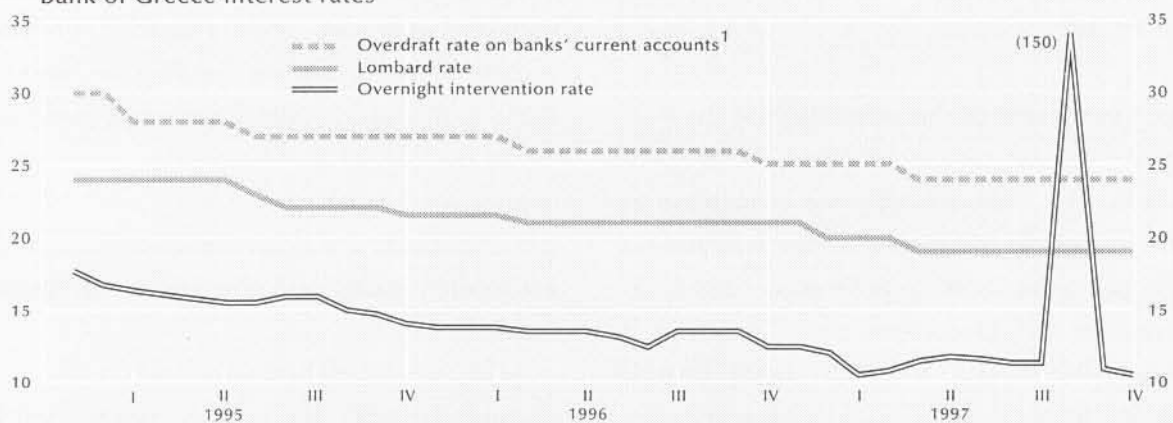
In the first five months of 1997, the interbank money market was characterised by excess liquidity, owing to increased capital inflows at the beginning of the year as well as an acceleration of credit expansion to the public sector. During this period, the Bank of Greece intervened extensively in the interbank market, absorbing liquidity in order to maintain interest rates at levels consistent with the anti-

Chart 8
Bank of Greece interventions in the interbank market
(Outstanding balances in billion drachmas)*



* Net absorption (-) or supply (+) of liquidity.
Source: Bank of Greece.

Chart 9
Bank of Greece interest rates



¹ A daily surcharge of 0.4 per cent as from 31 October 1997 and 0.2 per cent as from 29 December 1997 applies to further increments to the debit balances of banks' current accounts with the Bank of Greece.

Source: Bank of Greece.

inflationary target. It should be noted in this respect that, until the end of March, the daily outstanding balance of liquidity absorbed by the Bank of Greece amounted on average to some 1,300 billion drachmas (see Chart 8). At the same time, the Bank of Greece introduced certain changes with respect to the conduct of monetary policy in order to enhance its effectiveness. In particular, tenders for the acceptance of deposits or repos were reactivated in mid-February, while a two-tranche standing facility for deposits was established at the end

of March 1997, to allow interbank rates to be influenced more directly by market conditions.

This standing facility sets the lower limit of the range within which interbank rates can fluctuate and, at the same time, allows interest rates to be more responsive to changes in liquidity conditions, thus discouraging the inflow of speculative capital. Indeed, in April and May 1997, there was a considerable decrease in the amount of funds absorbed by the Bank of Greece from the interbank market. From Janu-

BOX 1

Monetary policy instruments

The existing monetary policy framework of the Bank of Greece comprises a broad array of instruments to influence indirectly the total liquidity of the economy and interest rates. The three broad categories of instruments are: standing facilities, open market operations, and minimum reserves.

(i) Through "standing facilities", liquidity is provided or absorbed on the initiative of banks. They comprise a deposit facility and two credit facilities.¹ Under the deposit facility, banks can deposit their excess daily liquidity with the Bank of Greece. There are two tranches, each with a different interest rate. More specifically, the first tranche, which has a higher interest rate (11.5 per cent as from 23 April 1998), comprises deposits by all banks up to a global ceiling currently set at 300 billion drachmas. Each bank has a quota dependent on its domestic market share. The second tranche, with a lower interest rate (9.75 per cent as from 23 April 1998), comprises any amount in excess of each bank's quota and is subject to no further quota.

Credit facilities include a lombard facility (i.e. credit granted with government securities as collateral) and an overdraft facility, to be used only in exceptional circumstances. Through the lombard facility, banks can obtain central bank liquidity at a higher interest rate (19 per cent as from 31 March 1998) than that prevailing in the interbank market. Funds are available up to a global ceiling of 150 billion drachmas, which is allocated to individual banks on the basis of own funds. Banks use the facility to deal with temporary liquidity shortages. Banks facing exceptionally

high liquidity needs, over and above the amounts available through the lombard facility, can raise additional funds through overdrafts on their current accounts with the central bank. The interest rate, however, is even higher (22 per cent as from 31 March 1998), and borrowing has to be collateralised by holdings of Greek government securities.

(ii) Open market operations include weekly tenders for deposits or repurchase agreements with a maturity of 14 days. These tenders are typically held every Wednesday and are the main instrument for influencing liquidity and interest rates in the interbank market, although in special circumstances interventions on different days and for different maturities are not ruled out. Depending on monetary conditions, tenders are either at fixed or variable rates. In addition, the Bank of Greece may occasionally conduct swap operations, as well as a limited volume of sales and purchases of government paper.

(iii) To comply with the reserve requirement, banks must deposit 12 per cent of their deposits and other liabilities in drachmas and foreign currency with the Bank of Greece. Only half of this amount is remunerated (at a rate of 11 per cent). This instrument aims largely at absorbing liquidity which is structural in nature. Reserve requirements incorporate averaging provisions, whereby banks can use their reserve holdings to meet temporary liquidity shortages, provided that the reserve requirement is met on average during a maintenance period of one month.

¹ The standing facility of credit to banks by the Bank of Greece via the rediscounting of bills of exchange and promissory notes, which had not been used for a long time, was abolished with effect from 10 April 1998.

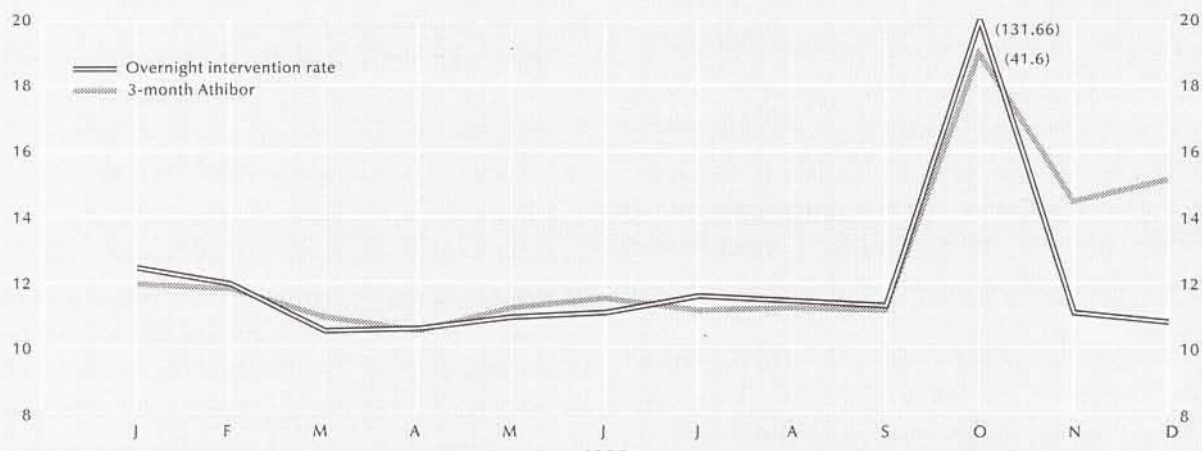
ary to May 1997, the interbank overnight rate, which is influenced directly by the intervention policy of the Bank of Greece, fell by about two percentage points, i.e. by as much as the drop in inflation over the same period.

Capital outflows, which accounted for a further

decrease in liquidity in the interbank market and a rise in interest rates, were recorded at the end of May and in the course of July. More specifically, interbank rates from June to August stood at early-1997 levels, even though interest rates on the two tranches of deposits were not raised. In September and early October, the

Chart 10

Interbank market rates



Source: Bank of Greece.

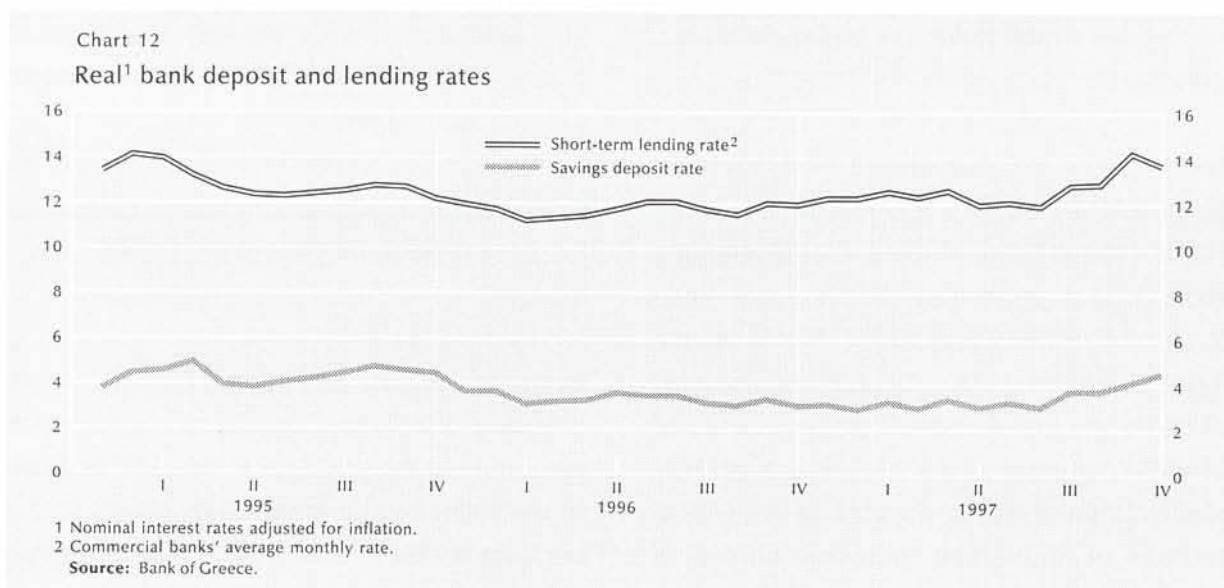
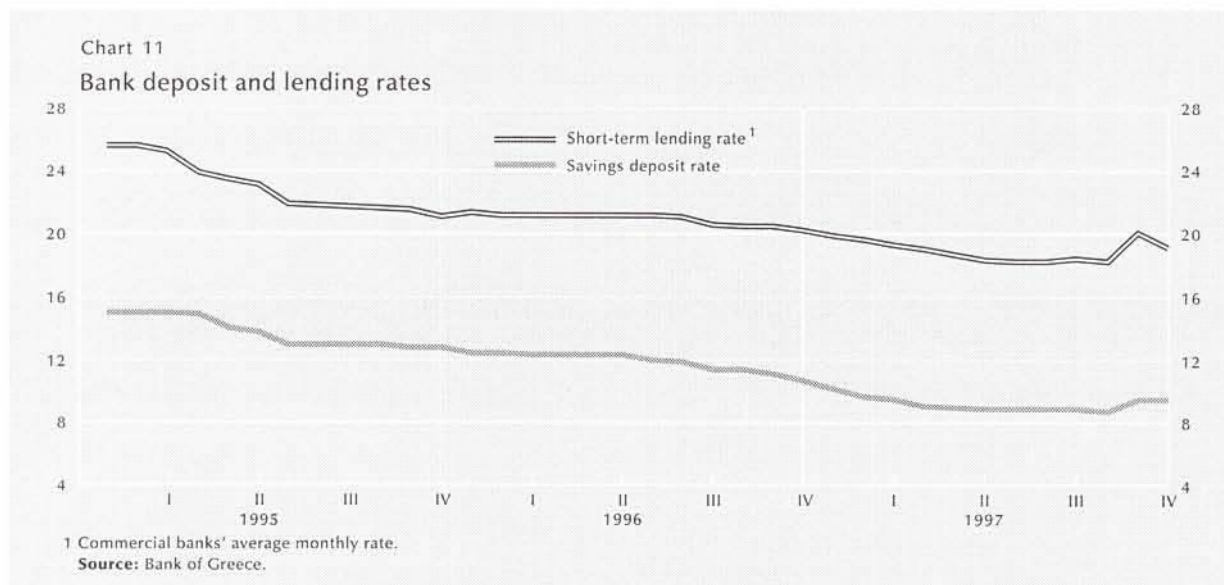
overnight interbank rate averaged 11 per cent, down from 11.7 per cent in the three months from June to August and 12.8 per cent in December 1996. Thus, over the first three quarters of 1997, this rate declined by 1.8 percentage points, i.e. by less than the drop in inflation over the same period (2.4 percentage points). The policy pursued by the Bank throughout this period consisted of keeping the decrease in short-term interbank rates, which are more sensitive to central bank interventions, smaller than the drop in inflation, so as to retain the anti-inflationary stance of monetary policy. In this context, the Bank of Greece reduced the interest rate on the first tranche of the standing facility by one percentage point from end-March to mid-October, while inflation fell by 1.3 per cent over the same period.

