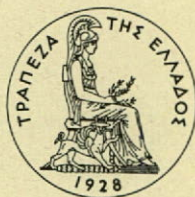


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BANK OF GREECE

REPORT
OF
GOVERNOR D. CHALIKIAS
FOR THE YEAR 1987



ATHENS 1988

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BANK OF GREECE

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GOVERNOR D. CHALIKIAS

FOR THE YEAR 1987



ATHENS 1988

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R E P O R T

**to the fifty-fifth
Annual Shareholders' Meeting
held on 29 April 1988**

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I. ECONOMIC DEVELOPMENTS AND MONETARY POLICY

1. ECONOMIC DEVELOPMENTS IN 1987

Following the stabilisation programme implemented over the period 1986-1987, the Greek economy has entered a new phase characterised by an easing of economic imbalances. Parallel to a substantial improvement in the balance of payments, significant progress has been made towards reducing inflation and weakening inflationary expectations. As a result, a more stable economic environment has been established and confidence in the economy has been restored.

The balance of payments, which had become a major constraint on the conduct of economic policy, started to improve around mid-1986. This improvement continued into 1987, despite the fact that the beneficial influence exerted by some exogenous factors in 1986 was reversed last year. Thus in 1987 external equilibrium was achieved and the country's external position was strengthened. Moreover, the slowdown in inflation continued in 1987 and became more pronounced since the beginning of the second half of the year. These developments are, to a large extent, due to the stabilisation policy pursued in the period 1986-1987. In particular, the progress achieved was the combined effect of the slower growth of labour costs, the improvement in competitiveness, the containment of domestic expenditure, the liberalisation of bank interest rates, the parallel increase in real rates, the deceleration of total bank credit expansion, and the improved profitability of business firms.

The implementation of the stabilisation programme had a limited negative impact on economic activity. In 1987, GDP decreased by only 0.6 per cent, despite the low level of agricultural production owing to highly adverse weather conditions. This limited drop in GDP should be partly attributed to the existence of a large segment of the economy whose income was affected by the stabilisation measures not only indirectly and with a significant time lag, but also much less than the income of wage earners and salaried employees. According to available indications, the decline in the real disposable income of wage earners and salaried employees, who bore the brunt of the fiscal drag, was partly offset by an increase in profits and the incomes of the self-employed. This contributed to sustaining domestic demand at a relatively high level.

Irrespective, however, of the costs entailed, it seems that the economic stabilisation programme has created favourable conditions which, if exploited, can ensure a further deceleration of inflation and maintenance of external equilibrium this year. More importantly, it seems that the stabilisation programme has led to the emergence of trends in the Greek economy which, provided they are strengthened and acquire a permanent character, could enhance the prospects for non-inflationary economic growth. The implementation of prudent economic policies is an essential prerequisite for maintaining stable economic conditions. Of crucial importance in this respect is to continue the efforts for a drastic reduction of public sector deficits as a proportion of GDP, which remain at a high level. Following its significant decrease by 4 percentage points of GDP in 1986, the public sector borrowing requirement (PSBR) tends to stabilise at around 13 per cent of GDP, thereby exerting pressure on available domestic economic resources, adversely affecting the balance of payments and inflation, and limiting the funds available for investment financing. In addition, monetary policy should continue to be aimed at controlling liquidity and containing credit expansion at a level compatible with a further deceleration of inflation and maintenance of external equilibrium. Specifically, recent experience has shown that interest rate policy can effectively contribute to curbing credit expansion, supporting foreign exchange policy and maintaining external balance.

In 1987, economic activity was favourably influenced also by an improvement in the balance of payments. An increase in the balance of invisibles by 44.3 per cent led to a substantial decrease in the current account deficit. Earnings from exports of goods rose at a high rate, faster than the growth rate of payments for imports. Given, however, that the value of merchandise imports is more than twice as large as export receipts, the trade deficit increased. The rapid growth of foreign exchange earnings from exports of goods and services last year — despite slower growth in foreign demand and reduced export subsidies — should, to a significant extent, be attributed to the maintenance of competitiveness. In fact, relevant indices show that the restrictive incomes policy implemented in the period 1986-1987, combined with the foreign exchange policy pursued, helped maintain the real effective exchange rate of the drachma virtually stable at the level it had reached after the devaluation in October 1985. In particular, the rate of increase of unit labour cost in manufacturing is estimated to have declined from 18.7 per cent in 1985 to 13.3 per cent in 1986 and 11 per cent in 1987.

Inflation deviated considerably from the target set for 1987, despite the progress made. During the year, the consumer price index rose by 15.7 per cent, against a targeted 10 per cent. The overshooting of the target was partly due to certain special factors of a transitory nature. Specifically, the CPI was adversely affected by the introduction of value added tax, owing not only to changes in the system of taxation but also to the fact that the VAT rates were higher than those they replaced. Furthermore, prices inevitably rose fast in the first months of 1987, following the end of the price freeze imposed in the last two months of 1986. It is worth noting that when the influence of these two factors waned, inflation slowed down markedly. In the July-December period, the annualised rate of inflation, on the basis of seasonally adjusted data, dropped to 11.4 per cent, against 20.2 per cent in the first half of the year, while the process of disinflation continued in the first months of 1988. In the first quarter of 1988, the CPI rose by 2.4 per cent, compared with 4.7 per cent in the same quarter of 1987, as both demand and cost pressures decreased and inflationary expectations weakened. The incomes policy pursued in 1986-1987 made a particularly significant contribution towards achieving a substantial reduction in the growth rate of labour cost over the past two years.

The composition of final private expenditure improved in 1987. On the basis of available data, private consumption, at constant prices, declined by 0.7 per cent, while private fixed asset formation increased by 4 per cent. If this trend in the distribution of economic resources in favour of investment is combined with further substantial improvement in the composition of investment, it will contribute to a broadening of the country's production base, a restructuring of the economy and a strengthening of its export orientation. By contrast, public consumption increased by 1.3 per cent in 1987, while public investment dropped by 14.2 per cent.

The decline in private consumer expenditure was smaller than in real private disposable income. As a result, the share of private saving in private disposable income decreased for the second consecutive year. This downward trend has to be reversed, so as to secure the resources required for financing both business investment and the large infrastructure projects planned by the Government; otherwise, the desired increase in investment will be constrained by inadequate domestic saving. If investment were to be financed with foreign borrowing, this would lead to an increase in the country's foreign debt, with adverse effects on the balance of payments and inflation. In addition to encouraging private saving, it is also necessary to make drastic reductions in

public consumption and thus in public deficits, which absorb domestic savings and lead to a corresponding reduction in aggregate domestic saving.

Total fixed asset formation declined by 2.3 per cent, as the sharp decrease in public investment was not offset by the increase in private investment. This decrease in investment by both Central Government and public enterprises was due to the efforts, within the context of the stabilisation programme, to curb the PSBR. The rise in private investment was partly due to an estimated 8.8 per cent increase of investment in housing. To a significant extent, however, it was due to a 7.7 per cent rise of investment in manufacturing. Various factors contributed to the revival of manufacturing investment: the improved profitability and financial position of business firms, which enhanced their capacity for self-financing; the liberalisation of direct investment by foreign residents as from mid-1986; the substantial investment incentives; the reduction of the red tape involved in the approval of investment projects under the laws providing development incentives; and, lastly, the restoration of stable economic conditions and confidence in the economy. The more efficient functioning of the markets for goods and factors of production also contributed towards improving productivity and the business climate. Price controls have to a very large extent been abolished. Today, the labour market is characterised by greater flexibility, while the liberalisation of the banking system and the abolition of a host of specialised credit rules and regulations have contributed to a more effective functioning of financial markets and a more efficient allocation of available financial resources.

It is clear that the Government's industrial policy should be oriented towards restructuring the economy instead of aiming — as it largely did since the 1970s — at maintaining an economic structure, especially in manufacturing, which cannot be viable, particularly following Greece's accession to the EEC and the opening up of the Greek economy to foreign competition. It is encouraging that progress has indeed been made in this direction. It is worth noting that, following the improvement in domestic economic conditions, the reluctance of businessmen to undertake new investment, observed in the first few years after the country's accession to the EEC and in the years immediately preceding the accession, seems to be decreasing. There are indications that a steadily growing number of firms, mainly of medium size, are adapting to the new competitive environment. This is reflected in the recovery of business investment which was observed in 1987 and, on the basis of available data, is expected to continue into the current year.

2. EXTERNAL PAYMENTS: DEVELOPMENTS AND PROSPECTS

Developments in the Greek balance of payments were particularly favourable in 1987. The current account deficit declined by 27 per cent to \$1,296 million. The improvement was more pronounced in the balance of invisibles, the surplus of which increased by 44.3 per cent, reaching \$5,647 million. This surplus covered 81 per cent of the merchandise trade deficit, compared with 69 per cent in 1986 and 48 per cent in 1985. Invisible receipts increased by 30.4 per cent to \$8,490 million, against \$6,512 million in 1986. Net of EEC transfers, invisible receipts grew by 33.3 per cent. It should be noted that transfers from the EEC in the last two months of 1987 were \$262 million less than in the corresponding period of 1986, owing to the deferment of disbursements of agricultural subsidies and grants.

The trade deficit widened by 22 per cent, from \$5,686 million in 1986 to \$6,942 million in 1987. Exports and imports grew by 24.4 and 23.1 per cent, respectively, while non-oil exports increased by 26.7 per cent and imports by 21.4 per cent. Nevertheless, the trade deficit widened because export earnings cover only 45 per cent of import payments.

The improvement in the current account was accompanied by a rise in net private capital inflows, which increased by 81.8 per cent in 1987 reaching \$1,525 million. In addition, the "errors and omissions" item in the balance of payments for 1987 was positive (\$309 million). Since a positive "errors and omissions" figure represents unallocated net earnings from exports of goods and services and net private capital inflows, the improvement in the balance of payments in 1987 was greater than that indicated by the reduction in the current account deficit and the growth of net private capital inflows.

Net official foreign borrowing increased by \$278 million and foreign exchange reserves by \$819 million, excluding valuation adjustments due to changes in the price of gold and in currency parities. Consequently, the country's net foreign exchange position improved by \$541 million in 1987, while non-gold reserves rose from \$1,519 million at the end of 1986 to \$2,681 million at the end of 1987. Including gold, valued at 65 per cent of its market price, foreign exchange reserves totalled \$3,738 million at year-end 1987, compared with \$2,360 million at the end of 1986.

The policies pursued in the last two years achieved in 1987 something more than the target set for the stabilisation of the external debt. As a percentage of GDP, the public and government-guaranteed external debt fell from 42 per cent in 1985 to 39.3 per cent in 1986 and to 36 per cent in 1987. In

absolute figures, it reached \$18,208 million at the end of 1987, against \$15,713 million at the end of 1986. Of last year's increase, 95 per cent was due to the depreciation of the US dollar against the other currencies in which part of the foreign debt is denominated.

The improvement in the balance of payments in 1987 was mainly due to the slowdown in inflation and the weakening of inflationary expectations, the increase in real interest rates owing to the deceleration of inflation and the liberalisation of interest rates, the liberalisation of some categories of capital movements, and the restoration of confidence. Exchange rate policy also had a positive effect on the balance of payments. The differential between domestic and foreign interest rates widened, partly owing to the drop in interest rates abroad, and it more than offset expectations of a drachma devaluation.

A central aim of economic policy should be to bring about a permanent improvement in the balance of payments and consolidate the downward trend in the country's external debt. This can be done, provided we continue to pursue appropriate fiscal and monetary policies and promote the implementation of structural policies. It is significant that it has now become widely accepted that, in a small and open economy like Greece, the conduct of an autonomous monetary policy is not feasible, especially as regards interest rates. The balance of payments was favourably influenced following the rise of domestic real interest rates to levels comparable to those prevailing abroad. The conduct of monetary policy, however, is subject to constraints, especially in view of the need to finance a large PSBR. Domestic economic objectives should not be overlooked in the formulation of monetary policy, particularly when they concern efforts to support economic activity, employment and investment. It is for this reason that, parallel to the conduct of an appropriate monetary policy, a drastic reduction in the PSBR and the adoption of methods for financing it that do not undermine the effectiveness of monetary policy are of crucial importance for maintaining external equilibrium. The progress already made in both these directions must continue.

It should be pointed out that the favourable developments observed in the balance of payments in 1987 do not imply that the external sector has ceased to be a constraint on the conduct of economic policy. Nor do they imply that the structural weaknesses of the economy, especially in the manufacturing sector, which are reflected in the large trade deficits, have been eliminated. As has already been pointed out, the improvement in the balance of payments should be attributed partly to the arrest of capital flight or to the repatriation of funds from abroad. This implies that economic stability and

the conduct of appropriate monetary and foreign exchange policies could help in the attainment of external equilibrium, particularly if the peculiarities of the Greek balance of payments are taken into consideration. At the same time, however, the structural weaknesses of the balance of payments should be dealt with via an enhancement of the economy's export orientation, as well as an expansion and improvement of the quality of domestic production to satisfy part of growing domestic demand.