As already mentioned, the Greek foreign exchange market came under strong pressure, with capital outflowing at the end of October 1997 after the outbreak of monetary turmoil in the Asian markets. To support its exchange rate policy, the Bank of Greece raised intervention rates by imposing a surcharge of 0.4 per cent

per day on the increase in the debit balances of commercial banks' current accounts with the central bank. This is equivalent to an annual interest rate of 170 per cent. The move discouraged borrowing in drachmas from the Bank of Greece, while the Bank's interventions in the drachma and foreign exchange markets put an end to capital outflows and eased the pressure on the drachma. At end-November and into early December 1997, the overnight interbank rate was almost back to the level that held before the outbreak of monetary turmoil (around 11 per cent). The rates on deposits of longer maturities gradually decreased as well, but remained significantly higher than their mid-October 1997 levels.

Bank rates

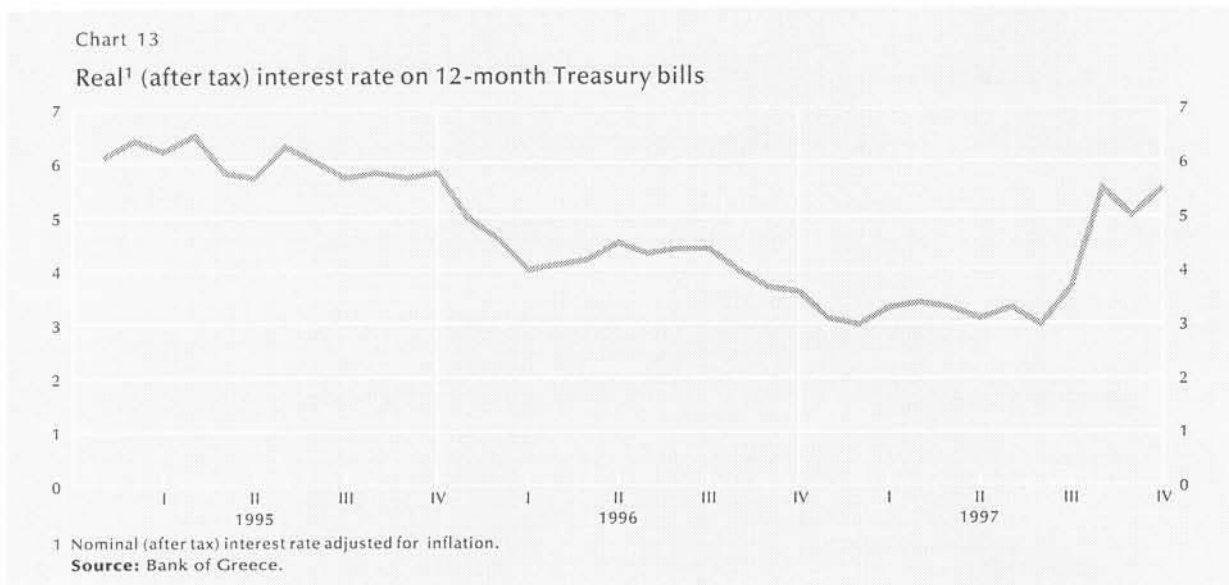
Until October 1997, bank deposit and lending rates followed a downward course which by and large went in parallel with the drop in inflation; only some bank rates fell at a slower pace. As a result, real interest rates (based on headline inflation over the last twelve months) remained roughly at their end-1996 levels or



rose only slightly, by around half a percentage point. The spread between deposit and lending rates remained virtually unchanged. In particular, it is worth noting that both the short-term lending rate and the savings deposit rate fell by two percentage points in the ten months to October 1997.

The downward trend in bank rates was reversed in the last two months of 1997, owing to the monetary turmoil that broke out at end-October. Greater changes were recorded in the

rates on time deposits of up to one month, which increased by as much as 10 percentage points during the period of turmoil. As soon as pressure in foreign exchange markets subsided, these rates decreased considerably, although not to pre-turmoil levels. The rates on other categories of deposits, as well as lending rates, increased, albeit with some delay, and by end-1997 were 1.7 percentage points higher than at end-October. The rise in savings deposit rates and short-term lending rates was smaller (0.8 and 0.9 percentage point, respectively).



Interest rates and yields on government securities

Interest rates on government securities followed a downward course in the first three quarters of 1997 and, at the end of September, stood 1.7-2.3 percentage points lower than in December 1996. Specifically, the 12-month Treasury bill rate, after successive reductions mainly in the first months of the year, levelled off at 9.5 per cent in the August through September period, compared with 11.2 per cent at the end of 1996. The monetary turmoil of October 1997 also affected the market for government paper, resulting in a drop in prices and an increase in yields during November and December. The yield in the secondary market for the 10-year bond issued in June 1997 with a fixed interest rate of 8.8 per cent, which is the reference rate for the Maastricht convergence criteria, rose from 9.3 per cent at the end of October to 11 per cent in mid-November. It then decreased slightly and, in December, ranged from 10.1 to 10.9 per cent. In the last two months of 1997, there were no new issues of drachma-denominated government bonds. Instead, the public sector raised funds from

the domestic markets through the issue of Treasury bills and one- and three-year bonds with an ECU clause.

1.7 Assessment of monetary policy in 1997

From the above analysis, it follows that the objective of a further deceleration of inflation was attained in 1997. Core inflation declined substantially by 2.3 percentage points to 5.1 per cent at the end of 1997, while economic activity accelerated, reflecting mainly an increase in investment. The fall in headline inflation as measured by the CPI was a little more pronounced, owing to certain special factors. Economic activity grew faster than in other EU countries. Consequently, in addition to the nominal convergence achieved as a result of the fall in inflation and the containment of the fiscal deficit, progress was also made in 1997 with real convergence.

Monetary policy contributed decisively to the deceleration of inflation through a strategy based on intermediate targets which were

attained to a satisfactory degree. In particular, the drachma exchange rate remained roughly stable against most other European Union currencies (except sterling). The growth rate of broad money (M3) was contained at 9.5 per cent between the beginning and the end of 1997, compared with a target range of 6-9 per cent. Fiscal policy and the evolution of unit labour costs also had a favourable effect on inflation. The general government deficit fell to 4 per cent of GDP in 1997, from 7.5 per cent in 1996, while unit labour costs in the economy as a whole slowed from 9.6 per cent in 1996 to 6.9 per cent in 1997. Thus, the monetary and fiscal policy mix was more appropriate in 1997 than in 1996. However, nominal earnings, particularly in the public sector, continued to rise at a rate considerably higher than the policy objective, thereby preventing a faster drop in inflation and adversely affecting the competitiveness of Greek products and services. Moreover, delays in implementing structural reforms impeded a permanent improvement in productivity, thus hampering the deceleration of inflation and the strengthening of competitiveness.

Interest rate policy was the principal means used by the Bank of Greece in implementing its anti-inflation strategy. From the beginning of 1997 until almost the end of October, the Bank's money market intervention rates decreased in parallel with the drop in inflation, bringing about a fall in the cost of capital for both the public and the private sector. The monetary turmoil at the end of October, however, caused a reversal of the downward course of interest rates, which, by the end of 1997, had increased by roughly two percentage points.

The monetary policy targets as regards inflation, the exchange rate of the drachma and the

money supply (M3) were broadly attained in 1997. Total credit expansion, however, accelerated and overshot its monitoring range. This development was primarily due to the fact that central government borrowing requirements were financed to a far lesser extent than in previous years by the non-bank private sector, being met instead by increased borrowing from the banking system and foreign sources. The acceleration of credit expansion led to considerable growth in broad money until October 1997, thereby hindering the conduct of monetary policy and negatively affecting the balance of payments. More specifically, the current account deficit, on a settlements basis, amounted to \$4.8 billion or 4 per cent of GDP in 1997, compared with \$4.5 billion or 3.7 per cent of GDP in 1996. The current account deficit was also affected by the faster growth of the Greek economy in comparison with other EU countries and by the cumulative loss of competitiveness.

The drachma came under strong pressure during the last two months of 1997. The monetary turmoil in Southeastern Asia, with its adverse repercussions on the foreign exchange and capital markets in several emerging economies, fuelled the pressure that was exerted on the drachma in October 1997. The extent and duration of the pressure, however, reflected certain characteristics and weaknesses of the Greek economy which made it more vulnerable than other EU countries to market concerns and expectations. The factors behind the market pressures included: the current account deficit and the loss of competitiveness, the external debt of the public and private sectors, as well as market expectations regarding the entry of the drachma into the Exchange Rate Mechanism (ERM) of the European Monetary System (EMS) accompanied by an adjustment

of the exchange rate of the drachma. The Bank of Greece dealt with these pressures effectively and supported its exchange rate policy both by

raising interest rates and by making extensive interventions in the money and foreign exchange markets.

II. Monetary Policy Objectives and Framework in 1998

II.1 Developments in January-February 1998

In early January 1998 the exchange rate of the drachma came under renewed pressure and capital outflows occurred. The Bank of Greece responded by increasing the lombard rate and intervention rates in the interbank market during the first half of January. In the two months that followed there were occasional inflows of funds, and for the most part, pressures on the drachma lessened, thus enabling a gradual fall in the Bank's money market intervention rates. The room for a further decline in interest rates was limited, however, as a series of events, such as the rekindling of the monetary crisis in Asia and market expectations that the drachma would enter the Exchange Rate Mechanism (ERM) of the EMS in May 1998 and would be devalued, prevented money market conditions from returning to normal (see Chart 14). As a result, interbank market rates remained relatively high right up to the time when the drachma joined the ERM in mid-March.

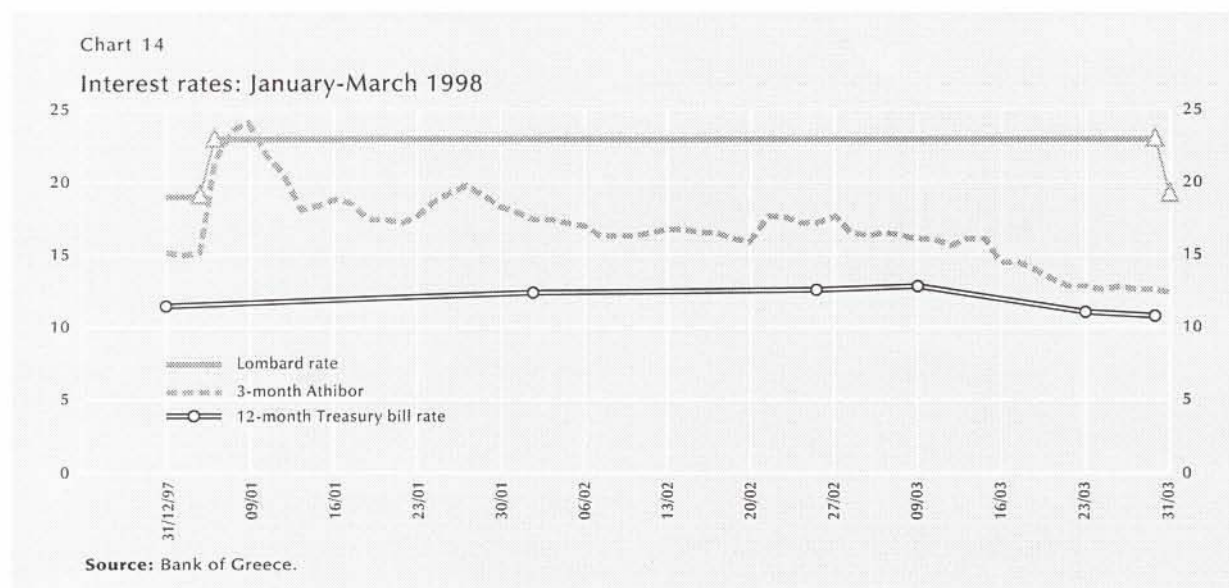
As expected, interbank rates affected bank

lending rates and interest rates on government paper issued during this period. In particular, the average interest rate on short-term bank credit rose by half a percentage point in February 1998, while the average rates on the twelve-month Treasury bills issued in early January, February and March 1998 were 11.4, 12.4 and 12.9 per cent, respectively.

Balance of payments data published in the first two months of 1998 showed a steady improvement in the current account deficit, while foreign exchange reserves increased by \$1.8 billion and inflation recorded a further fall to 4.3 per cent in February 1998 from 4.7 per cent in December 1997. Consequently, by 13 March, market conditions had stabilised to a certain extent, but interest rates remained at high levels.

II.2 Entry of the drachma into the Exchange Rate Mechanism (ERM)

Effective from 16 March 1998, the drachma joined the ERM, in which the currencies of all EU member states participate with the excep-



BOX 2

The Exchange Rate Mechanism of the European Monetary System

The European Monetary System (EMS) was established in 1979 with the primary goal of creating a zone of monetary stability in Europe. A key component of the EMS is the Exchange Rate Mechanism (ERM), which aims at reducing exchange rate fluctuations among participating currencies. At present, all EU currencies, except the pound sterling and the Swedish krona, participate in the ERM.

Around the bilateral *central rates* of participating currencies, which establish a grid as they connect each pair of currencies, fluctuation margins of ± 15 per cent have been in operation since August 1993. The exception to this is the Deutschmark/Dutch guilder exchange rate which, under a bilateral agreement between the two countries, may fluctuate within a narrower band (± 2.25 per cent). In practice, however, over the last two years, all ERM currencies have traded close to their central rates and only occasionally have recorded wider fluctuations. On the basis of 10-business-day moving averages, fluctuations have not exceeded 3.6 per cent, with the exception of the Irish pound.

To ensure that the exchange rate always remains within the fluctuation band, when two currencies have reached the floor and the ceiling, respectively, of their fluctuation margins, the two central banks involved are required to intervene up to an unlimited amount if necessary (intervention at the limits). These interventions can be financed without limit from the *Very Short-Term Financing Mechanism (VSTF)*.

It is also possible to intervene in the foreign exchange markets to finance these interventions via the VSTF even if the exchange rate has not reached the outer limits of the fluctuation band (intra-marginal intervention). It should be noted, however, that the Basle-Nyborg agreement (1987) suggested that, in order to discourage speculation, it is sometimes advisable to let the exchange rate use the whole width of the fluctuation bands. Moreover, it was acknowledged that changes in interest rates are a powerful means of supporting the exchange rate.

Under the Maastricht Treaty, an essential prerequisite for the adoption of the euro by any member state is participation in the ERM without "severe tensions". More specifically, Article 109j of the Treaty requires "the observance of the normal fluctuation margins provided for by the exchange-rate mechanism of the European Monetary System, for at least two years, without devaluing against the currency of any other Member State".

Aside from being one of the requirements under the Maastricht Treaty for joining the single currency area, participation in the Exchange Rate Mechanism has been proven to facilitate the fight against inflation, to help establish macroeconomic stability and to promote the functioning of the Single European Market, by averting sharp and arbitrary changes in competitiveness.

In Stage Three of Economic and Monetary Union (EMU), a new mechanism will succeed the present ERM. ERM-II will have the same main features, although the focus will be on the euro and the European Central Bank. In the Florence summit (1996) it was agreed that, in Stage Three of EMU, those member states which do not adopt the euro from the start are expected, though not obliged, to join ERM-II.

tion of the pound sterling and the Swedish krona. Participation in the ERM and the maintenance of exchange rate stability for at least two years are a prerequisite for accession to monetary union, as laid down in the Maastricht Treaty.

In addition to the fulfilment of the Treaty's requirement, the incorporation of a currency into the ERM implies in principle that economic policy is conducted in a more stable environment with fewer sources of possible disturbances. The structure and the functioning of

BOX 3**Depreciation of the drachma and appreciation of the ECU upon entry of the drachma into the ERM**

	12 March	16 March	Depreciation (-)/appreciation (+)
Drachma exchange rate	A = 1/313.05 ECU	B = 1/357 ECU	$[(B/A)-1] \times 100 = -12.3$ per cent
ECU exchange rate	A' = 313.05 drs	B' = 357 drs	$[(B'/A')-1] \times 100 = +14$ per cent

this mechanism are characterised by the coordinated management of potential pressures on any currency, while at the same time they impose discipline and constraints on the conduct of economic policy in participating countries, in order to avoid disturbances to the smooth operation of the system. This discipline, of course, enhances the credibility of the economic policy being pursued and therefore increases its effectiveness. This is achieved, in particular, through increased market confidence, expressed mainly in a curtailment of inflationary expectations and lower interest rates, as well as through favourable effects on the decisions of the social partners (employers-employees). Countries are thus compensated for their commitment to harmonise their policies so as to promote medium-term convergence between their economies and those of their ERM partners. Besides, the fact that the Treaty requires not only the maintenance of exchange rate stability in general but also participation in the ERM in particular aims at strengthening the convergence process and facilitating the transition to the irrevocable fixing of the exchange rates which will apply when countries join monetary union.

The drachma joined the ERM at a central rate of 357 drachmas per ECU. In relation to the rate of 313.05 drachmas per ECU at the fixing session of 12 March 1998, the agreed central rate implied a devaluation of the drachma by 12.3 per cent and a revaluation of the ECU by

14 per cent (see Box 3). The bilateral central rates of the drachma against the other ERM currencies are shown in Table III.

The entry of the drachma into the ERM at the above rate was decided after consultations with the other ERM members, as provided for in the agreement relating to the accession of countries to the ERM. The conclusion reached was that the new exchange rate was appropriate for offsetting the loss of competitiveness of Greek goods and services which had resulted from the real appreciation of the drachma in recent years. At the same time, it will contribute to the creation of suitable conditions that will sustain high rates of economic growth. In determining the central rate, consideration was also given to the need to ensure exchange rate stability for at least two years before joining monetary union, as required by the Treaty. The central rate of the drachma is deemed consistent with the maintenance of external balance after Greece's participation in the euro area in 2001.

The timing of the ERM entry was influenced by various factors. Since it was well-known that the government's intention was for Greece to join monetary union in 2001, markets initially expected that the drachma would enter the ERM towards the end of 1998 or early in 1999 at the latest. Subsequently, market speculation about the likely date of entry seemed to focus on early May of this year, when the irrevocable fixing of bilateral exchange rates for the curren-

Table III
Central parities of the drachma

100 BEF/LUF	= 875.335 drs	1000 ITL	= 182.365 drs
100 DKK	= 4,733.13 drs	100 NLG	= 16,023.4 drs
100 DEM	= 18,054.2 drs	100 ATS	= 2,566.15 drs
100 ESP	= 212.222 drs	100 PTE	= 176.129 drs
100 FRF	= 5,383.11 drs	100 FIM	= 5,938.86 drs
1 IEP	= 448.355 drs	1 ECU	= 357 drs

Source: European Commission.

cies in the first group of countries to enter the monetary union would be decided. Not surprisingly, as the perceived date of ERM entry was approaching, market decisions were influenced accordingly, and thus it was hard to restore normal monetary conditions after the October 1997 turmoil. Meanwhile, macroeconomic aggregates, as mentioned above, had evolved positively since October 1997 and the crisis in Asia had started to subside. Following an assessment of conditions and prospects, and particularly in view of the fact that interest rates had remained at high levels that could not possibly be sustained for long without having adverse effects on the economy, the government judged that it should promptly apply for membership of the ERM.