There are two reasons why the export orientation of the Greek economy should be enhanced. The first is that the opening of the domestic market to foreign competition following the country's accession to the EEC has already led to an increase in import penetration of the market for manufactured goods, from 23.6 per cent in 1980 to 34.5 per cent in 1987, and this trend should be expected to continue over the coming years, even though at a slower pace. The second reason, which is independent of the country's accession to the EEC, is that technological progress and a substantial improvement in productivity, and therefore in living standards, in a small economy like Greece, with the limited size of its market, can only be achieved through a higher degree of economic specialisation. This means that some branches of industry where Greece has or could gain a comparative advantage should be developed beyond the needs of the domestic market in order to realise a surplus of exportable goods. By exporting these goods, the country would be able to finance the growing volume of imports that would result from the exposure of the domestic market to foreign competition and from the increase in domestic production and demand. Progress in this direction is already considerable, but not adequate.

Trade deficits constitute a chronic phenomenon in the Greek balance of payments. In the sixties, the country's trade deficit was large, about 10 per cent of GDP, surging to 17.2 per cent in 1973, after the first oil crisis. Then, it gradually declined, dropping to 14 per cent of GDP in 1978, but after the second oil shock in 1979 it started rising again, reaching 18 per cent of GDP in 1981. A decline followed between 1982 and 1984, but in 1985 the trade deficit rose again to 18.8 per cent of GDP, then fell to 14.3 per cent in 1986, and was 14.7 per cent in 1987.

As a proportion of GDP, the non-oil trade deficit has not widened since the country's accession to the EEC in 1981, despite a considerable increase in import penetration. This deficit averaged 10.4 per cent of GDP in the first seven years after Greece's accession, compared with 10.9 per cent in the seven years before 1981. Parallel to the increase in imports, exports of goods also

grew at a relatively fast pace. Between 1985 and 1987, non-oil exports of goods increased by 46.5 per cent, while imports increased by 38.5 per cent. Since the terms of trade deteriorated in the last two years, the increase in the volume of exports must be considerably larger than the corresponding increase in the volume of imports.

These developments suggest that the Greek economy is adjusting, albeit slowly, to the new conditions created by the country's accession to the EEC. The manufacturing sector has weathered the opening of the domestic market to foreign competition. The investment climate has improved and business investment is recovering. Substantial qualitative changes are gradually being introduced in the manufacturing sector, with the adoption of modern management and marketing techniques and new methods of production. Provided that these trends continue, it would be possible not only to stabilise the trade deficit as a proportion of GDP, but also to reduce it to the extent that the adjustments required in the structure of the economy are promoted.

Over the next few years, however, even the stabilisation of the trade deficit as a proportion of GDP could be regarded as a positive development, in view of certain peculiarities of the Greek economy and of the Greek balance of payments. It is well known that, over a long period up to the early seventies, Greece's large trade deficit was no problem, since it was financed entirely out of invisible receipts and private capital inflows. The peculiarity of the Greek balance of payments lies in the fact that invisible receipts are considerably higher (by 51 per cent in 1987) than earnings from exports of goods. Even without transfers from the EEC, invisible receipts in 1987 were 21 per cent higher than receipts from exports of goods.

Apart from the large surplus on invisibles, however, Greece is in an advantageous position in yet another respect. It can rely on a sizeable net inflow of private capital, the bulk of which comes from Greeks living or working abroad and does not, therefore, increase the country's foreign indebtedness. Until the early seventies, private capital inflows enabled Greece to meet sizeable deficits on current account, without having to resort to foreign borrowing. Even during the 1970s, after the first energy crisis, the net inflow of private capital covered on average 93 per cent of the current account deficit. It was only after the second oil shock in 1979 that the share of net private capital inflow in financing the current account deficit declined as a result of a widening of the deficit because of, among other things, the increased oil bill, and a drop in the net inflow of private capital. But even during the period from 1979 to 1986 there was a sizeable net inflow of

private capital, which financed around half of the deficit on current account, while in 1987 net private capital inflow was 18 per cent larger than the current account deficit.

As in the case of invisible receipts, the drop in net private capital inflows after the second energy crisis should be attributed partly to international economic conditions, though it was largely due to domestic factors. High inflation and the concomitant climate of uncertainty, serious domestic economic imbalances, and low domestic interest rates relative to those prevailing abroad, had a negative impact on invisible receipts and capital inflows. Nevertheless, despite these unfavourable international and domestic conditions, the inflow of private capital remained an important source of funds for financing the country's increased deficit on current account. Following the gradual easing of economic imbalances, the deceleration of inflation, the restoration of confidence and the rise in real interest rates, the balance of payments started to improve. Considering that there was no improvement in international economic conditions, the increase in invisible receipts and private capital inflow should be attributed almost exclusively to better domestic economic conditions. This underlines how important it is for a small open economy like Greece to maintain stability and confidence.

3. DEVELOPMENTS AND PROBLEMS IN THE PUBLIC SECTOR

Efforts to reduce the public sector deficit continued into 1987, but the outcome was less satisfactory, compared with the progress made in 1986 and the targets set by the Government. On a cash basis, the net PSBR fell to 13.5 per cent of GDP, against 14 per cent in 1986, and 17.9 per cent in 1985. The improvement in 1987 was limited because of the widening of the central government deficit. The factors that contributed to the increase in this deficit were: the shortfall in revenue from tax arrears; the larger deficit in the oil account due to the rise in crude oil prices which was not offset by an appropriate adjustment in domestic oil prices; increased government transfers to the Social Insurance Institute (IKA) and public transport organisations. It should be noted that the borrowing requirements of central government in 1987 were also affected by two special factors: (i) the deferment of payments of agricultural subsidies by the EEC in the last two months of the year; and (ii) the strike called by public cashiers, as a result of which taxes due in 1987 were collected in 1988. It is estimated that, without the effect of these two

factors, the PSBR on a cash basis would have been lower by one percentage point of GDP.

The net borrowing requirements of social insurance, local government and other public organisations were considerably smaller than in 1986. This occurred because the deficits of IKA and public transport organisations were partly covered by transfers out of the government budget. Moreover, the decrease in the net borrowing requirements of public organisations was due to the large increase (73 per cent) relative to 1986 in the surpluses of certain social insurance organisations.

The borrowing requirements of public utilities were also reduced in 1987. This was due to an improvement in operating results, particularly those of the Hellenic Telecommunications Organisation and the Public Power Corporation, and to a decline in investment outlays.

Finally, considerable progress was made, especially during the second half of 1987, regarding the methods employed in financing the PSBR, as stated in the next section.

For 1988, according to government budget forecasts, it is estimated that the net PSBR on a cash basis will drop further, by approximately one percentage point of GDP. Moreover, it is planned to resort to the money and capital markets in order to finance a considerably larger portion of the PSBR. Regarding the planned reduction of borrowing requirements, it should be noted that, apart from the fact that it is inadequate, its realisation will necessitate concerted and persistent efforts. Stricter budgetary control, and perhaps a reduction of outlays, is necessary to restrain government budget expenditures within appropriate limits.

The containment of public sector expenditure comes up against certain difficulties, considering that the high deficits of recent years have increased the inelasticity of expenditure, both in the government budget and in the public sector as a whole. Expenditure for interest payments more than doubled between 1982 and 1987 as a percentage of total government outlays (net of amortisation payments) and as a percentage of tax revenue. In 1987, interest payments absorbed over 25 per cent of tax revenue. These developments imply that if public sector deficits remain high over a long period, with a concomitant increase in the public debt, the government budget deficit will become a structural problem, owing to the accelerating growth of interest payments. Similar remarks can be made with regard to the deficits of a considerable number of public organisations and enterprises. Over the past ten years, the debt of central government and social insurance organisations

tripled to almost 70 per cent of GDP at the end of 1987.

The very large increase in the public debt was due to the existence of high primary deficits, namely deficits after the deduction of public debt servicing. During the seven-year period 1981-1987, annual primary deficits averaged 6.2 per cent of GDP, having fluctuated in the range of 9 per cent in 1981 and 4.8 per cent in 1986. During the above period, interest payments made a relatively modest contribution to the increase in the public debt, owing to high inflation and low nominal interest rates. The average nominal interest rate was about 11.5 percentage points lower than the average growth rate of nominal GDP, whereas the average real interest rate was strongly negative. If the average real interest rate had been positive or even if the difference between the average growth rate of nominal GDP and the average nominal interest rate had been limited to five percentage points, then the public debt would have already exceeded GDP and expenditure for debt servicing would have been considerably higher. It should be stressed that the maintenance of negative real interest rates or even of positive real interest rates lower than those prevailing in international money markets is not a solution, since it would have serious negative repercussions on the allocation of financial resources and, mainly, on the balance of payments, especially in view of the forthcoming liberalisation of capital movements and the unification of EEC money markets.

The rapid growth of interest payments, especially since 1984, is an increasingly important factor contributing to the rise of the public debt as a percentage of GDP. In the last two years, the greater part of the PSBR was financed out of domestic sources at the prevailing high nominal and positive real interest rates. On the other hand, the deceleration of inflation led to lower growth rates of nominal GDP and tax revenue. In 1987, the average interest rate on the domestic public debt was 13.7 per cent, against 10 per cent over the five-year period 1981-1985, while the growth rate of nominal GDP dropped to 15 per cent, from 22 per cent during the five-year period 1981-1985. Maintenance of real domestic interest rates in 1988 and subsequent years at levels comparable to those prevailing in international money markets implies that the containment of public sector expenditure and the necessary further substantial reduction of public sector deficits will face greater difficulties, owing to rapidly increasing interest payments on the public debt. This has already occurred in a number of other European countries, where the public debt has reached or even exceeded the level of GDP. The only way to prevent a further rise in the public debt as a proportion of GDP is to reduce the primary public sector deficit to zero or, if possible, turn it into a surplus.

Given the level of real interest rates, the growth of real national income has a restraining effect on the public debt as a proportion of GDP.

The above remarks underline the necessity for sharp and rapid reductions in the PSBR. In addition, a serious problem is faced in connection with State revenue. Despite high tax rates, tax revenue is relatively low owing to extensive tax evasion, as regards both direct and indirect taxation, and this is probably the major cause of the large ordinary budget deficits. Similar problems are posed by considerable delays in the transfer to social insurance organisations of contributions collected on their behalf. The recent introduction of value added tax and the substantial reductions in income tax rates represent considerable progress towards a reform of the tax system and have prepared the ground for a drastic curtailment of tax evasion.

In connection with public organisations, social insurance funds in particular, it is expected that they should have little difficulty in keeping their net borrowing requirements within the limits set by the Government, in view of the further large increase in government transfers to the Social Insurance Institute (IKA), provided that the efforts to improve IKA's financial results are continued. In the case of social insurance organisations, the central aim should be to collect insurance contributions in arrears, irrespective of whether unpaid contributions are owed by public or private enterprises. Controls should be tightened and every possible effort should be made to improve the assessment and collection of social insurance contributions. It is similarly advisable to make vigorous efforts to introduce organisational improvements which would help contain operational expenditure and exercise more effective control over insurance benefits. The Seamen's Pension Fund is a special case, since the imbalance between its revenue and expenditure is largely structural.

Following the progress achieved in 1987, public enterprises could contribute to economic stability and growth. In 1987, a policy of containing operational costs and increasing revenue was successfully implemented, especially in certain major public enterprises. The same policy must be continued in 1988, and be more strictly applied in the case of deficit-running public enterprises. Success of this policy would make it possible to undertake larger investment programmes, which would contribute to expanding and improving economic and social infrastructure.

In 1988 the public sector plans to finance a larger part of its deficit than in 1987 by resorting to the money and capital markets. In fact, it expects to raise a total of 350 billion drachmas from the financial markets. In order to

achieve this, it is necessary that the Government and other public entities continue to offer securities on market terms. In the first quarter of 1988, the value of treasury bills sold in the financial markets amounted to an estimated 123 billion drachmas, while in the same period net borrowing (new issues minus redemptions) amounted to an estimated 70 billion drachmas.

4. MONETARY DEVELOPMENTS AND POLICY

In 1987, monetary policy aimed at two broad objectives: stabilisation and deregulation. At the macroeconomic level, the goals were a further deceleration of inflation and an improvement in the current and capital accounts of the balance of payments. At the microeconomic level, the objective was to accelerate the pace of financial reform by liberalising interest rates, eliminating specialised credit rules and regulations, strengthening competition and developing the financial markets.

Developments in the money and credit markets in 1987 were to a considerable extent the result of policy action aimed at achieving the above objectives. They were also the result of other factors, both domestic and external, which exerted strong pressure on the financial markets. In particular, the limited progress, relative to the target, towards reducing the PSBR as a percentage of GDP, the significant changes in the method of financing public sector deficits, the substantial improvement in the balance of payments and particularly in net capital inflows, the improved profitability of business firms, and the abolition of the import deposit scheme affected financial developments.