In the first weeks after entry, market reaction was particularly favourable. Specifically, from 16 March to 10 April, \$3.1 billion flowed into the foreign exchange market, resulting in an increase to \$19.2 billion in foreign exchange reserves and a 2-3.5 per cent appreciation of the drachma against its central ERM rates. Over the same period, the Athens Stock Exchange (ASE) index rose by 40 per cent. The price of 10-year government bonds rose sharply, leading to a decline of two percentage points in their yield, to below 8 per cent. This allowed the average yield on new 10-year

bonds with a fixed interest rate of 8.6 per cent, which were sold by tender on 23 March, to fall to 7.9 per cent. Similarly, the yield on the one-year Treasury bills issued on 30 March fell to 10.8 per cent from 12.9 per cent, the yield at the tender of 9 March. Short-term interest rates in the interbank market for maturities of 1 to 12 months fell by 2.7-3.3 percentage points and banks proceeded to a cautious lowering of their lending and deposit rates in line with the interest rate policy of the Bank of Greece and its recommendation that, in this early period following entry, the excess liquidity conditions generated by the inflow of foreign capital should not lead to such an adjustment of interest rates that could be perceived as relaxation of the anti-inflationary policy stance.

II.3 Monetary policy objectives for 1998

The monetary policy objectives for this and the coming years are set and will be pursued in the new institutional environment established by Law 2548/1997 regarding "Provisions relating to the Bank of Greece" and within the new operational framework that emerged following the incorporation of the drachma into the ERM.

The primary objective of monetary policy, as explicitly stated in the above law, is to ensure price stability. In practice, the concept of price stability is not interpreted in absolute terms. It is internationally accepted that a satisfactory degree of price stability is achieved when inflation does not exceed 2 per cent. Consequently, Greek monetary policy will aim at reducing inflation to below 2 per cent by the end of 1999. The time horizon for the attainment of this target was decided taking account of, on the one hand, the time lags with which monetary policy instruments affect prices and economic activity and, on the other, estimates of the potential impact of the devaluation of the drachma on prices in the following months. In particular, monetary policy in 1998 will seek to contain the inflationary pressures induced by the devaluation and bring inflation back to a downward path as soon as possible, so that it converges with inflation rates in the other EU member states.

To meet the price stability criterion of the Treaty, a member state must have achieved, for one year prior to the assessment of eligibility for monetary union, an average inflation rate not exceeding by more than 1.5 percentage points the rate of the three, at most, member states with the best performance in terms of price stability.⁴ Taking into account projections from international organisations on the evolution of prices in the EU in 1999, it is estimated that if the criterion of price stability is to be met in the first half of the year 2000, *the average annual inflation rate*, in the twelve-month period before the assessment, must not exceed 3 per cent. The achievement of this target is consistent with the pursued deceleration of inflation to below 2 per cent by December 1999.

The main intermediate target of monetary pol-

icy for the attainment of its primary goal will be to maintain the exchange rate of the drachma against the other ERM currencies broadly stable. As the Greek experience between 1995 and 1997 has shown, stabilising the value of the national currency against the currencies of low-inflation countries is an effective means of curbing domestic inflation and achieving the ultimate goal of price stability. To this end, the bilateral exchange rates of the drachma against the ERM currencies will remain close to the respective central rates and, in any case, they should not deviate from the central rates by more than 2.5 per cent on average during the year. The containment of fluctuations in the exchange rate of the drachma within a narrow band (on average) is essential not only for achieving the inflation target but also for meeting the criterion of exchange rate stability. It should be stressed that, since disinflation is the central objective of monetary policy, the achievement of the inflation target will take precedence over other goals, and consequently the drachma may appreciate, moving outside the forecast narrow fluctuation band, as was the case in the first weeks after its entry into the ERM.

The change in the monetary policy framework following the participation of the drachma in the ERM and the priority given to exchange rate stability within the mechanism, together

⁴ The Treaty provisions regarding the achievement of a high degree of price stability are Article 109 j(1) of the Treaty and Article 1 of Protocol No. 6. Inflation is calculated on the basis of the Harmonised Consumer Price Index (HICP). The average inflation rate of the three best-performing countries during the period February 1997-January 1998, which was the reference period for the examination of economic convergence by the European Commission and the EMI, was 1.2 per cent. By adding 1.5 percentage points, the reference value becomes 2.7 per cent. The inflation rate of a country must not exceed this figure, to meet the relevant convergence criterion in March 1998.

with the full liberalisation of cross-border capital movements and the continuing introduction of financial innovations, reduce the usefulness of monetary and credit aggregates as intermediate targets, and their controllability. The Bank of Greece will not adopt an intermediate monetary target in 1998, as it has done in the past. Considering, however, that changes in the money stock and liquidity as well as in bank credit can, under certain conditions, provide useful information on the factors shaping the course of inflation and inflationary expectations, the Bank of Greece will continue to monitor closely the development of basic monetary aggregates and compare them with the corresponding indicative projections. Such projections are calculated so as to be consistent with the attainment of the inflation target in the medium term and, at the same time, are based on certain assumptions pertaining to the stability of private saving behaviour as well as to the level of the PSBR and its financing.

The specific indicative projections for those rates of change in monetary and credit aggregates in 1998 which the Bank of Greece will be closely following for a more comprehensive assessment of monetary conditions are:

- broad money, M3: 6-9 per cent;
- total bank credit to the private and the public sector: 4-6 per cent.

The compatibility of the aforementioned projections with the inflation target for the end of 1999 depends on certain assumptions, in particular:

— the demand for M3 and broader liquidity (M4) by the non-bank private sector will not be affected by financial innovations resulting in considerable shifts of funds among various monetary or financial aggregates;

— the net PSBR in 1998 will be contained to the budgeted level of 1,660 billion drachmas⁵ and the share of the non-bank private sector in the financing of government deficit will be about 70 per cent, as was the case in 1995.⁶

In addition, the Bank of Greece will continue to monitor a series of other indicators which provide information on the factors directly or indirectly affecting the course of inflation and especially core inflation. Specifically, the Bank will continue to monitor indicators of labour market conditions and aggregate demand and supply, such as the unemployment rate and the degree of capacity utilisation.

The monetary policy to be pursued in 1998, while mainly aiming at the further deceleration of inflation, is also compatible with GDP growth of 3.5 per cent, as projected in the updated convergence programme of the Greek economy. The maintenance of the exchange rate of the drachma close to its ERM central rate, in conjunction with the deceleration of inflation, implies that the economy will benefit from the improvement in competitiveness brought about by the devaluation. This will

⁵ Net PSBR includes net borrowing requirements of the central government, public entities (social security funds, local authorities etc.) and public enterprises. Central government borrowing requirements, according to the budget, are projected at 2,163 billion drachmas or 6.1 per cent of GDP; the surplus left by public utilities is estimated at about 540 billion drachmas and there is a provision for interest capitalisation and ELEGEF (Special Accounts of Guarantees of Agricultural Products) financing of 37 billion drachmas. The projected deficit of central government, on an accruals basis, of 1,560 billion drachmas or 4.4 per cent of GDP arises if an amount of 603 billion drachmas is deducted from the borrowing requirements, since, according to the budget, this amount constitutes the government's share in the increase of the capital of certain public enterprises.

⁶ In that year the investment behaviour of the non-bank private sector was not affected by the taxation of government paper yields, effective from 1 January 1997 but announced in 1996, or by the considerable decrease in real pre-tax yields recorded in the first ten months of 1997.

BOX 4

Enhancement of the technical infrastructure for the conduct of monetary policy

The effective conduct of monetary policy in the future and the integration of Greek money and capital markets into the single European market require the development and operation of modern payments systems. The Bank of Greece is developing the real-time payments system HERMES which is expected to start operating in 1998 and which will be linked to the trans-European system TARGET for the settlement of cross-border payments in euros. Thus, even though Greece is not to adopt the single currency in 1999, it will be possible to settle large value payments both in euros and drachmas from and to Greece. HERMES will contribute considerably towards preventing credit risks related to the settlement of payments, thereby also reducing possible spillovers to the entire banking system. The system will, in addition, provide credit institutions with fast and comprehensive information on their accounts with the central bank. Besides, with a view to

contributing to the development of a modern and automated system for small-value payments, the Bank of Greece participates actively in the management of the "Interbank payment system" DIAS S.A.

For the expansion and more effective operation of the secondary market in securities, the Bank of Greece has developed an electronic system for securities trading, which is soon to become operational. The Electronic Secondary Market for Securities (HDAT) is a fully automated system for transactions through terminals installed on the premises of each participant. It is linked to the system of book-entry securities and ensures automation not only of the secondary but also of the primary securities market, as well as maximum transparency and safety of transactions. Primary Dealers — a new institution introduced by a recently enacted law — will have to carry out their transactions through HDAT. The simultaneous establishment of HDAT and Primary Dealers is an important breakthrough in the operation and expansion of the secondary market and it will contribute to the more effective conduct of monetary policy and to the management of public debt.

contribute to an increase in domestic production for export and home consumption, with a favourable impact on employment. Besides, the aforementioned monitoring ranges for money supply and bank credit were set bearing in mind the forecast GDP growth. Consequently, exchange rate stability and a projected credit expansion of 4-6 per cent are consistent with the high growth rate set for 1998.

Interest rate policy is the main instrument used by the Bank of Greece for attaining both its primary goal and the intermediate target for the exchange rate. Therefore, the evolution of interest rates, through which the Bank influences monetary conditions, will depend on how core inflation will turn out in 1998 and 1999 and will reflect the anti-inflationary stance of monetary policy. Following the entry of the

drachma into the ERM and the abatement of pressures in the foreign exchange market, conditions emerged that allowed a decline in interest rates from the peak reached during the first two months of the year. However, since inflation is expected to rise temporarily, as a result of the devaluation, before returning to its downward path, the way interest rates evolve over the coming months will inevitably depend on the intensity of inflationary pressures and the policy response of the Bank of Greece. Over the medium term, from 1999 onwards, the deceleration of inflation and the reduction in the government deficit will allow a significant fall in interest rates and their convergence towards the rates of the euro area.

The effective control of inflation in 1998 and the achievement of monetary stability in the

coming years cannot be ensured by the conduct of an anti-inflationary monetary policy alone. At the same time it is necessary to implement a suitable fiscal policy and structural adjustment measures, both of which will contribute to a faster deceleration of inflation and help sustain the conditions of stability that will emerge. More specifically, at the present juncture, and following the devaluation of the drachma and its participation in the ERM, it is essential to implement an appropriate macroeconomic policy, compatible with the monetary policy pursued, in order to ensure the drachma's smooth participation in the ERM and sustain the improved competitiveness of the Greek economy. The implementation of the additional measures aimed at speeding up fiscal and structural adjustment already announced by the government, within the framework of its overall macroeconomic policy, constitutes a key prerequisite for consolidating the benefits reaped from the devaluation, minimising its inflationary effects and establishing conditions conducive to fast and sustainable economic growth.

The return of inflation to a downward path and its maintenance at a low level depends also on labour market developments, firms' pricing policy and the degree of competition in markets for goods and services. In order to reduce inflation and secure the improvement in international competitiveness that resulted from the devaluation, it is necessary to ensure that wage increases are compatible with the medium-term rise in Greek productivity and with developments in labour costs and productivity in competitor countries. The containment of labour cost increases within these limits will also help to create conditions that will enable faster and more sustainable economic growth and, hence, a rise in workers' real income as

well as a reduction in the unemployment rate which remains high.