The salient features of monetary and credit developments in 1987 were: (i) a continuous deceleration of total domestic credit expansion, for the second consecutive year, (ii) an acceleration of the growth rate of broad money (M3), which reversed the downward trend that had started in mid-1985, and (iii) a substantial increase in real interest rates over the year, reflecting a modest rise in nominal rates, following the liberalisation measures, and mainly a significant deceleration of inflation. These developments may seem somewhat contradictory, since credit and interest rate developments imply a further tightening of monetary policy, while the faster money growth may be interpreted as indicating an easing of monetary controls. This apparent inconsistency is examined in the last part of this section, where it is argued that financial developments are consistent with the restrictive stance of policy in

1987, which contributed to the stabilisation of the economy. As has already been pointed out, the balance of payments improved substantially over 1987, while the process of disinflation has continued steadily. The improvement in the balance of payments and the downward trend of inflation became more evident during the second half of 1987.

a. Credit Markets

Credit expansion to the private sector continued to decelerate in 1987. It reached 10 per cent, compared with 15.6 per cent in 1986 and 18.8 per cent in 1985, and was below the target of 11 per cent. The financing of the private sector by the banking system remained at a relatively low level throughout the year, except for a transitory acceleration during the third quarter, associated with the financing of marketing boards and farmers' cooperatives. The slower than initially projected credit expansion to the private sector in 1987 reflects the marked slowdown of the growth rate of lending by commercial banks to 6.6 per cent, which was 3.5 percentage points below the target and 8 percentage points below the figure for 1986. By contrast, credit extended to the private sector by specialised credit institutions, i.e. the Agricultural Bank and investment and mortgage banks, increased by 13.5 per cent, 1.5 percentage points above the initial projection.

Developments in the market for commercial bank credit were influenced by various special factors on both the demand and the supply side. The deceleration in credit expansion, however, was primarily due to the restraining influence of the private sector's credit demand reflecting: a decline in industrial production, the improved profitability of firms, the abolition of advance deposit requirements on imports which released funds of about 86 billion drachmas to the private sector, and the sharp rise in the real cost of borrowing. Real interest rates on short-term commercial bank borrowing, calculated on the basis of the annual rate of price changes, rose from 4.7 per cent in March 1987, after the price freeze and the introduction of value added tax, to 7.1 per cent in December, while they averaged about 7.4 per cent over the last quarter of 1987. Another factor which limited demand for commercial bank credit was the increase in foreign borrowing and in suppliers' credit, partly in response to the widening of the differential between domestic and foreign interest rates and to improved expectations concerning inflation and the exchange rate of the drachma.

On the supply side, the sharp rise of private drachma deposits with commercial banks by 26.1 per cent and the abolition of the requirement that banks allocate 15 per cent of their deposits for the financing of investment resulted in a substantial rise in bank liquidity. This rise was offset in part by successive increases in reserve requirements. However, commercial bank liquidity remained high, especially over the second half of the year. The high level of bank liquidity in 1987 is reflected by developments in the interbank interest rate, which on average remained at relatively low levels.

The larger than initially projected credit expansion to the private sector by specialised credit institutions resulted exclusively from the faster growth of credit extended by the Agricultural Bank of Greece and the Hellenic Industrial Development Bank. Credit extended by the Agricultural Bank rose by 12.7 per cent in 1987, against 19 per cent in 1986 and a credit ceiling of 12 per cent. The overrun was largely due to the financing of agricultural marketing boards and cooperatives, which absorbed one-third of the Agricultural Bank's credit to the private sector. These entities faced increased borrowing needs last year, owing to difficulties associated with the marketing of cereals and tobacco from the 1986 crop. In order to limit the growth of liquidity of the Agricultural Bank, at the end of September the Bank of Greece imposed non-interest bearing reserve requirements on the Agricultural Bank's deposits. Credit provided by investment banks, which was not subject to any formal ceiling, rose by 23.2 per cent against 12.7 in 1986. This reflects in part a revival in business investment.

The effect of the PSBR on bank liquidity and money growth was contained in 1987 through a substantial increase in the sales of government paper directly to the public. A variety of financial instruments were offered throughout the year, including treasury bills, two-year drachma bonds, and ECU-linked medium-term bonds. In addition, the Public Power Corporation issued a seven-year DM-indexed bond. During the first months of the year, net sales of public sector securities remained at very low levels. But following a reduction in interest rates on time deposits in April and, in particular, a rise in rates on treasury bills by one percentage point in June, and as inflation decelerated and inflationary expectations weakened, demand for government paper increased considerably. As a result, the share of the borrowing requirement of the central government which was financed from nonbank sources rose to 18.9 per cent, against 3.8 per cent in 1986. These positive developments over the second half of the year made possible a further reduction of domestic bank credit expansion to the public sector, from 20.8 per cent in 1986 to 16.5 per cent in 1987. In addition, the share of the net PSBR financed by foreign

borrowing declined sharply from 28.4 per cent in 1986 to 8.7 per cent in 1987. The substitution of domestic credit for foreign borrowing and the substantial increase in the nonbank financing of the public sector contributed to the effectiveness of monetary policy last year.

As a result of these developments, total domestic credit expansion to both the public and private sectors decelerated for the second consecutive year to 13.7 per cent in 1987, against 18.9 per cent in 1986 and 26 per cent in 1985.

b. Monetary Aggregates and Liquidity

Money broadly defined (M3), which includes currency in circulation plus all private drachma deposits, grew by 24.5 per cent in 1987, exceeding by a wide margin the target of 15.5 per cent set in the monetary programme. The rate of M3 growth last year was also substantially higher than the rate recorded in 1986 (19.1 per cent). The higher M3 growth is associated with an acceleration of the growth rate of both savings and time deposits, from 21.4 per cent in 1986 to 26.8 per cent in 1987, and of narrow money (M1), i.e. currency in circulation plus private sight deposits, from 9.4 per cent to 13.6 per cent respectively.

The overshooting of the monetary (M3) target last year was the combined effect of various factors. Some of these factors reflect positive developments in the economy, while others relate to fiscal policy and special developments in the financial market. As noted above, the borrowing requirement of the public sector, measured either as a percentage of GDP or in terms of its growth rate, exceeded original projections. But the marked increase in the share of the PSBR which was financed directly from the nonbank credit market, appreciably reduced demand for bank credit by the public sector and limited its contribution to M3 growth. Thus, although the financing of the public sector contributed to the deviation of M3 growth from the target, it cannot account by itself for the acceleration of money growth in 1987.

The significant improvement in the balance of payments, especially in the second half of the year, explains to a large extent the acceleration of broad money growth. The positive developments in the balance of payments are closely related to and reflect the rise in domestic real interest rates and the corresponding widening of the differential between domestic and international interest rates. The restoration of confidence in the economy, the liberalisation

of some categories of capital movements and the relaxation of controls on foreign borrowing by domestic firms also contributed to the rise in the inflow of foreign private capital to a level higher than initial estimates. Finally, the abolition of the import deposit scheme contributed to the acceleration of M3 growth in 1987, while in the previous year advance import deposits had had the opposite effect.

The influence of the above factors on money growth was not uniform throughout the year. In the first five months, the annualised growth rate of M3 fluctuated around 21.5 per cent and did not exhibit any upward trend. As from June, however, it rose continuously, initially as a result of the improvement in the balance of payments and subsequently also as a result of the higher borrowing needs of the public sector in the last quarter of the year. To stem money growth, the yields on treasury bills were raised by one percentage point in June. In conjunction with the slowdown of inflation and the weakening of inflationary expectations, this interest rate adjustment enabled the public sector to sell short- and medium-term securities totalling about 140 billion drachmas, thus limiting bank liquidity. To the same end, the Bank of Greece increased reserve requirements on commercial bank deposits in June and October, and also imposed for the first time reserve requirements on the Agricultural Bank's deposits (1 per cent in September and 2 per cent in October). Nevertheless, these measures proved inadequate to contain M3 growth at a rate close to the target, owing to the pressure exerted by the external and public sectors. Another factor which seems to have contributed to the acceleration of M3 growth is a higher degree of intermediation following the rise in real rates on bank deposits and the restoration of confidence in the economy.

At average annual levels, the growth rate of broad money exceeded that of nominal GDP, and resulted in a further rise of the corresponding liquidity ratio from 67.1 per cent in 1986 to 71.1 per cent in 1987, compared with an average 57.6 per cent in the previous ten years. As has been noted in previous Reports, the long-run upward trend of the liquidity ratio is associated mainly with the inadequate development of domestic financial markets, which restricts the portfolio choices of the public mainly to bank deposits. In addition, this ratio is influenced by the rates of return on bank deposits and on competing domestic and foreign financial assets, by inflationary expectations, and other factors affecting saving behavior, such as confidence. To the extent that the faster rise in the liquidity ratio in 1987 reflects a voluntary accumulation of deposits induced by their higher real rates of return and by other

positive economic developments, there is less danger of potential adverse effects on the balance of payments and inflation. Nevertheless, an excessive accumulation of liquid assets requires careful monitoring and the implementation of appropriate macroeconomic policies. It should also be noted that the change in the liquidity ratio in the last two years was affected by the import deposit scheme. If the liquidity ratio is calculated for a broader measure of bank liabilities, which includes advance import deposits, the increase observed over the last two years is more modest.

An important issue is whether the growth rates of broad money and liquidity are more reliable indicators of the stance of monetary policy than domestic credit expansion and interest rates. In 1987, domestic credit expansion to both the private and public sectors continued to decline steadily, while inflation-adjusted interest rates rose sharply and have remained at high levels since the middle of last year. Developments in domestic credit expansion reflect more accurately the joint evolution of the two variables which have been the main objectives of macroeconomic policy in recent years: nominal GDP growth, and thus inflation, and the balance of payments. The substantial and steady decline of domestic credit expansion in recent years not only reflects the progress made in reducing inflation and improving the net external position of the country, but also provides a positive indication regarding the future evolution of nominal national income. To the extent that the faster growth of broad money is the result of a portfolio shift from foreign to domestic assets, it does not necessarily imply an acceleration of inflation in the future, provided that the conditions which have influenced portfolio preferences are not reversed. In this respect, the conduct of an appropriate macroeconomic policy and maintenance of confidence are of crucial importance.

Finally, the high real interest rates are also more reliable indicators than money growth of the restrictive stance of monetary policy last year. The interest rate policy pursued in 1987, which is discussed in greater detail in the next section, played a major role in the success of the stabilisation effort. It helped contain the expansion of bank credit, contributed to the improvement in the current and capital accounts of the balance of payments, and supported a disinflationary exchange rate policy, which maintained competitiveness as measured by relative unit labour costs without fully accommodating inflation differentials. The policy of high real interest rates and relative exchange rate stability has been, and still is, necessary for the stabilisation of the economy until appropriate adjustments in fiscal policy are implemented and pressures on the financial and foreign exchange markets are mitigated. An early easing

of monetary policy could have serious negative consequences on inflation and the balance of payments.

5. LIBERALISATION OF INTEREST RATES AND OF THE BANKING SYSTEM

In 1987, significant steps were taken towards the liberalisation of bank interest rates and the abolition of a host of credit rules and regulations restricting the management of banks' portfolios. As a result of a series of measures taken by the Bank of Greece, only a few interest rates are still administratively determined. These are mainly interest rates on savings deposits, the special interest rates on loans to small and medium-size manufacturing firms, and the interest rates on loans under some categories of social housing programmes. In particular, commercial bank loans with market determined interest rates account for more than 80 per cent of commercial bank credit to the private sector, while in the case of investment banks the ratio rises to 100 per cent. As regards credit provided by the Agricultural Bank, minimum interest rates have been set for the bulk of its loans, while the interest rates on the remaining categories of its loans have been liberalised. Lastly, mortgage banks have been permitted to determine freely the interest rates on their housing loans.

The first step towards liberalising commercial bank deposit rates was taken in March 1987, when banks were granted permission to accept time deposits at market rates with maturities ranging from 7 days to 3 months. Then, at the end of June 1987, certificates of deposit were introduced, with maturities ranging from 3 to 18 months, at negotiable interest rates. Late in November 1987, commercial banks and other financial institutions were granted permission to determine: (i) interest rates on the other categories of time deposits with maturities of 3 months and over, and (ii) interest rates on deposits subject to notice and the length of time required for such notice. At the same time, credit institutions authorised to issue bank bonds were granted permission to determine the respective interest rates and other terms of issue. It should be noted that since the end of June 1987 interest rates on treasury bills have been fixed at a level slightly higher than interest rates on bank deposits with comparable maturities.

Liberalisation of bank lending rates started towards the end of June 1987 with the abolition of the maximum rate of 21.5 per cent on short-term credit and other categories of bank loans, accounting for about 55 per cent of commercial bank lending to the private sector. The minimum interest rate on

these loans was set at 21 per cent and banks were permitted to set lending rates above this minimum, in accordance with market conditions, maturity and credit risk. In connection with this minimum lending rate, it should be pointed out that it was unprofitable for the banks to offer their customers lending rates lower than 21 per cent, in view of: (i) the average rate on bank deposits, which is influenced by the interest rates on treasury bills, (ii) the existing reserve/rebate system on bank loans and (iii) the existing special levies on such loans. In practice, lending rates, following their partial liberalisation, rose and ranged initially between 22 and 25 per cent. Gradually, however, the average rate fell and at the end of 1987 was around 22.5-23 per cent.

The Bank of Greece intended to keep the minimum lending rate in force only for a transitional period. Thus this rate was abolished on 1 January 1988. At the same time, the first reduction was made (from 20 to 18 per cent) in reserves on bank credit to which the minimum lending rate of 21 per cent was applicable. The Bank of Greece intends to dismantle gradually the entire reserve/rebate system, so as to ensure eventually a structure of lending rates that will be based exclusively on banking criteria. As changes in reserve/rebate ratios have monetary repercussions, they will have to be decided on a case-by-case basis, in a manner that would not undermine the effectiveness of monetary policy.

As from the end of November 1987, interest rate liberalisation has been extended to long-term loans. The interest rates on these loans can be fixed or variable. Some banks have started to offer variable interest rates on long-term credit, thereby reducing their credit risk, while borrowers are protected during a period of decelerating inflation.

Parallel to the liberalisation of interest rates, the Bank of Greece took significant measures aimed at abolishing or simplifying the system of credit controls, and improving the flexibility of banks in managing their portfolios and setting the terms of borrowing. The most important of these measures is that commercial banks are no longer required to earmark 15 per cent of their deposits for financing fixed investment by private enterprises, a regulation which in practice had failed to promote private investment. Thus, an amount of 89 billion drachmas, which was previously required to be deposited with the Bank of Greece, was gradually released in the second half of 1987. In addition, a series of measures have been taken, which enable the banks to offer new services and adopt new methods of financing, provide for increased bank lending to business firms, abolish credit restrictions and simplify regulations on bank credit to private enterprises (see Appendix for a description of

some of these measures). Such measures, in conjunction with interest rate liberalisation, have strengthened competition in the banking system and have contributed to a more efficient allocation of economic resources.

It should also be noted that 1987 saw the completion of changes in the means of financing of the Agricultural Bank and mortgage banks by the central bank. As from 1 January 1988, these credit institutions are to finance their loans by attracting savings or by securing funds from sources other than the Bank of Greece. These specialised credit institutions may from now on resort to central bank funds only to meet unforeseeable and temporary liquidity shortages, by drawing on their current accounts with the Bank of Greece and paying interest at the high rates charged to commercial banks. Thus, besides investment banks, the Agricultural Bank and mortgage banks are also financed by the Bank of Greece on the same terms as commercial banks. In the second half of 1987, the Agricultural Bank was included — for the first time — in the system of reserve requirements, in order to control its liquidity.

Interest rate liberalisation and the abolition of a host of specialised credit rules and regulations have paved the way for the credit system's adjustment and modernisation. It should be noted that, in the second half of 1987, banks started to compete, although their response to the new environment has so far been fairly slow and inadequate. It is worth mentioning in this respect that although the reductions as from 1 January 1988 of the required reserve ratio on categories of bank credit and of the discount rate have established certain favourable, albeit limited, conditions to encourage a decrease in bank rates, the banks have maintained their lending rates virtually unchanged. Interest rates on time deposits remained essentially unchanged for a considerable period, despite high bank liquidity in the first quarter of 1988. Even after interest rates on three-month and six-month treasury bills were reduced by half a percentage point early last February, interest rates on time deposits remained at the same level for about one month. It should be noted, however, that since early March banks have been more active, especially as regards deposit rates.

The slow response of the banks to interest rate liberalisation is partly explained by the banks' effort to maintain their market share, even at the expense of profitability. Moreover, it would seem that banks were reluctant to promote treasury bill sales in the period immediately after the interest rates on treasury bills were readjusted at competitive levels. To some extent, however, this slow response should be attributed to the oligopolistic structure of the banking system, as well as to the complicated system of credit

controls and regulations and administratively determined interest rates that remained in effect for a long time and suppressed new initiatives. Lastly, it seems that certain credit institutions still hold the view that the central bank and the Government have to assure their profitability. Obviously, so long as this view prevails, it will hamper the smooth functioning and development of efficient financial markets. As a result, the adjustment of credit institutions is slow and insufficient to cope with the competitive environment emerging, especially in view of the forthcoming unification of the Community's financial markets. Furthermore, to the extent profitability of the banks is considered to be assured by the central bank, proper care may not be taken — to the extent required — in limiting credit risks and improving the quality of banks' portfolios.

Apart from the above reasons, the lack of well developed and efficient money and capital markets seems to have adversely affected competitive conditions and the modernisation of the banking system. Thus banks have essentially monopolised the financial intermediation process and have become complacent to some extent. This means that resort by Central Government and other public sector organisations — and gradually by private enterprises as well — to the nonbank market for financing a considerable and growing part of their borrowing requirements could have widespread favourable effects. Resort by the Government to the financial markets has already started exerting pressure on credit institutions to search for more efficient means of mobilising savings, better suited to savers' preferences. At the same time, it is forcing banks to upgrade the quality of their services and expand into new fields of banking to improve profitability. It should be noted that the foreign banks operating in Greece seem to be quicker at seizing the opportunities provided by interest rate liberalisation and the development of a money and capital market. In this respect, they are making a positive contribution to fostering competition and financial innovation.

As was stressed in last year's Report, it is the view of the Bank of Greece that pressure from competition is the most effective means of overcoming the conservative attitude and the rigidity which still characterise to some extent, despite the progress made, a considerable part of the Greek banking system. In the new deregulated environment, banks are offered considerable leeway for expanding into new, more profitable fields of financial activity and enhancing their profitability. Furthermore, in the Greek banking market there are possibilities and prospects for satisfactory profits for credit institutions that adjust faster to the new competitive environment and exploit the new opportunities

being offered. In keeping with its view that strengthened competitive conditions are necessary for a modernisation of the Greek banking system, the Bank of Greece has pursued, and will continue to pursue, policies which are neutral and do not discriminate between financial institutions.

Modernisation and rapid adjustment of the Greek banking system, and development of money and capital markets are essential prerequisites in order to withstand foreign competition after unification of the Community's financial markets in 1992, as capital movements will be liberalised and banks will be free to offer their services to both member and non-member countries. Greek banks are already modernising and adjusting, knowing that any delay will make it difficult for them to cope with competition from foreign banks, not only those operating branches in Greece, but also banks operating in the other member-countries, as the latter will be able to extend loans freely or provide other financial services to the domestic market. By contrast, substantial benefits of a more permanent character, for both the banks and the Greek economy, can accrue if they take advantage of the transitional period to reorganise operations, improve efficiency, and expand and upgrade the quality of the services they offer, parallel to the promotion of a broad and efficient money and credit market. Progress in the above areas would provide alternative portfolio opportunities to savers. This would stimulate saving and increase private capital inflows. Moreover, business firms would be able to diversify the sources and means of their financing, while the method and terms of borrowing by the public sector would be significantly influenced.

The Bank of Greece will continue to adapt its role to the new deregulated environment and encourage and support the modernisation of the country's credit system. To this end, the system of banking supervision is also being adjusted. A major obstacle, however, to the development of more competitive conditions in the banking sector are the requirements imposed on commercial banks to earmark a large part of their deposits for the financing of public sector deficits and small and medium-size manufacturing firms. Although gradual abolition of these requirements would contribute significantly to the creation of a competitive environment, it is not possible without parallel development of a large and efficient money and capital market.

II. ECONOMIC ACTIVITY

1. PRODUCTION AND NATIONAL INCOME

During 1987, second year of implementation of the stabilisation programme, economic activity decreased slightly following a slowdown in its growth rate in 1986, whereas the rate of unemployment remained at the 1986 level.

Public expenditure exerted a contractionary influence on the level of economic activity, while the effect of private expenditure was virtually neutral. Although external factors, such as international demand, interest rates and oil prices were not as favourable to the Greek economy in 1987 as in the previous year, the contribution of the foreign sector to economic activity was positive.

TABLE II.1
SECTORAL CHANGES AND CONTRIBUTION TO CHANGES IN REAL GDP
(At 1970 prices)

Sector	Annual percentage changes					Contribution to changes in real GDP				
	1983	1984	1985	1986 ¹	1987 ²	1983	1984	1985	1986 ¹	1987 ²
Primary	-8.9	7.0	1.9	0.6	-4.5	-1.3	0.9	0.3	0.1	-0.6
Secondary	0.2	1.2	3.7	0.3	-1.1	0.1	0.4	1.1	0.1	-0.3
(Mining & Quarrying)	(6.8)	(12.1)	(1.8)	(0.3)	(0.4)	(0.1)	(0.2)	(0.0)	(0.0)	(0.0)
(Manufacturing)	(-1.7)	(1.2)	(3.5)	(-0.1)	(-2.2)	(-0.3)	(0.3)	(0.7)	(0.0)	(-0.4)
(Electricity and Water Companies)	(3.8)	(5.8)	(6.4)	(2.6)	(6.1)	(0.1)	(0.2)	(0.2)	(0.1)	(0.2)
(Construction)	(3.3)	(-4.9)	(2.9)	(-0.1)	(-2.9)	(0.2)	(-0.3)	(0.2)	(0.0)	(-0.1)
Services	3.0	2.9	3.6	2.0	0.6	1.6	1.6	2.0	1.1	0.3
Gross domestic product	0.4	2.9	3.4	1.3	-0.6	0.4	2.9	3.4	1.3	-0.6

¹ Provisional data.

² Estimates.

Source: Ministry of National Economy; General Secretariat of NSSG.

According to provisional estimates of the National Accounts Directorate of the Ministry of National Economy, nominal GDP at factor cost increased by 12.9 per cent in 1987, compared with an increase of 18.4 per cent in 1986. If these growth rates are compared with those of GDP at constant prices, the GDP deflator shows a substantial deceleration from 16.9 per cent in 1986 to 13.6 per cent in 1987. This deceleration was due to the large drop in the rate of price increases of manufactured products (see Chapter III).

Real GDP at factor cost was down by 0.6 per cent in 1987 (see Table II.1). A decrease in real income by 4.5 per cent was registered in the primary sector and by 1.1 per cent in the secondary sector. These decreases were not offset by the 0.6 per cent growth of income from the services sector, whose share in GDP continued to rise and reached 57.1 per cent in 1987 (1986: 56.4 per cent). The positive development of income from services stemmed from income generated in social services, banking operations and housing. National income dropped at a slightly lower rate (-0.5 per cent) than that of GDP. This was the result of the reduction in the negative magnitude of net income from abroad, owing to the larger increase in receipts — compared with payments — mainly from shipping.

Besides the considerable decrease in the primary sector's product, mainly due to extremely adverse weather conditions, the level of manufacturing output declined substantially, for the first time after 1983. The decline of manufacturing output was due to reduced domestic demand combined with a continuing increase in import penetration. The growth in the volume of exports of manufactures did not fully offset the impact that reduced domestic demand had on manufacturing output.

2. AGRICULTURAL PRODUCTION

Following limited growth in 1985 (1.1 per cent) and stagnation in 1986, agricultural production in 1987 is estimated to have decreased by 2 per cent. This decrease stemmed from the lower output of arable crops (-4.1 per cent) as well as of tree crops (-9.8 per cent). In contrast, livestock production showed a considerable increase (5.5 per cent), which offset only partly the decrease of crop production.

Developments in crop production were due to the cold wave in March and the heat wave in the summer of 1987, which caused considerable damage to the production of several crops and to the overall crop capital. Damage caused by the heat wave in July was, however, limited since, during that period, most of growing crops were irrigated. By contrast, in non-irrigated crops, particularly that of sunflower, there was a substantial drop in yields.

The switching-over of arable crops in 1987 followed the trend in recent years (see Table II.2). There was a decrease in the areas under soft wheat, barley and alfalfa and a parallel increase in the areas under maize and sunflower. This switching-over was favourably affected by the resowing that fol-

lowed the adverse weather conditions in March. With the exception of burley tobacco and sugar beet, areas under the other basic arable crops remained near the corresponding levels of the previous year.

Developments in the volume of production of basic farm products were as follows:

Soft wheat production was below one million tonnes owing to reduced acreage and yields. The continuing reduction of soft wheat cultivation was

TABLE II.2
AREAS OF BASIC ANNUAL CROPS
(Thous. hectares)

Culture	1979/80 ¹	1983	1984	1985	1986	1987 ²	Increase/decrease (percentage) between two-year periods 1979/80 & 1986/87
Soft wheat	725.4	699.6	606.3	510.3	439.6	357.7	-45
Durum wheat	222.5	308.4	312.2	372.2	432.1	428.4	+93
Barley	352.2	327.9	333.1	326.4	296.5	199.8	-30
Maize	142.5	172.7	205.7	205.9	202.6	245.5	+57
Alfalfa	205.0	178.6	168.0	158.6	154.4	153.4	-25
Tomatoes for processing	23.5	28.1	28.3	29.2	16.9	17.6	-27
Tobacco (oriental)	85.8	83.1	82.1	88.6	92.6	89.6	+ 6
Tobacco (burley)	5.5	9.6	10.6	10.2	6.9	5.0	+ 8
Cotton	138.8	168.0	192.0	209.0	210.0	202.0	+48
Sugar beet	37.0	38.6	28.5	43.5	43.7	28.2	- 3
Sunflower	2.3	12.9	41.8	49.9	79.1	90.6	+3.589

¹ Two-year average.