At the same time, it is both imperative and feasible for firms to pursue a moderate pricing policy so that inflationary pressures remain under control and the improvement in competitiveness is safeguarded. Such a pricing policy is imperative for strengthening firms' profitability in the future, and for their viability, particularly in view of the adoption of the single European currency, and it is feasible because profit margins and productivity have improved considerably in recent years.

If, in the course of 1998, fiscal and structural policies in conjunction with labour and product market developments do not contribute, to the desired degree, to the deceleration of inflation, the Bank of Greece will have no alternative but to pursue a tighter monetary policy, so as to reduce inflation below 2 per cent by the end of 1999. However, an effort to disinflate the economy by means of monetary policy would have, at least in the short term, unfavourable repercussions on economic activity and public finances, since it would entail an increase in interest rates. For precisely this reason, it is important that the government's economic policy as well as price and wage policies be consistent with the anti-inflationary stance of monetary policy.

The primary objective of the Bank of Greece, as also stated in the new law, is to ensure price stability. This implies the preservation of the purchasing power of the currency and hence of labour income. Furthermore, the attainment of this goal is an essential condition for the achievement of high and sustainable economic growth and a corresponding rise in employment. The Bank of Greece will consistently pursue the monetary policy required for securing monetary stability in our country.

III. Monetary Policy Measures

1997

14 February

As of 17 February 1997, the Bank of Greece lowers its rediscount rate for bills of exchange and promissory notes from 16.5 per cent to 15.5 per cent and the lombard rate from 21 to 20 per cent.

26 March

As of 28 March 1997, the Bank of Greece introduces a standing deposit facility in two tranches, each bearing interest at a different rate. In the first tranche, credit institutions may deposit surplus liquidity up to a global ceiling, currently set at 300 billion drachmas. Each credit institution's quota in the above amount shall depend on its domestic market share. Any amount in excess of each credit institution's quota may be deposited in the second tranche. The respective interest rates are set at 11.90 per cent and 9.90 per cent.

12 May

As of 13 May 1997, the Bank of Greece rediscount rate is lowered from 15.5 to 14.5 per cent, the lombard rate from 20 to 19 per cent and the rate on overdrafts on banks' current accounts with the central bank from 25 to 24 per cent.

24 July

The deposit facility rates are lowered from 11.90 per cent to 11.60 for the first tranche and from 9.90 to 9.60 per cent for the second tranche.

28 July

As of 1 August 1997, natural or legal persons who are residents of Greece are free to hold deposit accounts in foreign exchange with

credit institutions in Greece. The existing categories of foreign exchange deposits, with the exception of those held by seamen and emigrants, will gradually cease to be subject to the 70 per cent redeposit requirement with the Bank of Greece and will henceforth be subject to the same management framework as drachma deposits, which currently involves a reserve ratio of 12 per cent.

14 August

As of 18 August 1997, the interest rate of the first tranche of the deposit facility is lowered from 11.60 to 11.30 per cent.

7 October

As of 8 October 1997, the interest rate of the first tranche of the deposit facility is lowered from 11.30 to 10.90 per cent.

31 October

— New debit balances or increments to existing debit balances on credit institutions' current accounts with the Bank of Greece are henceforth subject to a daily surcharge of 0.4 per cent, in addition to the annual overdraft rate of 24 per cent.

— The Bank of Greece, through a fixed-rate tender, absorbs overnight liquidity of 150 billion drachmas from the interbank market at a rate of 150 per cent.

3 November

The Bank of Greece provides liquidity to financial institutions holding large portfolios of government securities, through a three-month swap operation amounting to 139 billion drachmas, at a fixed rate of 11.6 per cent. Financial institutions are required to provide collateral in the form of Greek government securities twice the value of the liquidity obtained.

5-6 November

The Bank of Greece, through a fixed-rate tender for seven- and six-day deposits, absorbs liquidity from the interbank market totalling 86 billion drachmas, at a rate of 70 per cent.

12 November

The Bank of Greece provides liquidity to banks through a four-month swap operation, amounting to 123.5 billion drachmas, at a rate which is reset every month (initially: 14 per cent). Banks are required to provide collateral in the form of Greek government securities twice the value of the liquidity obtained.

24 December

As of 29 December 1997, the daily surcharge of 0.4 per cent which applies to further increments to the debit balances of banks' current accounts with the Bank of Greece is lowered to 0.2 per cent.

1998

8 January

As of 9 January 1998, the Bank of Greece raises its lombard rate to 23 per cent from 19 per cent. The maximum borrowing per credit institution under this facility is lowered by 50 per cent.

14 January-11 March

During this period, the Bank of Greece absorbs liquidity through regular tenders for 14-day deposits. The intervention rate is gradually reduced from 20 per cent (14 January 1998) to 16.5 per cent (11 March 1998).

30 March

As of 31 March 1998, the Bank of Greece lowers its lombard rate from 23 per cent to 19 per cent. The maximum borrowing per credit institution under this facility is restored to the level in effect before 9 January 1998.

In addition, as of 31 March 1998, the overdraft rate is lowered from 24 per cent to 22 per cent, and the 0.2 per cent daily surcharge is abolished.

9 April

As of 10 April 1998, the Bank of Greece abolishes its standing facility for the discounting of bills of exchange and promissory notes. This facility had not been used for a long time.

22 April

As of 23 April 1998, the interest rates of the deposit facility are raised to 11.5 per cent for the first tranche and 9.75 per cent for the second tranche, from 10.9 per cent and 9.6 per cent, respectively.

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Table 1
Consumer price index: general index and basic sub-indices

Period	General index		Goods		Services		CPI excluding fruit and vegetables and fuels		CPI excluding food and fuels	
	(1994=100)	Per cent change over previous year	(1994=100)	Per cent change over previous year	(1994=100)	Per cent change over previous year	(1994=100)	Per cent change over previous year	(1994=100)	Per cent change over previous year
1994	100.0	10.9	100.0	...	100.0	...	100.0	...	100.0	...
1995	108.9	8.9	107.4	7.4	111.4	11.4	109.4	9.4	109.6	9.6
1996	117.8	8.2	115.2	7.2	122.4	9.9	118.2	8.1	118.7	8.4
1997	124.3	5.5	119.5	3.7	132.6	8.4	125.3	6.0	126.8	6.8
1996 I	114.4	8.6	111.4	7.4	119.6	10.4	115.0	8.7	115.3	9.0
II	118.4	8.6	116.6	7.8	121.3	10.1	117.9	8.4	118.4	8.6
III	117.7	8.0	114.8	7.3	122.6	9.3	118.1	7.7	118.4	8.0
IV	120.8	7.6	117.9	6.3	126.0	9.7	121.7	7.4	122.8	7.9
1997 I	121.8	6.4	117.0	5.0	129.9	8.6	122.7	6.7	123.7	7.3
II	125.0	5.6	120.9	3.6	132.0	8.8	125.4	6.4	127.1	7.3
III	123.9	5.3	118.6	3.2	133.1	8.6	125.0	5.8	126.4	6.7
IV	126.7	4.9	121.6	3.1	135.5	7.6	128.1	5.3	130.1	5.9
1998 I	127.1	4.4	121.0	3.4	137.7	6.0	128.2	4.5	130.0	5.0
1994 Dec.	105.2	10.6	104.8	...	105.9	...	105.2	...	105.5	...
1995 Jan.	104.7	10.7	102.7	9.6	108.2	12.5	105.1	10.6	105.2	10.8
Feb.	104.5	10.0	102.4	8.2	108.1	13.1	104.8	10.2	104.6	10.4
March	106.9	9.9	105.9	8.1	108.8	13.1	107.4	10.2	107.8	10.4
Apr.	108.1	9.4	106.7	7.7	110.5	12.4	108.5	9.8	108.8	10.1
May	109.1	9.6	108.7	8.2	109.8	12.3	108.4	9.7	108.6	9.9
June	109.7	9.5	109.3	8.0	110.5	12.2	109.5	9.7	109.8	10.0
July	108.0	8.5	105.9	7.0	111.5	11.1	108.6	9.2	108.5	9.4
Aug.	108.1	8.3	106.0	4.3	111.7	10.8	108.9	9.1	108.8	9.4
Sept.	110.7	8.1	109.2	6.8	113.2	10.1	111.4	8.7	111.7	8.9
Oct.	111.5	7.8	110.2	6.7	113.8	9.8	112.6	8.6	113.1	8.8
Nov.	111.9	7.8	110.7	6.8	114.0	9.7	113.0	8.5	113.4	8.7
Dec.	113.5	7.9	111.8	6.6	116.7	10.1	114.2	8.6	114.9	8.8
1996 Jan.	113.5	8.4	109.8	6.9	119.8	10.7	114.3	8.8	114.7	9.0
Feb.	113.3	8.4	109.8	7.2	119.4	10.4	113.9	8.8	114.1	9.1
March	116.4	8.9	114.5	8.1	119.7	10.0	116.7	8.7	117.2	8.7
Apr.	117.6	8.8	115.3	8.0	121.6	10.0	117.6	8.5	118.2	8.7
May	118.6	8.7	117.3	7.9	120.8	10.1	117.6	8.5	118.0	8.7
June	118.9	8.4	117.3	7.3	121.6	10.1	118.5	8.2	119.0	8.4
July	116.8	8.1	113.8	7.4	122.1	9.5	117.2	7.9	117.4	8.2
Aug.	116.7	8.0	113.6	7.2	122.2	9.4	117.3	7.7	117.5	8.0
Sept.	119.5	7.9	117.1	7.3	123.5	9.1	119.8	7.5	120.4	7.8
Oct.	120.4	8.0	117.7	6.8	125.1	10.0	121.1	7.6	122.2	8.1
Nov.	120.3	7.5	117.6	6.2	125.1	9.8	121.3	7.4	122.4	7.9
Dec.	121.8	7.3	118.4	6.0	127.7	9.5	122.7	7.4	123.8	7.8
1997 Jan.	121.2	6.8	115.9	5.6	130.1	8.6	122.1	6.9	122.9	7.1
Feb.	120.7	6.5	115.6	5.3	129.5	8.5	121.5	6.6	122.4	7.2
March	123.4	6.0	119.4	4.3	130.2	8.8	124.3	6.5	126.0	7.4
Apr.	124.5	5.9	120.0	4.1	132.2	8.7	125.3	6.5	127.0	7.4
May	125.0	5.4	121.0	3.1	131.9	9.2	125.3	6.6	126.9	7.6
June	125.5	5.6	121.7	3.7	132.0	8.5	125.7	6.1	127.4	7.0
July	123.1	5.4	117.7	3.5	132.5	8.5	124.0	5.8	125.2	6.6
Aug.	123.2	5.6	117.7	3.6	132.8	8.7	124.2	5.9	125.4	6.8
Sept.	125.3	4.9	120.3	2.7	134.0	8.5	126.8	5.8	128.5	6.8
Oct.	126.1	4.7	121.1	2.9	134.6	7.6	127.7	5.4	129.5	6.0
Nov.	126.5	5.2	121.7	3.5	134.8	7.7	127.8	5.3	129.7	6.0
Dec.	127.6	4.7	122.0	3.0	137.1	7.4	128.9	5.1	131.0	5.8
1998 Jan.	126.5	4.4	119.9	3.4	137.8	5.9	127.4	4.3	129.1	5.1
Feb.	125.9	4.3	119.3	3.2	137.2	5.9	126.8	4.4	128.4	4.9
March	129.0	4.6	123.7	3.6	138.2	6.1	130.2	4.7	132.4	5.1

Source: Calculations based on NSSG data.

Table 2

Wholesale price index: general index and basic sub-indices

Period	General index		Domestic primary products ¹		Domestic industrial products ¹		Exported products		Imported products	
	1980=100	Per cent change over previous year	1980=100	Per cent change over previous year	1980=100	Per cent change over previous year	1980=100	Per cent change over previous year	1980=100	Per cent change over previous year
1994	748.7	8.7	754.3	13.7	769.9	7.4	589.3	8.7	856.2	9.2
1995	807.2	7.8	792.5	5.1	832.0	8.1	649.4	10.2	915.9	7.0
1996	856.8	6.1	862.7	8.9	891.1	7.1	686.0	5.6	930.9	1.6
1997	887.8	3.6	860.9	-0.2	933.4	4.8	717.8	4.6	947.4	1.8
1996 I	850.2	6.6	853.0	3.1	876.6	7.5	687.3	8.1	945.2	5.0
II	860.4	6.7	924.1	13.5	884.0	6.8	685.7	6.6	930.1	1.5
III	851.2	6.3	838.0	14.3	890.2	6.7	681.0	5.2	923.4	0.9
IV	865.4	5.0	835.6	5.0	913.4	7.3	690.1	2.7	924.9	-0.7
1997 I	875.7	3.0	852.8	0.0	921.7	5.1	701.8	2.1	935.1	-1.1
II	887.1	3.1	893.1	-3.3	925.9	4.7	714.6	4.2	947.2	1.8
III	893.6	5.0	867.3	3.5	938.1	5.4	728.5	7.0	950.6	2.9
IV	894.9	3.4	830.1	-0.7	948.1	3.8	726.3	5.2	956.6	3.4
1994 Dec.	782.0	10.2	835.3	21.0	796.1	8.5	618.5	10.5	881.1	7.8
1995 Jan.	794.0	10.5	821.7	18.9	812.4	9.2	634.9	11.8	893.0	8.0
Feb.	797.1	9.6	831.8	15.9	814.1	8.6	635.7	10.6	898.5	7.8
March	801.7	9.5	827.6	13.1	820.2	8.8	636.0	10.4	910.1	8.6
Apr.	806.8	8.8	851.1	11.8	823.7	8.4	637.1	9.4	910.5	7.6
May	810.7	8.5	817.1	5.2	830.8	8.6	650.3	11.1	922.4	8.4
June	801.6	7.2	773.5	4.0	828.6	7.9	642.0	8.3	915.7	6.5
July	795.1	6.7	733.9	2.9	827.1	7.2	638.8	8.4	914.0	6.3
Aug.	798.3	6.6	727.5	0.3	832.2	7.2	645.1	9.9	914.5	6.3
Sept.	808.0	7.1	738.7	-3.0	842.5	8.6	658.0	11.8	917.3	5.9
Oct.	815.4	6.4	765.5	-3.4	845.6	7.6	662.6	10.5	927.7	6.4
Nov.	822.9	6.3	794.9	-0.8	849.0	7.1	671.6	10.3	930.4	6.0
Dec.	834.3	6.7	826.3	-1.1	857.9	7.8	681.2	10.1	936.9	6.3
1996 Jan.	846.6	6.6	843.8	2.7	874.4	7.6	682.7	7.5	942.3	5.5
Feb.	848.5	6.4	843.9	1.5	873.8	7.3	688.9	8.4	949.9	5.7
March	855.4	6.7	871.4	5.3	881.7	7.5	690.3	8.5	943.4	3.7
Apr.	863.4	7.0	920.2	8.1	886.8	7.7	691.7	8.6	936.2	2.8
May	866.4	6.9	963.3	17.9	885.2	6.5	689.3	6.0	929.4	0.8
June	851.3	6.2	888.7	14.9	880.1	6.2	676.0	5.3	924.7	1.0
July	846.1	6.4	835.2	13.8	883.1	6.8	677.3	6.0	921.4	0.8
Aug.	847.6	6.2	834.3	14.7	885.0	6.3	678.5	5.2	923.8	1.0
Sept.	860.0	6.4	844.4	14.3	902.4	7.1	687.3	4.5	924.9	0.8
Oct.	865.2	6.1	838.4	9.5	912.2	7.9	693.7	4.7	921.4	-0.7
Nov.	864.0	5.0	837.5	5.4	911.6	7.4	686.9	2.3	924.8	-0.6
Dec.	866.9	3.9	831.0	0.6	916.3	6.8	689.7	1.2	928.5	-0.9
1997 Jan.	872.7	3.1	844.1	0.0	921.0	5.3	697.3	2.1	930.3	-1.3
Feb.	877.2	3.4	860.2	1.9	922.8	5.6	702.1	1.9	934.5	-1.6
March	877.3	2.6	854.2	-2.0	921.3	4.5	706.1	2.3	940.5	-0.3
Apr.	884.6	2.5	894.6	-2.8	922.6	4.0	711.9	2.9	944.6	0.9
May	888.7	2.6	906.9	-5.9	925.5	4.6	714.4	3.6	947.9	2.0
June	888.0	4.3	877.9	-1.2	929.5	5.6	717.4	6.1	949.2	2.6
July	890.1	5.2	875.8	4.9	932.4	5.6	722.8	6.7	947.9	2.9
Aug.	896.7	5.8	878.3	5.3	939.9	6.2	733.4	8.1	950.1	2.8
Sept.	893.9	3.9	847.9	0.4	942.0	4.4	729.2	6.1	953.8	3.1
Oct.	895.2	3.5	819.9	-2.2	949.4	4.1	731.1	5.4	956.3	3.8
Nov.	895.7	3.7	827.7	-1.2	950.4	4.3	725.4	5.6	956.5	3.4
Dec.	893.9	3.1	842.7	1.4	944.5	3.1	722.3	4.7	957.1	3.1
1998 Jan.	898.8	3.0	873.8	3.5	946.6	2.8	719.8	3.2	959.3	3.1
Feb.	898.8	2.5	874.5	1.7	946.7	2.6	714.1	1.7	965.4	3.3

¹ For home consumption.

Source: Calculations based on NSSG data.

Table 3
Gross domestic product
(at market prices and factor cost)

	Billion drachmas	Annual per cent change (at constant prices of previous year)								
		1988	1989	1990	1991	1992	1993	1994	1995	1996	1997
1.1 Primary sector (agriculture)	1,034.5	3.9	-13.4	14.9	0.0	-0.3	5.9	-1.2	-2.9	1.0
1.2 Secondary sector	2,264.5	1.8	-0.9	3.0	-2.6	-1.4	-0.4	1.1	4.3	4.8
1.2.a Mining and quarrying	89.3	-3.4	-4.9	-3.3	0.4	1.2	-0.8	-0.9	4.0	4.2
1.2.b Manufacturing	1,308.7	1.7	-2.0	3.7	-3.5	-3.1	3.2	1.7	4.0	4.0
1.2.c Electricity - town gas - water supply	214.1	9.2	2.5	3.3	8.1	-3.8	9.5	2.9	2.1	1.2
1.2.d Construction	652.4	0.4	0.8	2.3	-4.4	2.7	-9.5	-0.3	5.7	7.5
1.3 Tertiary sector	5,243.5	3.8	1.6	0.4	2.4	-2.7	4.0	3.1	3.4	4.2
1.3.a Transportation - communications	556.8	2.2	-2.7	0.6	11.4	3.2	-0.7	2.5	-0.2	2.0
1.3.b Trade	1,261.8	4.6	1.7	0.4	7.6	-0.4	2.5	4.4	7.7	8.5
1.3.c Insurance-banking	295.8	-7.5	-0.9	14.8	9.6	-26.4	12.7	6.1	9.6	11.0
1.3.d Ownership of dwellings	979.3	3.0	2.6	3.0	-4.4	-2.9	2.1	2.2	1.7	1.7
1.3.e Public administration - defence	596.2	3.2	1.1	-6.7	-4.7	-0.7	0.8	4.9	1.5	-0.2
1.3.f Health-education	682.7	10.8	5.7	0.6	0.2	-2.9	11.6	2.0	-0.3	2.0
1.3.g Miscellaneous services	870.9	3.4	0.3	-1.9	3.6	0.3	3.8	2.0	4.2	4.5
1.4 Statistical discrepancies	-224.2	...	...	...	...	...	...	...	...	...
1.5 GDP at factor cost	8,318.3	3.1	-0.9	2.6	0.8	-1.7	2.8	2.1	2.8	3.5
2.1 Private consumption	6,502.0	6.0	2.6	2.8	2.4	-0.8	2.1	2.2	2.3	2.5
2.2 Public consumption	1,311.0	5.4	0.6	-1.5	-3.0	2.6	-1.1	8.0	0.5	-0.1
2.3 Gross fixed capital formation	1,966.7	7.1	5.0	4.8	-3.2	-3.5	-2.8	7.3	9.4	10.9
2.3.a.a By type: Construction	1,326.0	2.0	3.2	3.2	-8.3	-6.0	-3.4	2.0	6.4	12.4
2.3.a.b Equipment	640.7	17.4	8.4	7.9	6.7	0.6	-1.8	16.0	13.8	8.7
2.3.b.a By investor: Private	1,542.6	7.0	8.7	2.0	-6.3	-5.0	-2.3	6.0	9.0	8.3
2.3.b.b Public	424.1	7.2	-8.3	16.9	8.2	1.1	-4.2	11.0	10.3	18.2
2.4 Change in stocks and statistical discrepancies (as a per cent of GDP)	53.4	-0.3	-0.2	0.9	-0.3	-0.3	0.1	-0.6	-0.1	0.0
2.5 Total domestic demand	9,833.1	5.3	2.9	3.7	-0.6	-0.9	1.2	3.2	3.3	3.8
2.6 Exports of goods and services	1,696.4	4.8	-4.1	3.7	10.4	-3.3	6.5	1.0	0.2	5.2
2.6.a Exports of goods	1,111.6	11.1	-7.2	5.7	11.6	-6.9	5.2	3.9	-0.7	3.8
2.7 Imports of goods and services	-2,360.5	10.7	8.7	6.0	1.3	0.2	1.3	6.1	3.9	5.9
2.7.a Imports of goods	-2,157.9	10.9	9.0	6.8	1.7	0.2	0.9	6.8	4.4	5.5
2.8 Balance of trade in goods and services	-664.1	...	...	...	...	...	...	...	...	...
2.9 GDP at market prices	9,169.0	3.8	0.0	3.1	0.7	-1.6	2.0	2.1	2.7	3.5

Source: 1988 - 94: NSSG/National Accounts (October 1997 and March 1998). Final data on the basis of the European System of Integrated Economic Accounts (ESA).