² Provisional data.

Source: Ministry of Agriculture.

mainly due to the lower returns of this crop, compared with that of sunflower; as a result, in the last few years its production has been lagging behind domestic needs.

Acreage and production of durum wheat were near the 1986 level. The reduction of soft wheat cultivation was accompanied by an increase of the area under durum wheat which, for the first time, exceeded by 20 per cent the area under soft wheat. This development was mainly due to the common aid per hectare for durum wheat which amounts to more than 10 per cent of the average durum wheat receipts. Since annual domestic consumption is around 300 thousand tonnes, excess quantities are mostly exported to EEC countries. However, the parallel increase in production of the other EEC countries has begun to hamper sales of Greek durum wheat to the Community.

Barley production showed a considerable decrease (-15.4 per cent) owing to a reduction in cultivated areas. The drop in production lessens even more the degree of the country's self-sufficiency in barley, which in the last few years has been around 80 per cent.

TABLE II.3
OUTPUT OF BASIC AGRICULTURAL PRODUCTS
(Thous. tonnes)

Products	1979/80 ¹	1983	1984	1985	1986	1987 ²	Percentage change between two-year periods 1979/80 & 1986/87
Soft wheat	2,142	1,476	1,717	1,114	1,283	952	-48
Durum wheat	522	568	904	661	1,210	1,158	+127
Barley	896	578	818	619	740	626	-24
Maize	982	1,654	1,913	1,822	1,985	2,412	+124
Alfalfa	2,123	1,805	1,772	1,637	1,570	1,624	-25
Leaf tobacco (oriental varieties)	104	84	111	118	128	132	+25
Leaf tobacco (burley variety)	18	26	32	31	20	13	- 8
Cotton (natural)	336	402	452	520	634	548	+76
Tomatoes for processing	1,476	1,265	1,702	1,475	932	974	-35
Sugar beet	2,120	2,500	1,654	2,650	2,562	1,700	—
Sunflower (seed)	4	26	67	85	164	133	+3,613
Dried grapes	132	177	154	165	145	129	+ 4
Olive- oil	266	222	230	344	218	230	-16
Lemons	160	188	155	186	187	88	-14
Oranges	410	690	775	554	869	460	+62
Apples	271	319	289	257	312	295	+12
Peaches	336	484	520	532	512	545	+57
Meat, total	504	514	509	515	491	529	+ 1
— Beef and veal	(100)	(86)	(85)	(82)	(82)	(86)	(-16)
— Goat and sheep	(121)	(121)	(122)	(122)	(107)	(125)	(- 4)
— Pigmeat	(139)	(149)	(146)	(152)	(153)	(164)	(+14)
— Poultry	(140)	(154)	(152)	(155)	(145)	(149)	(+ 5)
— Other	(4)	(4)	(4)	(4)	(4)	(5)	(+12)
Milk, total	1,698	1,687	1,687	1,702	1,720	1,707	+ 1
— Beef and veal	(699)	(677)	(664)	(648)	(643)	(633)	(- 9)
— Goat and sheep	(999)	(1,010)	(1,023)	(1,054)	(1,077)	(1,074)	(+ 8)

¹ Two-year average.

² Provisional data.

Source: Ministry of Agriculture.

The cultivated areas and production of maize in 1987 were higher by nearly 21 per cent than in the year before. This considerable increase was also

due to the resowing of areas under winter cereals damaged by the cold wave in March. Despite the hot spell in July, the yield per hectare of this crop was around the 1986 level. The substantial increase of production in 1987 is expected to lead to higher net sales to EEC countries. The self-sufficiency degree of the EEC (around 75 per cent) and the high competitiveness of Greek maize in terms of quality and cost, owing to high yield per hectare, provide possibilities for further crop expansion.

The reduction in cotton cultivation in 1987, combined with the drop in the yields below the exceptionally high levels of 1986, led to a decline in natural cotton output by nearly 90 thousand tonnes. It is estimated, however, that production will cover domestic needs and leave a small surplus to be exported.

The expansion of sunflower cultivation, which mainly stemmed from the sowing of sunflower in soft wheat and barley areas, did not result in higher production since non-irrigated crops were heavily affected by the hot spell in July. The average yields per hectare of non-irrigated and irrigated lots dropped by 28 and 5 per cent respectively; as a result, total sunflower output, despite a considerable expansion of cultivation, was 20 per cent lower than in 1986.

The production of tomatoes for industrial processing in 1987 was slightly higher than in 1986, yet lower, for the second consecutive year, than the EEC-guaranteed national threshold of production of 1,013 thousand tonnes. The low levels of cultivation and production in the last two years were due to difficulties experienced in selling the processed product from previous, comparatively high, crops.

Low earnings — compared with other competitive crops, particularly maize — of sugar beet producers from the 1986 crop, combined with damages from bad weather in March, reduced considerably the acreage and production of sugar beet in 1987. Reduced sugar production is estimated to have covered two-thirds of annual domestic consumption (around 300 thousand tonnes).

The production of oriental tobacco expanded slightly in 1987, despite a small decrease in the areas under crop. This expansion was mainly due to the varieties of "mavra" and "tsebelia" which, however, belong to the group of varieties the Community seeks to reduce. These varieties have found their way, during the last few years, into the markets of non-EEC countries and producer prices and sales conditions of these products permitted the expansion of cultivation and production. By contrast, acreage and production of

burley tobacco suffered a considerable decrease in 1987. This was due to comparatively low producer prices in the last two years, which reflected the existence of large stocks and sales difficulties in the world market. The upward trend in cultivation and production of the promoted Virginia variety continued in 1987 at a brisk pace. Production doubled along with doubled areas under crop. Inasmuch as the processing of Virginia tobacco includes its drying in furnaces, further expansion of production is closely connected with the creation of the proper infrastructure.

Adverse weather conditions, already mentioned, reduced production of certain tree crops to nearly half of their normal output. A particularly unfavourable effect was exerted on the production of walnuts, almonds, table olives and citrus fruit, while production of the remaining tree crops was not affected severely in 1987 and came to a slightly lower level than in 1986. Conversely, production of olive-oil increased (5.5 per cent), owing to favourable weather conditions during flowering time.

Following a decrease of 2.7 per cent in 1986 and relative stagnation in the previous years, livestock production increased considerably (5.5 per cent). A part of this increase was due to the higher output of goat and sheep meat, while production of beef and veal, pigmeat and poultry meat made a positive contribution. The substantial increase in goat and sheep meat in 1987 is attributed to the restoration of the slaughter rate to normal levels and to the exceptional increase of headage registered in the year before. Conversely, the growth of beef and veal output was due to the higher number of calves imported for fattening.

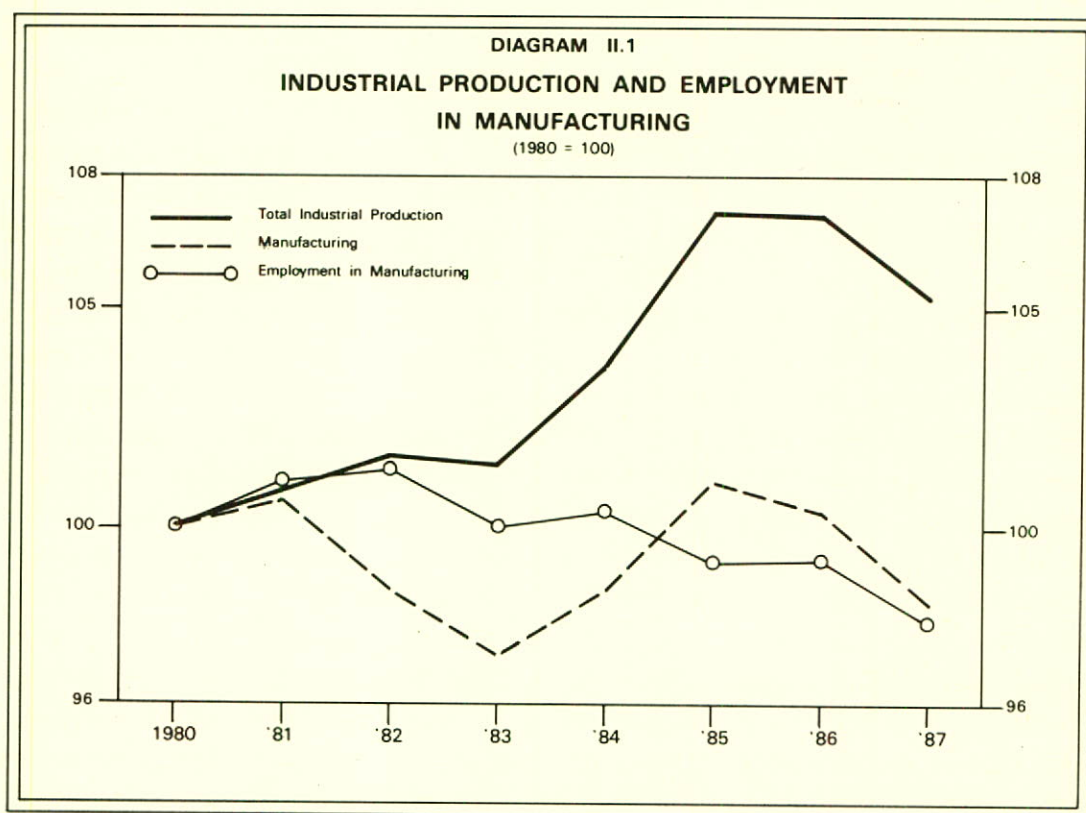
3. SECONDARY PRODUCTION

The product of the secondary sector of the economy decreased in 1987, thus reflecting the decline in the output of manufacturing and construction, whereas electricity and gas production increased (see Table II.1). Construction dropped by 2.9 per cent, compared with stagnation in 1986 and an increase of 2.9 per cent in 1985. This drop was the result of the significant decline in the public sector's construction activity, which was not offset by the growth of activity in the private sector.

Analytically, developments in industry by branch of activity were as follows.

a) *Manufacturing*

The course of manufacturing production in 1987 was determined by developments and the structure of total demand. Manufacturing production dropped by 2 per cent (see Table II.4 and Diagram II.1), owing to reduced domestic demand for Greek manufactures, which was not counterbalanced by the growth of exports. This was due to the decline of private disposable income and to the increase of import penetration, inasmuch as there seemed to be no problems of quantitative insufficiency on the supply side.



The estimated drop of private consumption by 0.7 per cent, combined with the increase of import penetration by 1.5 percentage points (nine-month period data, see Table II.2), must have led to the decline of internal "apparent" consumption of domestic manufactures (production minus exports). Furthermore, according to the data of the survey conducted by the Institute

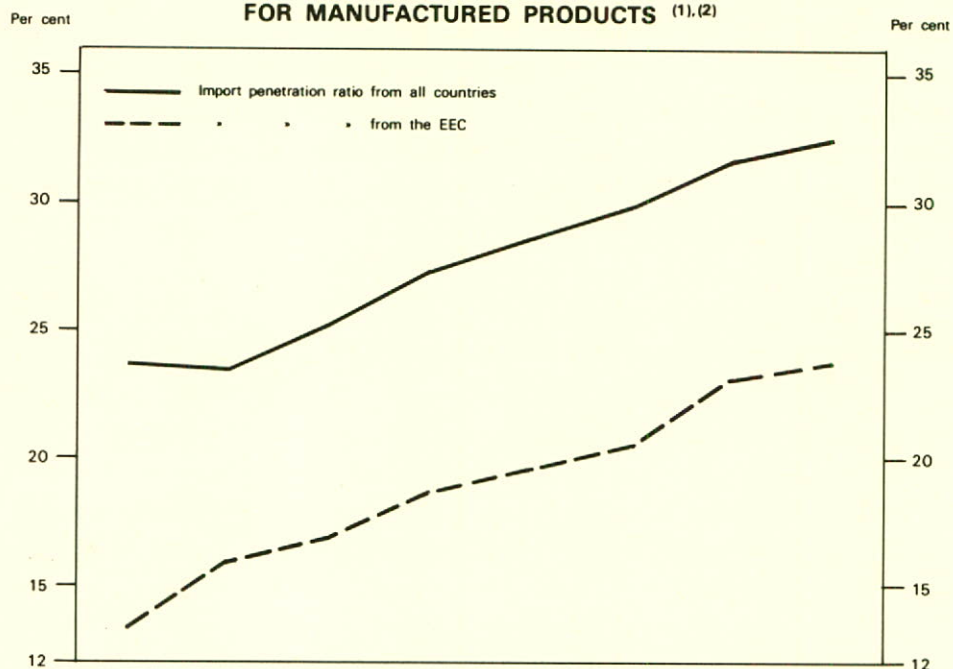
of Economic and Industrial Research, the stocks of finished products in manufacturing grew in the first half of 1987 and then showed signs of decline, a fact which supports the view that there was a slackening of demand for domestic products.

As regards foreign demand, the volume of exports of manufactured products, excluding oil, according to payments data deflated by the wholesale price index for exported manufactures, showed an estimated increase of nearly 20 per cent in 1987. This rate, however, overestimates the growth of the volume of exports realised and, consequently, their contribution to production. The real growth rate of exports in 1987 must have been smaller, as suggested by the latest available data of the NSSG for the volume of exports of manufactures, which show an increase of 1.5 per cent in the nine-month period January-September 1987, compared with the same period in 1986. The divergence between payments and customs statistics data is probably due, besides the usual reasons, to the acceleration of exports in the second half of 1986, owing to the anticipation of considerably smaller export subsidies as from 1 January 1987. It is to be noted that the growth of exports of manufactured products in 1986 is estimated at 3 per cent, according to payments statistics, whereas the corresponding index of the NSSG showed an increase of nearly 26 per cent in the same period. The growth of Greek exports in 1987 was realised under conditions of slower growth of international demand, as shown by OECD estimates for imports of manufactures by member countries (1987: 6.5 per cent; 1986: 9.7 per cent). The continuing growth trend of exports of manufactured products is also attested by the increase of the average propensity to export (at current prices) to all countries and particularly to EEC members (see Diagram II.2). The growth of the volume of exports was also affected by the improvement of competitiveness, which was mainly due to the containment of labour costs and to the foreign exchange policy pursued. In particular, the increase in unit labour cost was contained to 11 per cent (1986: 13.3 per cent), while the average effective depreciation of the drachma was 11 per cent. Furthermore, according to the relevant index of the Bank of Greece, prices of raw materials increased by 10.8 per cent, compared with an increase of 16.2 per cent in 1986.

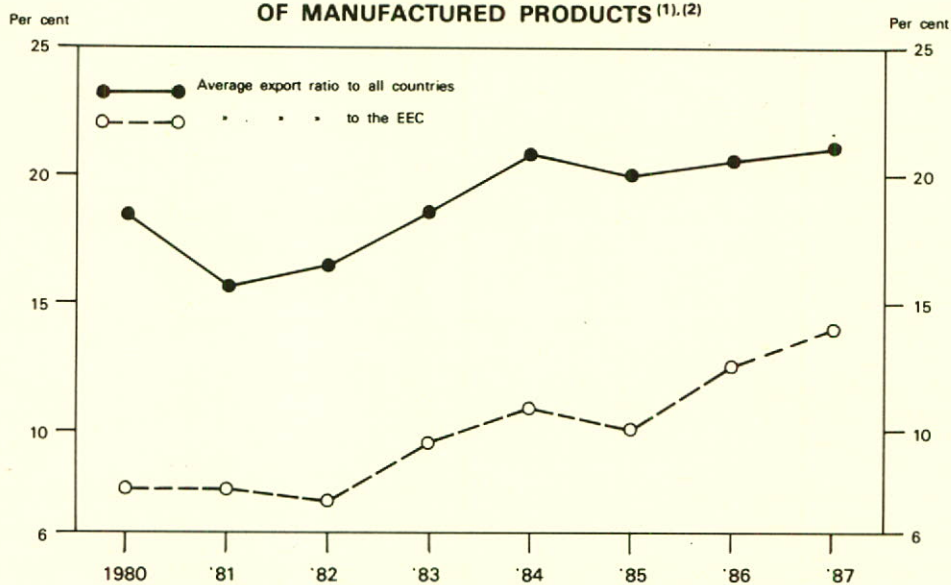
As regards developments in individual manufacturing sectors in 1987, there was a decrease in all three basic categories of manufactures: production of consumer goods dropped by 1.3 per cent, capital goods by 4.3 per cent, while production of consumer durables showed a substantially larger decrease (-12.2 per cent).

DIAGRAM II.2

IMPORT PENETRATION RATIO FOR MANUFACTURED PRODUCTS (1),(2)



AVERAGE EXPORT RATIO OF MANUFACTURED PRODUCTS (1),(2)



(1) The figures for 1987 are estimates based on data for the first 9 months.
 (2) At current prices.

NSSG data show that the reduction in the output of consumer goods stemmed from the decline in production of all branches except textiles and leather. The decline in production of food, beverages and tobacco (-5.9 per

TABLE II.4
INDUSTRIAL PRODUCTION
(Average percentage change over previous year)

	1983	1984	1985	1986	1987*
INDUSTRY	- 0.3	2.4	3.3	- 0.3	- 1.5
Manufacturing	- 1.4	1.3	2.5	- 0.7	- 2.0
a. Consumer goods	0.8	2.7	3.1	0.2	- 1.3
b. Consumer durables	- 8.2	- 7.6	11.4	4.2	-12.2
c. Capital goods	- 5.1	- 1.3	- 0.7	- 2.3	- 4.3
Manufacturing industries					
Foodstuffs	1.1	9.9	2.6	-9.5	- 5.4
Beverages	0.5	5.6	12.5	3.4	- 3.2
Tobacco	8.5	- 6.2	11.4	- 7.5	-14.2
Textiles	- 2.0	0.0	3.8	6.8	2.7
Footwear and clothing	- 8.0	- 1.8	8.4	- 1.3	- 7.1
Wood and cork	- 1.1	-11.6	-12.7	- 2.1	4.1
Furniture	-34.2	- 7.6	11.7	- 4.7	- 7.5
Paper	-11.8	11.5	15.8	15.2	15.1
Printing and publishing	0.0	7.2	6.6	-12.2	- 0.8
Leather	- 1.1	- 6.0	- 1.6	1.2	18.6
Rubber and plastics	4.9	- 1.1	6.0	-10.4	- 4.5
Chemicals	7.6	8.2	6.7	- 4.9	0.1
Petroleum and coal products	- 1.1	- 1.2	- 1.5	12.3	8.1
Non metallic minerals	- 3.5	1.8	- 2.6	3.2	3.0
Basic metals	9.0	2.2	1.6	- 4.0	- 2.4
Metallurgical products	- 1.1	- 1.1	-10.9	7.4	-14.5
Machinery and apparatus, excluding electrical	- 9.4	-11.4	8.5	-10.5	-10.4
Electrical machinery and appliances	- 5.3	- 6.9	15.5	0.7	-14.3
Vehicles	-13.8	- 6.8	-16.7	9.3	1.8
Miscellaneous	3.5	23.3	10.7	-18.7	9.8
Mining and quarrying	8.8	10.3	2.5	1.2	- 2.3
Electricity and gas	2.3	3.8	13.3	1.9	6.6

* Provisional data.

Source: Ministry of National Economy; General Secretariat of NSSG.

cent) is attributed to reduced demand for domestic products. It seems that the considerable growth (9.1 per cent) of consumption of these products, as shown

in the relevant volume index of retail sales, was satisfied by imports. This is illustrated by the increase of import penetration in the above three branches by one percentage point (at constant prices) during the nine-month period January-September 1987, compared with the same period in 1986.

The growth of foreign demand for textiles must have contributed to the 2.7 per cent increase in the production of this branch, whereas the contribution of domestic demand was negative. At the same time a significant increase of stocks of finished products was witnessed, according to data compiled by the Institute of Economic and Industrial Research, as well as a continuing upward trend of import penetration, which during the nine-month period January-September increased, at constant prices, by nearly 1.5 percentage point.

By contrast, production of footwear and clothing dropped by 7.1 per cent; this seems to have been due to the decline of domestic demand, which was accentuated by the growth of import penetration (at constant prices). Conversely, exports exhibited a spectacular increase. Specifically, the volume index of retail sales of these articles decreased by 3.6 per cent, whereas the volume of exports and imports, according to payments statistics, grew by 24 and 23 per cent respectively. The volume indices of the NSSG show respective increases of 13 and 14 per cent during the nine-month period.

Lastly, the downward trend in the production of capital goods continued in 1987; this was directly connected with reduced total domestic investment activity, whereas foreign demand increased. Reduced production of capital goods stemmed from all individual sectors, with the exception of non metallic minerals (3 per cent) mainly due to the higher production of refractories (15.9 per cent). The decline in the production of basic metallurgy (-2.4 per cent) was due to lower output of the main products, like cast iron (-1.4 per cent) and ferronickel (-10.2 per cent), whereas the output of alumina-aluminium was higher (1.5 per cent). It should be noted that the volume of alumina-aluminium exports grew by about 23 per cent in the nine-month period January-September. This favourable development reflects the improvement of foreign demand for aluminium, the reduction of stocks in the international market and the rise in prices of this product in terms of U.S. dollars. As regards the steel industry, it is to be noted that in Greece, as well as in the other EEC countries, this industry is subject to a special regime of production quotas and its output is expected to decline further.

As regards increasing import penetration, available data for the nine-month period January-September 1987 show that this refers both to consumer goods (mainly textiles and footwear-clothing) and to capital goods (basic metals

and vehicles). In general, following Greece's accession to the EEC, it was noticed that the increase in import penetration was higher in those traditional industries which, from 1981 onwards, have been showing a high export performance, mainly to EEC countries. This development shows: first, that domestic industry, following the two oil crises and Greece's accession to the EEC, tends to specialise in products where it enjoys comparative advantages. This finding is also upheld by the structure of industrial investment in the last few years on the basis of increased horsepower. Second, that a retrospective study of these developments indicates that there is, in the medium run, scope for quantitative and qualitative progress in these industries, without, of course, underestimating, in the long run, the potential contribution of the remaining branches of manufacturing, provided they are technologically upgraded.

b) Mining and Quarrying

According to the index compiled by the NSSG, mine and quarry production dropped by 2.3 per cent in 1987, compared with an increase of 1.2 per cent in

TABLE II.5
PRODUCTION OF MINERALS AND ORES
(Average percentage change over previous year)

	1983	1984	1985	1986	1987*
TOTAL	8.8	10.3	2.5	1.2	- 2.3
Lignite	1.9	13.2	15.5	7.8	2.5
Bauxite	-16.3	- 3.9	3.6	- 4.7	9.2
Iron and nickel ores	158.8	43.1	17.9	-46.6	-11.2
Chrome and manganese ores	- 2.4	83.7	25.8	1.1	2.4
Oil wells and extraction of natural gas	20.4	7.1	0.6	0.4	- 5.0
Quarry and construction materials	0.0	12.2	- 0.7	2.5	- 2.4
Sulfur compounds, barytes	2.3	6.0	- 8.7	0.3	- 4.9
Magnesite	- 8.0	31.2	-16.0	- 2.3	-6.7

* Provisional data.

Source: Ministry of National Economy; General Secretariat of NSSG.

1986 (see Table II.5). Reduced output of certain products, such as lead and magnesium carbonate ores, was due to the considerable decline of foreign demand. For other products, however, reduced output reflected unfavourable

conditions of demand from manufacturing industries, such as the iron and nickel industries, which use these ores as inputs. The growth of domestic demand for lignite, used in electricity production, contributed to higher production (2.5 per cent). Conversely, the reduction of total construction activity seems to have affected negatively the production of quarry and construction materials (-2.4 per cent).

c) Electricity and Gas

According to the relevant NSSG index, electricity and gas production in 1986 grew by 6.6 per cent (1986: 1.9 per cent). This acceleration stemmed both from electricity (6 per cent) and from gas production (23.4 per cent). In particular, on the basis of PPC data, electric energy production totalled 27,335 GWH against 25,624 GWH in 1986. At the same time, installed capacity grew by 610 MW, owing to the start-up of two steam-electric stations at Amyntaion (600 MW) and smaller diesel-operated units on a number of islands. On the demand side, there was an increase of 4.2 per cent, which stemmed chiefly from higher electricity consumption in households (9.4 per cent) and commercial establishments (8.4 per cent). By contrast, electricity consumption by industry declined by 1 per cent. The increase of production at a rate higher than that of domestic demand led to a decrease of net imports of electric energy, which met 2.4 per cent of domestic requirements against 5.2 per cent in 1986.

4. SERVICES

As in 1986, income from services increased at a decelerating pace in 1987. However, the share of services in GDP expanded further and reached 57.1 per cent¹ owing to decreased income from material production. The growth trend of the relative size of the tertiary sector, after the second oil crisis, was accompanied by a reduced share of the secondary sector, particularly manufacturing. The expansion of the tertiary sector in the period 1980-1987 was

¹ The size of the tertiary sector, as indicated in national accounts, is probably underestimated, owing to the "underground economy" which seems to concentrate more in services than in the other sectors of the economy.

due to the growth of market services and social services, which increased at average annual rates of 2.2 and 2.4 per cent respectively (see Table II.6),

TABLE II.6
INCOME FROM SERVICES
(At 1970 prices)

	Annual percentage changes					Average annual rate (%)	Percentage structure	
	1983	1984	1985	1986 ¹	1987 ²		1980	1987 ²
A. Market Services	3.2	3.0	4.0	2.0	0.4	2.2	75.5	75.3
Transport-Communications	3.5	6.9	6.1	1.2	0.0	3.1	18.0	19.1
Trade-Banking etc.	5.2	0.5	4.4	3.3	-0.8	1.8	27.8	27.1
Housing	3.2	2.9	2.2	2.5	3.0	3.1	17.2	18.2
Miscellaneous Services	-1.7	2.9	2.1	-0.4	-0.4	0.3	12.5	10.9
B. Social Services	2.4	2.7	2.5	1.9	1.2	2.4	24.5	24.7
Public Administration-Security	2.5	4.8	2.2	1.2	...	...	16.6	...
Health-Education	2.4	-1.8	3.2	3.3	...	...	7.9	...
Total Services	3.0	2.9	3.6	2.0	0.6	2.2	100.0	100.0

¹ Provisional data.