1995 - 96: NSSG/National Accounts (March 1998). Provisional estimates.

1997: Ministry of National Economy/Directorate of Macroeconomic Analysis (March 1998). Provisional estimates.

Table 4
Drachma exchange rate

Date ¹	Against the ECU		Against the DEM		Against the USD	
	Drachmas per ECU	Per cent change over the end of previous year ²	Drachmas per DEM	Per cent change over the end of previous year ²	Drachmas per USD	Per cent change over the end of previous year ²
31.12.95	303.760	-3.0	165.490	-6.3	237.040	1.3
31.12.96	306.830	-1.0	158.970	4.1	247.020	-4.0
31.12.97	312.120	-1.7	157.890	0.7	282.610	-12.6
31.01.96	303.280	0.2	165.304	0.1	246.535	-3.9
29.02.96	303.370	0.1	163.900	1.0	240.540	-1.5
29.03.96	302.680	0.4	163.330	1.3	241.020	-1.7
30.04.96	299.210	1.5	159.164	4.0	243.320	-2.6
31.05.96	298.630	1.7	158.078	4.7	242.500	-2.3
28.06.96	299.920	1.3	158.200	4.6	240.720	-1.5
31.07.96	300.000	1.3	159.630	3.7	234.580	1.0
30.08.96	301.200	0.8	160.100	3.4	236.860	0.1
30.09.96	301.250	0.8	157.900	4.8	241.300	-1.8
31.10.96	301.480	0.8	157.085	5.4	237.560	-0.2
30.11.96	303.850	0.8	157.325	5.2	241.560	-1.9
31.12.96	306.830	-1.0	158.970	4.1	247.020	-4.0
31.01.97	304.350	0.8	157.600	0.9	257.120	-3.9
28.02.97	304.360	0.8	156.840	1.4	265.500	-7.0
31.03.97	308.300	-0.5	158.710	0.2	265.870	-7.1
30.04.97	310.200	-1.1	158.900	0.0	274.600	-10.0
30.05.97	311.000	-1.3	159.935	-0.6	271.250	-8.9
30.06.97	309.330	-0.8	157.685	0.8	275.220	-10.2
31.07.97	308.000	-0.4	156.210	1.8	286.460	-13.8
29.08.97	309.200	-0.8	157.330	1.0	282.830	-12.7
30.09.97	309.730	-0.9	158.045	0.6	278.910	-11.4
31.10.97	309.640	-0.9	157.100	1.2	271.320	-9.0
28.11.97	310.980	-1.3	156.930	1.3	277.050	-10.8
31.12.97	312.120	-1.7	157.890	0.7	282.610	-12.6
31.01.98	312.820	-0.2	158.520	-0.4	289.260	-2.3
27.02.98	313.200	-0.3	158.400	-0.3	286.670	-1.4
31.03.98	343.540	-9.1	172.800	-8.6	319.800	-11.6

¹ Last working day.

² A negative sign indicates depreciation of the drachma against the respective foreign currency.

Source: Bank of Greece.

Table 5
Drachma exchange rate against basic currencies¹

Currency		1994	1995	1996	1997
European Currency Unit	(ECU)	294.780	303.760	306.830	312.120
Deutsche mark	(DEM)	155.100	165.490	158.970	157.890
French franc	(FRF)	44.934	48.410	47.182	47.194
Dutch guilder	(NLG)	138.580	147.886	141.685	140.105
Belgian franc	(BEF)	7.551	8.058	7.720	7.654
Danish krone	(DKK)	39.536	42.750	41.582	41.436
Italian lira (100 units)	(ITL)	14.814	14.976	16.185	16.072
Pound sterling	(GBP)	375.500	366.280	419.180	468.720
Irish pound	(IEP)	371.700	378.800	414.800	403.680
Spanish peseta	(ESP)	1.824	1.951	1.888	1.866
Portuguese escudo	(PTE)	1.510	1.585	1.581	1.542
US dollar	(USD)	240.100	237.040	247.020	282.610
Japanese yen (100 units)	(JPY)	241.155	230.135	212.430	217.740
Swiss franc	(CHF)	183.264	206.030	183.135	194.380
Effective exchange rate (1990=100)		67.221	64.619	64.884	63.889

¹ Last working day of the year.
Source: Bank of Greece.

Table 6

New central rates of the Exchange Rate Mechanism currencies

(effective as of 16 March 1998)

	100 BEF/LUF=	100 DKK=	100 DEM=	100 GRD=	100 ESP=	100 FRF=	1 IEP=	1000 ITL=	100 NLG=	100 PTE=	100 ATS=	100 FIM=
BEF/LUF	100.000	540.723	2062.55	11.4242	24.2447	614.977	51.2210	20.8338	1830.55	20.1214	293.162	678.468
DKK	18.4938	100.000	381.443	2.11276	4.48375	113.732	9.47269	3.85295	338.537	3.72120	54.2167	125.474
DEM	4.84837	26.2163	100.000	0.553888	1.17547	29.8164	2.48338	1.01010	88.7517	0.975559	14.2136	32.8947
GRD	875.335	4733.13	18054.2	100.000	212.222	5383.11	448.355	182.365	16023.4	176.129	2566.15	5938.86
ESP	412.462	2230.27	8507.22	47.1204	100.000	2536.54	211.267	85.9313	7550.30	82.9929	1209.18	2798.42
FRF	16.2608	87.9257	335.386	1.85766	3.94237	100.000	8.32893	3.38773	297.661	3.27189	47.6704	110.324
IEP	1.95232	10.5567	40.2676	0.223038	0.473335	12.0063	1.00000	0.406743	35.7382	0.392834	5.72347	13.2459
ITL	4799.90	25954.2	99000.2	548.350	1163.72	29518.3	2458.56	1000.00	87864.4	965.805	14071.5	32565.8
NLG	5.46285	29.5389	112.674	0.624087	1.32445	33.5953	2.79812	1.13812	100.000	1.09920	16.0150	37.0637
PTE	496.984	2687.31	10250.5	56.7765	120.492	3056.34	254.560	103.541	9097.53	100.000	1456.97	3371.88
ATS	34.1108	184.445	703.552	3.89689	8.27006	209.774	17.4719	7.10657	624.415	6.86357	100.000	231.431
FIM	14.7391	79.6976	304.001	1.68382	3.57345	90.6420	7.54951	3.07071	269.806	2.96571	43.2094	100.000

Source: European Commission.

Table 7
Balance of payments
(Million US dollars)

	January – December			Per cent change	
	1995	1996	1997*	1996	1997
Imports (cif)	22,928.6	24,135.5	23,643.4	5.3	-2.0
Oil	2,229.5	2,879.7	2,784.4	29.2	-3.3
Non-oil	20,699.1	21,255.8	20,859.0	2.7	-1.9
Exports (fob)	5,782.8	5,769.9	5,372.1	-0.2	-6.9
Oil	490.6	651.8	591.7	32.9	-9.2
Non-oil	5,292.2	5,118.1	4,780.4	-3.3	-6.6
TRADE BALANCE	-17,145.8	-18,365.6	-18,271.3	7.1	-0.5
NON-OIL TRADE BALANCE	-15,406.9	-16,137.7	-16,078.6	4.7	-0.4
OIL TRADE BALANCE	-1,738.9	-2,227.9	-2,192.7	28.1	-1.6
Invisible receipts	20,770.4	20,444.1	19,965.5	-1.6	-2.3
Travel	4,135.8	3,723.1	3,770.6	-10.0	1.3
Transportation	2,189.8	2,263.5	2,104.2	3.4	-7.0
Emigrants' remittances	3,070.7	2,996.0	2,924.2	-2.4	-2.4
Interest-dividends-profits	1,008.9	971.4	962.3	-3.7	-0.9
Withdrawals by non-residents	2,810	3,005.7	3,060.0	7.0	1.8
Other	2,578.2	2,427.4	2,522.2	-6.2	3.9
EU transfers (net)	4,968.0	5,057.0	4,622.0	1.8	-8.6
Invisible payments	6,475.0	6,617.7	6,527.9	2.2	-1.4
Travel	1,322.9	1,210.1	1,325.1	-8.5	9.5
Government services	365.1	407.9	455.4	11.7	11.6
Interest-dividends-profits	2,682.7	3,003.2	2,482.3	11.9	-17.3
Transportation	421.6	431.2	391.9	2.3	-9.1
Other	1,682.7	1,565.3	1,873.2	-7.0	19.7
BALANCE ON INVISIBLES	14,295.4	13,826.4	13,437.6	-3.3	-2.8
CURRENT ACCOUNT BALANCE	-2,850.4	-4,539.2	-4,833.7	59.2	6.5
CAPITAL MOVEMENT	3,161.8	8,657.4	112.4		
Private sector	2,341.7	7,216.2	-4,369.8		
Entrepreneurial capital**	3,731.5	4,844.4	2,624.8		
Real estate investment	1,040.4	1,043.9	960.4		
Commercial banks**	5.7	5.5	-7.1		
Deposits by credit institutions (by individuals)	-2,115.7 (-2,173.0)	-602.6 (-686.0)	-3,338.4 (-3,400.0)		
Suppliers' credits	527.1	259.1	468.9		
Other	-847.3	1,665.9	-5,078.4		
Public sector	820.1	1,441.2	4,482.2		
Long-term borrowing	-24.9	4,431.0	3,257.7		
Central government	4,108.3	9,755.3	9,516.5		
Public enterprises/entities	623.3	871.8	307.6		
Suppliers' credits	-0.2	-0.2	0.0		
SDR allocation	0.0	0.0	0.0		
Amortisation	-4,756.3	-6,195.9	-6,566.4		
Short-term borrowing (net)	845.0	-2,989.8	1,224.5		
Errors and omissions	-341.7	77.5	177.0		
Valuation adjustment	334.3	-754.0	-1,302.0		
OVERALL BALANCE	304.0	3,441.7	-5,846.3		
IMF credit	0.0	0.0	0.0		
Change in foreign exchange reserves	304.0	3,441.7	-5,840.3		
Change in clearing accounts	0.0	0.0	-6.0		
FOREIGN EXCHANGE RESERVES (end-of-period)	15,735.6	19,177.3	13,337.0		
CLEARING ACCOUNTS (end-of-period)	11.0	11.0	5.0		

* Provisional data.

** Net movement.

Source: Bank of Greece.

Table 8

Money supply and liquid assets¹

(End-of-period balances in billion drachmas)

Period	Currency in circulation (1)	Sight deposits (2)	M 1 (3)	Savings deposits (4)	Time deposits (5)	Repos & bank bonds (6)	M 3 (7)	Treasury bills and one-year government bonds (8)	M 4 (9)
1993	1,512.0	711.7	2,223.7	7,709.7	1,944.0	2,597.4	14,474.8	4,092.1	18,566.9
1994	1,687.7	1,105.8	2,793.5	8,811.5	2,994.2	1,156.2	15,755.4	5,394.0	21,149.4
1995	1,863.6	1,285.4	3,149.0	10,445.4	3,119.2	666.8	17,380.4	5,509.0	22,889.4
1996	1,941.4	1,606.6	3,548.0	12,201.7	3,106.6	149.0	19,005.3	6,631.0	25,636.3
1997*	2,185.5	1,817.1	4,002.6	13,311.6	3,330.1	163.1	20,807.4	4,406.2	25,213.6
1996 Jan.	1,581.9	1,101.7	2,683.6	10,344.5	3,035.4	503.9	16,567.4	5,475.0	22,042.4
Feb.	1,574.0	1,101.3	2,675.3	10,311.7	3,029.1	468.5	16,484.6	5,575.0	22,059.6
March	1,603.8	1,107.4	2,711.2	10,334.6	3,019.5	463.1	16,528.5	5,765.5	22,293.9
Apr.	1,698.2	1,144.5	2,842.7	10,577.8	2,994.5	363.7	16,778.7	5,777.2	22,555.9
May	1,693.3	1,095.2	2,788.5	10,475.9	2,982.8	278.4	16,525.7	5,746.9	22,272.6
June	1,745.3	1,207.0	2,952.3	10,989.5	2,959.3	235.4	17,136.4	5,959.8	23,096.2
July	1,777.6	1,217.1	2,994.7	11,027.2	2,930.9	149.5	17,102.3	5,950.0	23,052.3
Aug.	1,798.2	1,239.6	3,037.8	11,190.3	2,922.0	110.2	17,260.2	5,901.9	23,162.1
Sept.	1,742.3	1,346.2	3,088.5	11,213.8	2,886.2	127.8	17,316.3	6,312.0	23,628.3
Oct.	1,693.6	1,264.4	2,958.0	11,089.5	2,856.7	150.1	17,054.3	6,526.3	23,580.6
Nov.	1,743.7	1,244.7	2,988.3	11,169.9	2,842.3	125.2	17,125.8	6,778.7	23,904.5
Dec.	1,941.4	1,606.6	3,548.0	12,201.7	3,106.6	149.0	19,005.3	6,631.0	25,636.3
1997 Jan.	1,787.3	1,425.7	3,213.0	12,284.8	3,081.4	278.9	18,858.1	5,746.9	24,605.0
Feb.	1,753.8	1,418.8	3,172.6	12,181.1	3,128.3	227.0	18,709.0	5,241.2	23,950.2
March	1,712.9	1,475.1	3,188.0	12,218.0	3,146.5	245.5	18,798.0	5,311.1	24,109.1
Apr.	1,916.2	1,527.1	3,443.3	12,408.3	3,095.5	231.3	19,178.4	5,474.7	24,653.1
May	1,885.7	1,510.3	3,396.1	12,462.3	3,080.7	221.7	19,160.7	5,225.7	24,386.4
June	1,899.5	1,771.8	3,671.3	12,823.5	3,115.9	264.7	19,875.4	5,141.2	25,016.6
July	2,011.9	1,542.7	3,554.6	12,938.6	3,014.0	221.4	19,728.6	4,867.4	24,596.0
Aug.	1,972.4	1,520.0	3,492.4	13,024.7	2,999.7	193.5	19,710.3	4,899.3	24,609.6
Sept.	1,902.2	1,709.9	3,612.1	13,198.1	3,041.9	211.4	20,063.5	4,386.9	24,450.4
Oct.	1,934.9	1,766.5	3,701.4	13,059.8	3,161.0	193.1	20,115.3	4,212.9	24,328.2
Nov.	1,865.5	1,467.2	3,332.7	12,211.4	3,707.1	175.5	19,426.7	4,609.7	24,036.4
Dec.*	2,185.5	1,817.1	4,002.6	13,311.6	3,330.1	163.1	20,807.4	4,406.2	25,213.6
1998 Jan.*	1,989.5	1,460.0	3,449.5	12,580.6	3,357.4	224.9	19,612.4	4,418.5	24,030.9
Feb.*	1,933.4	1,393.8	3,327.2	12,496.4	3,391.4	197.7	19,412.7	4,282.7	23,695.4

¹ Deposits and liquid assets of non-bank private sector.

M1 = (1) + (2).

M3 = M1 + (4) + (5) + (6).

M4 = M3 + (8).

* Provisional data.

Source: Bank of Greece.

Table 9
Financing of the private sector
(End-of-period balances in billion drachmas)

	Total			In drachmas			In foreign currency		
	Outstanding balance	Change		Outstanding balance	Change		Outstanding balance	Change	
		In billion drachmas	Per cent		In billion drachmas	Per cent		In billion drachmas	Per cent
1990	4,457	648	16.5	4,266	589	15.6	191	59	40.1
1991	5,135	732	16.4	4,805	593	13.9	330	139	72.8
1992	5,828	878	17.1	5,338	718	14.9	490	160	48.5
1993	6,009	673	11.5	5,372	526	9.9	637	147	30.0
1994	6,825	827	13.8	5,909	548	10.2	916	279	43.8
1995	8,328	1,503	22.0	6,858	949	16.1	1,470	554	60.5
1996	9,676	1,414	17.0	7,362	570	8.3	2,314	844	57.4
1997*	11,252	1,576	16.3	8,503	1,141	15.5	2,749	435	18.8

1 Excluding the effect of the conversion of state-guaranteed loans into government bonds, because the relevant guarantees were called in.

* Provisional data and estimates.

Source: Bank of Greece.

Table 10
 Financing of selected branches of the private sector
 (End-of-period balances in billion drachmas)

	Industry & mining		Small-scale industry		Trade		Housing		Consumer credit	
	Outstanding balance	Per cent change ¹	Outstanding balance	Per cent change ¹	Outstanding balance	Per cent change ¹	Outstanding balance	Per cent change ¹	Outstanding balance	Per cent change ¹
1990	1,347	10.2	418	10.6	500	36.2	702	14.1	65	14.0
1991	1,569	20.4	434	3.8	623	24.6	778	10.8	74	13.8
1992	1,735	13.3	465	7.8	826	32.6	858	10.3	97	31.1
1993	1,714	5.3	478	2.8	1,043	26.3	930	11.9	128	32.0
1994	1,913	12.2	524	9.6	1,232	18.1	1,021	11.4	231	65.6
1995	2,178	13.9	611	16.6	1,585	28.7	1,219	19.4	423	83.1
1996	2,370	11.7	659	7.9	1,890	19.3	1,554	27.5	574	35.8
1997*	2,469	4.2	726	10.2	2,315	22.5	1,928	24.0	731	27.3

¹ Per cent change of end-of-period balances. Excluding the effect of the conversion of state-guaranteed loans into government bonds, because the relevant guarantees were called in.

* Provisional data and estimates.

Source: Bank of Greece.

Table 11
Bank of Greece interest rates

End of period	Rediscount rate ¹	Lombard rate	Overdraft rate on banks' current accounts	Bank of Greece intervention rate in the interbank market	
				Overnight ²	14-day
1993	21.5	25.5	30.0	20.5	...
1994	20.5	24.0	30.0	17.0	...
1995	18.0	21.5	27.0	14.0	...
1996	16.5	21.0	25.0	12.4	...
1997	14.5	19.0	24.0 ³	10.5	12.8
1996 Jan.	18.0	21.5	27.0	13.8	...
Feb.	18.0	21.5	27.0	13.8	...
March	18.0	21.5	27.0	13.8	...
Apr.	17.5	21.0	26.0	13.4	...
May	17.5	21.0	26.0	13.4	...
June	17.5	21.0	26.0	13.4	...
July	17.5	21.0	26.0	13.0	...
Aug.	17.5	21.0	26.0	12.4	...
Sept.	17.5	21.0	26.0	13.4	...
Oct.	17.5	21.0	26.0	13.4	...
Nov.	17.5	21.0	26.0	13.4	...
Dec.	16.5	21.0	25.0	12.4	...
1997 Jan.	16.5	21.0	25.0	12.4	...
Feb.	15.5	20.0	25.0	11.9	11.9
March	15.5	20.0	25.0	10.5	11.9
Apr.	15.5	20.0	25.0	10.7	11.9
May	14.5	19.0	24.0	11.4	11.9
June	14.5	19.0	24.0	11.7	11.9
July	14.5	19.0	24.0	11.6	11.9
Aug.	14.5	19.0	24.0	11.3	-
Sept.	14.5	19.0	24.0	11.3	-
Oct.	14.5	19.0	24.0 ³	150.0 ⁴	-
Nov.	14.5	19.0	24.0 ³	10.9	14.0
Dec.	14.5	19.0	24.0 ³	10.5	12.8
1998 Jan.	14.5	23.0	24.0 ³	10.9	19.0
Feb.	14.5	23.0	24.0 ³	10.9	17.0
March	14.5	19.0	22.0	10.3	15.5

1 The standing credit facility to banks through the rediscounting of bills of exchange and promissory notes was abolished as from 10 April 1998.

2 As from 28 March 1997, data refer to the average weighted interest rate on credit institutions' overnight deposits with the Bank of Greece.

3 As from 31 October 1997, new debit balances or the increase in existing ones were charged by additional interest at the rate of 0.4 per cent per day and as from 29 December 1997 at 0.2 per cent per day. As from 31 March 1998, the additional charge was abolished.

4 Interest rate on 3-day auctions.

Source: Bank of Greece.

Table 12

Bank interest rates, Treasury bill rate and inflation

End of period	Savings deposit rate ¹	12-month Treasury bill rate	Short-term bank lending rate ²	Consumer price index ³
1993	17.1	20.3	28.4	12.0
1994	15.1	17.5	26.4	10.6
1995	12.8	14.2	21.1	7.9
1996	10.7	11.2	20.2	7.3
1997	9.5	11.4	19.1	4.7
1996 Jan.	12.5	13.8	21.4	8.4
Feb.	12.5	13.4	21.2	8.4
March	12.4	13.3	21.2	8.9
Apr.	12.4	13.3	21.2	8.8
May	12.4	13.3	21.2	8.7
June	12.4	13.3	21.2	8.4
July	12.0	12.8	21.2	8.1
Aug.	11.9	12.7	21.1	8.0
Sept.	11.4	12.7	20.6	7.9
Oct.	11.4	12.3	20.5	8.0
Nov.	11.2	11.5	20.5	7.5
Dec.	10.7	11.2	20.2	7.3
1997 Jan.	10.2	10.9	19.9	6.8
Feb.	9.7	10.5	19.6	6.5
March	9.5	10.3	19.3	6.0
Apr.	9.1	10.3	19.0	5.9
May	9.0	9.6	18.7	5.4
June	8.9	9.6	18.3	5.6
July	8.9	9.6	18.2	5.4
Aug.	8.9	9.5	18.2	5.6
Sept.	8.9	9.5	18.4	4.9
Oct.	8.7	11.3	18.2	4.7
Nov.	9.5	11.2	20.1	5.2
Dec.	9.5	11.4	19.1	4.7
1998 Jan.	9.5*	12.4	19.5	4.4
Feb.	9.5*	12.7	19.5*	4.3
March	9.4*	10.8	19.3*	4.6

1 Commercial banks' interest rate.

2 Monthly average.

3 Per cent change over previous year.

* Provisional data.

Source: Bank of Greece and NSSG.