² Estimates.

Source: Ministry of National Economy; General Secretariat of NSSG.

compared with a stagnation of income from material production. It should be noted that the share of income from services in GDP is already at a high level approaching that of developed economies (see Table II.7).

TABLE II.7
PERCENTAGE STRUCTURE OF GDP, 1985
(At 1980 prices)

	Agriculture	Secondary Sector	Services
U.S.A	2.8	32.6	64.6
Japan	3.1	42.4	54.5
W.Germany	2.3	38.6	59.1
France ^{1,3}	5.8	38.4	55.8
United Kingdom	2.1	40.1	57.8
Italy ¹	6.5	39.9	53.6
Spain	6.9	36.2	56.9
Netherlands	4.6	32.9	62.5
Belgium	2.5	33.9	63.6
Austria ²	4.8	41.6	53.6
Greece ¹	13.5	30.5	56.0

¹ At 1970 prices.

² At 1976 prices.

³ Year 1984.

Source: OECD, National Accounts 1973-1985.

Analytically, the small growth of income from services in 1987 was due to social services, which showed a limited increase compared with previous years, and to income from banking and housing. Income from transport and communications remained stagnant, owing to reduced communications volume, for the first time after a lengthy period of constant growth. The reduction of communications volume was barely covered by the increase in the volume of transport services, mainly aviation. A small decrease was seen in income from trade and banking, owing to the reduction in the volume of trade, which was not offset by the growth of banking business. A decrease was also recorded, for the second consecutive year, in income from "miscellaneous services", mainly owing to reduced domestic tourism. By contrast, income from housing rose at a slightly higher rate than in 1986, reflecting the larger increase in dwellings, as a result of higher private building activity.

5. EXPENDITURE OF THE ECONOMY

According to provisional estimates of the Directorate of National Accounts, the aggregate expenditure of the economy, at constant prices, decreased by 1.2 per cent in 1987, against a decrease of 0.6 per cent in 1986 and an increase of 5.7 per cent in 1985 (see Table II.8). The drop in expenditure at a rate faster than that of GDP led to a decline of the external deficit, that is of the balance of goods and services on a national accounts basis, and stemmed from both total consumption and fixed capital formation. The structure of GDP at market prices did not record a significant change in the last two years, while in the period 1970-1987, when the two oil crises affected inflation and consumer behaviour, there was a distinct upward trend of the share of total consumption in GDP, from 81.8 per cent in 1970 to 85.2 per cent in 1987, with a parallel reduction of the share of investment from 23.6 per cent to 14.9 per cent respectively (see Table III.9). During the same period the deficit in the balance of goods and services, at 1970 prices, fluctuated, dropping finally from 8.4 to 3.7 per cent of GDP. It should be noted that these percentages do not add up to 100 per cent of GDP, which includes the change in stocks and statistical discrepancies.

Analytically, developments in aggregate expenditure in 1987 were as follows:

Private consumption declined, for the first time after 1980, mainly because of the drop in real disposable income for the second year running.

The decline of private consumption, which was slower than that of disposable income, led to a saving rate of about 16 per cent, which is the lowest in the last 15 years. Conversely, public consumption, despite the implementation of the stabilisation programme, increased, compared with stagnation in the year

TABLE II.8
GROSS EXPENDITURE OF THE ECONOMY
(At 1970 prices)

	Annual percentage changes					Contribution to changes in real GDP				
	1983	1984	1985	1986 ¹	1987 ²	1983	1984	1985	1986 ¹	1987 ²
Consumption	0.8	1.9	3.4	0.0	-0.3	0.7	1.6	2.9	0.0	-0.3
(Private)	(0.4)	(1.6)	(3.5)	(0.0)	(-0.7)	(0.3)	(1.1)	(2.4)	(0.0)	(-0.5)
(Public)	(2.7)	(3.0)	(3.2)	(0.0)	(1.3)	(0.4)	(0.5)	(0.5)	(0.0)	(0.2)
Gross fixed capital formation	-1.3	-5.7	5.2	-5.7	-2.3	-0.2	-1.0	0.8	-0.9	-0.3
(Private)	(-7.1)	(-13.3)	(2.3)	(2.4)	(4.0)	(-0.9)	(-1.6)	(0.2)	(0.2)	(0.4)
(Public)	(13.4)	(10.1)	(10.0)	(-18.1)	(-14.2)	(0.7)	(0.6)	(0.6)	(-1.1)	(-0.7)
Changes in stocks ³	0.7	1.8	2.0	1.1	} 3.6	-1.3	1.0	0.3	-0.8	} -0.6
Statistical discrepancies ³	2.0	0.2	2.0	3.1		1.4	-1.8	1.9	1.1	
Gross expenditure of the economy	0.6	-0.1	5.7	-0.6	-1.2	0.6	-0.1	5.9	-0.6	-1.2
Balance of goods and services ³ (net balance)	-6.6	-3.7	-6.4	-4.3	-3.6	-0.2	2.9	-2.8	1.8	0.6
(Imports of goods and services)	(6.6)	(0.2)	(12.8)	(3.6)	(...)	(-1.5)	(-0.1)	(-3.0)	(-0.9)	(...)
(Exports of goods and services)	(8.0)	(16.9)	(1.3)	(14.0)	(...)	(1.3)	(3.0)	(0.3)	(2.7)	(...)
Gross Domestic Product at market prices	0.4	2.8	3.1	1.2	-0.6	0.4	2.8	3.1	1.2	-0.6

¹ Provisional data.

² Estimates.

³ As a percentage of the previous year's GDP in the columns of annual changes.

Source: Ministry of National Economy; General Secretariat of NSSG.

before, owing to the growth of expenditure for the purchase of goods connected with the country's defence, and for salaries. The growth of expenditure for salaries reflects the increase in the number of employees as well as higher seniority benefits due to the "ageing" of personnel.

Gross fixed capital formation recorded a decrease, which stemmed exclusively from the public sector, whereas private investment increased for the second consecutive year (see Table III.10). It should be noted that the recovery of private investment occurred mainly in housing (8.8 per cent), manufacturing (7.7 per cent) and vehicles (5.6 per cent).

An analysis of long-run developments in investment structure shows a decline of the share of investment in construction, from 73 per cent of total investment in the beginning of the 1960s to 55 per cent in the last few years, while there is a corresponding increase of the share of investment in machinery (vehicles and mechanical equipment). These changes in the structure of investment indicate that investment in mechanical equipment related mainly to the replacement of obsolete equipment. This view is supported by NSSG data for installed horsepower, which grew faster in existing plants than in new ones.

TABLE II.9
GROSS EXPENDITURE OF THE ECONOMY
(At 1970 prices)

	Percentage structure							
	1960	1970	1980	1983	1984	1985	1986	1987*
Consumption	89.5	81.8	81.5	86.5	85.8	86.0	85.0	85.2
(Private)	(75.2)	(69.2)	(67.0)	(70.3)	(69.5)	(69.8)	(68.9)	(68.8)
(Public)	(14.3)	(12.6)	(14.5)	(16.2)	(16.3)	(16.2)	(16.1)	(16.4)
Gross fixed capital formation	20.3	23.6	19.6	17.4	16.0	16.3	15.2	14.9
(Private)	(13.4)	(17.0)	(14.9)	(11.7)	(9.9)	(9.8)	(9.9)	(10.4)
(Public)	(6.9)	(6.6)	(4.7)	(5.7)	(6.1)	(6.5)	(5.3)	(4.5)
Changes in stocks	-0.6	4.5	4.1	0.7	1.7	1.9	1.1	} 3.6
Statistical discrepancies	-3.5	-1.5	-3.3	2.0	0.1	2.0	3.0	
Gross expenditure of the economy	105.7	108.4	101.9	106.6	103.6	106.2	104.3	103.7
Balance of goods and services (net balance)	-5.7	-8.4	-1.9	-6.6	-3.6	-6.2	-4.3	-3.7
(Imports of goods and services)	(-13.3)	(-18.4)	(-20.6)	(-24.1)	(-23.5)	(-25.7)	(-26.3)	(...)
(Exports of goods and services)	(7.6)	(10.0)	(18.7)	(17.5)	(19.9)	(19.5)	(22.0)	(...)
Gross Domestic Product at market prices	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

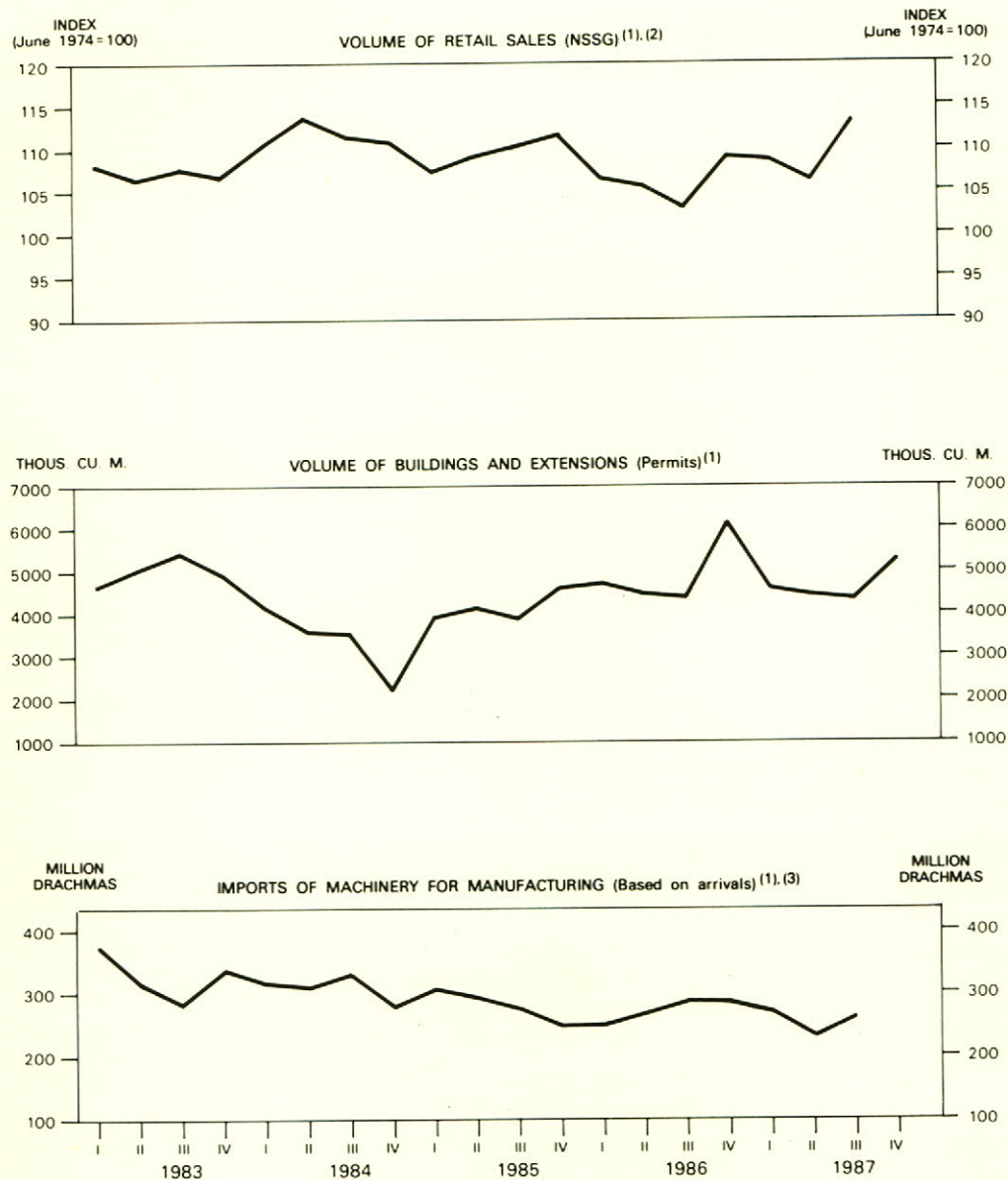
* Estimates.

Source: Ministry of National Economy; General Secretariat of the NSSG.

During the last few years, particularly after the enacting of the development-promoting Law 1262/82 and the implementation of a series of measures to modernise the banking sector, the capital market and other administrative mechanisms, a favourable business climate has been created, which encourages new investment initiatives in the private sector.

DIAGRAM II.3

MAIN ECONOMIC INDICATORS



(1) Quarterly seasonally adjusted data.

(2) Deflated by the consumer price index (special index for goods).

(3) At 1970 prices.

TABLE II.10
ANNUAL RATES OF CHANGE (1983 - 1987)
AND PERCENTAGE STRUCTURE (1960 - 1987)
OF GROSS FIXED INVESTMENT
(At 1970 prices)

	Annual rates of change					Percentage structure			
	1983	1984	1985	1986	1987 ¹	1960 ²	1970 ³	1980 ⁴	1985 ⁵
Total	- 1.3	- 5.7	5.2	- 5.7	- 2.3	100	100	100	100
<i>Breakdown by item</i>									
Housing	3.6	-19.1	0.1	13.5	8.2	31	31	29	24
Other dwellings	3.0	3.3	- 6.2	5.8	- 3.0	15	14	13	12
Other works and constructions	9.5	3.7	12.0	-15.3	-18.0	27	23	17	19
Transport means	-31.8	-19.0	14.0	-19.4	5.3	7	8	16	12
Other equipment	7.4	2.3	5.5	-10.1	-3.2	20	24	25	33
<i>Breakdown by sector</i>									
Agriculture - Livestock etc.	6.4	25.6	2.1	-35.6	-19.7	15	10	8	7
Mines - Quarries	- 0.9	- 1.9	8.4	-40.3	-18.5	1	2	5	4
Manufacturing	- 6.9	- 0.1	-8.6	18.1	- 4.9	12	13	15	15
Electricity - Water supply - Sewerage	29.0	- 2.4	19.7	-30.3	-10.7	8	9	7	11
Transport - Communications	-17.2	-12.8	12.0	-17.9	- 3.4	18	20	22	22
Housing	3.6	-19.1	0.1	13.5	8.2	31	31	29	24
Other activities	4.4	4.8	7.2	11.4	- 0.4	15	15	15	17
<i>Breakdown by agency</i>									
Private	- 7.1	-13.3	2.3	2.4	4.0	66	70	75	65
(Housing)	(4.6)	(-19.7)	(-0.5)	(14.6)	(8.8)	(29)	(30)	(28)	(23)
(Other)	(-12.8)	(- 9.5)	(3.7)	(- 3.5)	(1.2)	(37)	(40)	(47)	(42)
Public	13.4	10.1	9.9	-18.1	-14.2	34	30	25	35
Total (million dracmas)						28.832	72.250	90.555	79.432

¹ Estimates.

² Average 1958-62.

³ » 1968-72.

⁴ » 1978-82.

⁵ » 1983-87.

Source: Ministry of National Economy; General Secretariat of NSSG.

6. EMPLOYMENT - UNEMPLOYMENT

According to the annual sample survey carried out by the National Statistical Service of Greece, total employment dropped by 0.9 per cent in 1987 (see Table II.11), compared with a small increase in 1986. This was the result of a

drop of employment in rural areas, which was not offset by its increase in urban and semi-urban areas.

As regards employment by sectors of activity, the relevant index of the NSSG for manufacturing declined by 1.3 per cent, a fact which is consistent with developments in manufacturing production. By contrast, there was an increase in the number of civil servants (1987: 1.5 per cent; 1986: 1.2 per cent) as well as employees of public enterprises (1987: 0.8 per cent; 1986: 1.3 per cent) and of banks (1987: 1 per cent; 1986: 1.8 per cent).

Despite the decrease of total employment, registered unemployment did not expand, owing to the decline of manpower. This decline stemmed mainly from the substantial reduction of agricultural manpower (by 55,000 people), possibly as a result of domestic migration. The movement of manpower may not have been fully registered in urban manpower owing among

TABLE II.11
POPULATION, MANPOWER AND EMPLOYMENT
(In thousands)

	1981	1982	1983	1984	1985	1986	1987 ¹
Population, age 15-64 (Percentage change)	6,018 (...)	6,116 (1.6)	6,071 (-0.7)	6,114 (0.8)	6,260 (2.4)	6,292 (0.5)	... (...)
Manpower (Percentage change)	3,674 (...)	3,718 (1.2)	3,846 (3.4)	3,868 (0.6)	3,892 (0.6)	3,888 (-0.1)	3,855 (-0.8)
Total employment (Percentage change)	3,256 (...)	3,502 (7.6)	3,545 (1.2)	3,553 (0.2)	3,588 (1.0)	3,601 (0.4)	3,570 (-0.9)
Rate of unemployment Share ²	4.0 61.1	5.8 60.8	7.8 63.4	8.1 63.3	7.8 62.2	7.4 61.8	7.4 ...

¹ Provisional data.

² Total Manpower as percentage of population aged 15-64.

Source: Ministry of National Economy; General Secretariat of NSSG.

other things to the "discouragement of unemployed effect" which must have also affected total manpower. These developments explain the stagnation of the unemployment rate as shown in the NSSG and the MEA (Manpower Employment Agency) data (1987: 6.2 per cent; 1986: 6.1 per cent), which relate only to the jobless receiving relief payments. Other indications, which stem from MEA data and support the above estimates, are the small decrease in the number of layoffs (1987: -0.7 per cent; 1986: -4.6 per cent) and the

small increase in the number of new placements (1987: 1.9 per cent; 1986: 5.2 per cent).

On the basis of developments described above, it is clear that the rate of unemployment in Greece in 1987 remained at levels considerably lower than the average for EEC countries (11 per cent). Individual categories of jobless point to the continuation of the trends observed in the last few years; the number of unemployed construction workers rose by 5.7 per cent, while the share of unemployed young people aged 14-29 in overall unemployment rose from 47.7 per cent to 49.9 per cent (first ten months of 1987 against the same period in 1986).

III. WAGES, PRICES AND BUSINESS PROFITS

1. PRICES

Inflation continued to decelerate in 1987, though at a fairly low rate between the beginning and the end of the year. At average annual levels, however, the

TABLE III.1
ANNUAL RATE OF PRICE INCREASES
(Percentage change in average levels)

Years or Quarters	Consumer Price Index (NSSG)						Wholesale Price Index (NSSG)				
	GENERAL INDEX	Sub-indices					GENERAL INDEX	Sub-indices			
		Food	Clothing and footwear	Housing	Transport and communi- cations	Other goods and services		Final domestic products for home consumption	Exported products	Imported products	
								Primary	Industrial		
1977	12.1	14.0	12.8	11.8	7.5	11.9	13.7	14.1	12.5	19.9	12.1
1978	12.6	14.3	14.1	11.4	6.3	12.9	10.3	12.5	9.7	5.4	12.9
1979	19.0	18.8	22.4	19.4	24.5	15.0	21.0	21.0	20.2	25.7	20.0
1980	24.9	27.6	18.7	29.0	22.6	23.1	28.4	24.8	30.4	26.3	28.3
1981	24.5	30.1	21.5	27.2	13.7	22.1	25.9	25.1	24.2	25.1	31.0
1982	21.0	21.1	27.8	18.4	15.3	21.6	16.0	20.6	16.8	8.1	15.4
1983	20.2	18.0	22.3	13.7	21.0	24.3	19.8	15.5	20.8	19.6	21.2
1984	18.5	18.3	26.2	14.8	11.6	20.1	21.4	20.2	18.3	29.6	24.0
1985	19.3	19.5	22.1	17.1	16.8	20.0	20.6	17.7	19.8	22.1	23.3
1986	23.0	20.3	25.4	20.8	26.7	24.3	17.9	12.5	21.2	9.1	20.6
1987	16.4	12.6	21.7	14.6	11.4	21.4	9.2	13.5	7.1	7.6	11.1
1984 a	18.9	17.1	26.2	11.4	11.6	24.4	19.6	17.6	19.1	26.0	18.4
b	18.3	17.8	27.4	13.0	11.0	20.5	22.2	22.7	18.6	29.6	25.1
c	18.7	19.8	27.8	16.7	11.8	17.4	23.0	22.6	18.2	34.0	27.1
d	18.0	18.3	23.7	17.9	12.3	17.7	20.9	18.0	17.6	28.9	25.2
1985 a	18.5	19.5	21.2	18.5	12.4	14.0	20.1	21.3	17.3	28.2	20.4
b	17.3	17.0	21.1	15.2	12.2	19.2	17.7	14.2	16.6	21.9	19.9
c	18.2	18.2	21.1	14.6	15.6	19.7	17.8	14.0	19.2	15.8	19.2
d	23.0	23.0	24.7	19.9	26.7	22.0	26.3	21.5	25.5	23.3	33.0
1986 a	24.7	22.1	23.6	22.8	31.7	25.8	23.8	15.2	26.7	13.8	30.9
b	24.5	21.8	25.9	22.1	30.2	25.4	20.8	14.1	24.7	11.0	24.1
c	23.8	21.7	26.1	20.9	28.3	24.4	18.0	12.0	20.6	9.7	22.1
d	19.5	16.0	25.6	17.8	17.8	22.3	10.2	9.1	14.1	2.6	8.3
1987 a	16.4	15.1	22.3	11.7	9.8	20.4	8.1	13.3	6.6	4.2	9.5
b	17.8	15.6	23.5	15.9	12.8	20.9	10.7	19.6	7.7	7.4	12.2
c	16.0	10.3	21.9	15.8	12.3	21.6	9.9	13.1	6.9	10.9	13.2
d	15.5	9.8	19.8	15.2	10.8	22.3	8.1	8.2	7.3	8.0	9.5

rate of increase in prices declined considerably. Specifically, the rise in the consumer price index (CPI) between the beginning and the end of 1987 was limited to 15.7 per cent, against 16.9 per cent in 1986 and 25 per cent in

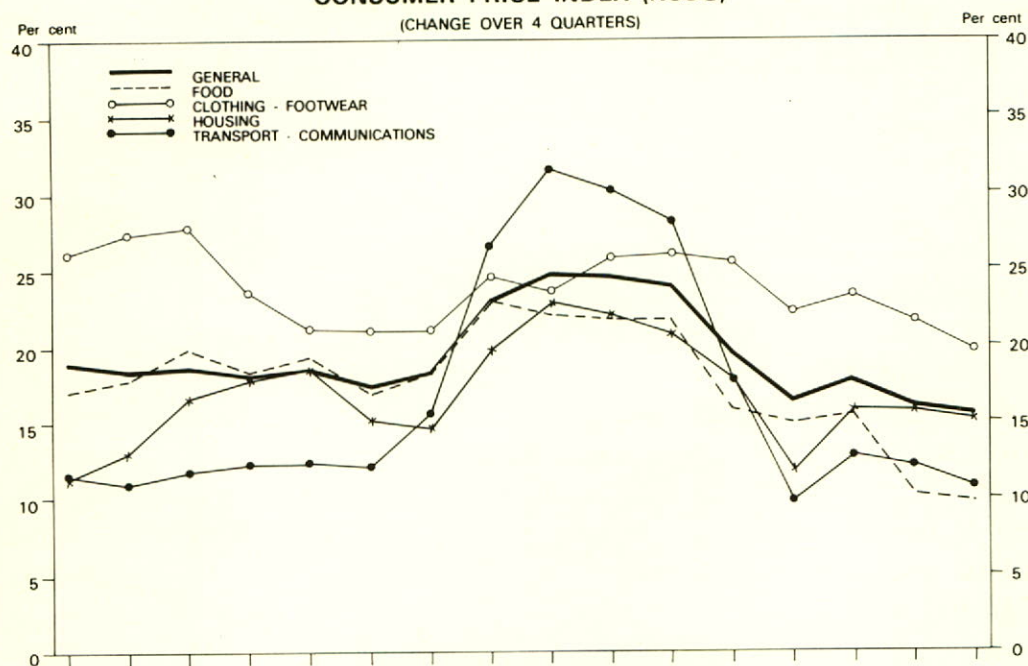
1985, while at average levels the rise in the CPI slowed down from 23 per cent in 1986 to 16.4 per cent in 1987. Similar developments were recorded in wholesale prices, but their rate of increase was considerably lower. Between the beginning and the end of 1987, the wholesale price index (WPI) rose by 7.5 per cent, against 8.5 and 28.2 per cent in 1986 and 1985 respectively. At average annual levels, the rise in the WPI was much slower (1987: 9.2 per cent; 1986: 17.9 per cent).

The relatively limited deceleration of inflation in 1987 was due to extraordinary factors, particularly in the first half of the year, such as the introduction of Value Added Tax (VAT) as from 1 January 1987, the removal at the end of January 1987 of the price freeze imposed in November 1986, and the extremely adverse weather conditions in March, which led to a rise in the prices of agricultural products. Specifically, the increase in net indirect taxes per unit of final expenditure and, in particular, the introduction of VAT are estimated to have contributed by about 3 to 4 percentage points to the acceleration of the rate of increase in the CPI. The downward trend of inflation gained momentum and became more evident in the second half of the year, when the annual rate of inflation, for seasonally adjusted data, dropped to 11.4 per cent, compared with 20.2 per cent in the first half. Inflationary pressures continued to abate in the first quarter of 1988, when the CPI rose by 2.4 per cent against 4.7 per cent in the same quarter of 1987.

Regarding cost effects on prices, two main factors contributed to the checking of price increases in 1987: (i) The limited rise in prices of imported goods, compared with 1986, as a result of the relative stability of international prices of raw materials, and the smaller decline in the effective exchange rate of the drachma (1987: -11 per cent; 1986: -22.2 per cent), and (ii) The profit squeeze in 1987 (following the large profit expansion in 1986), as a result of increased competition from imports. Furthermore, the rise in unit labour costs in the non- agricultural sector was contained again in 1987, though it was slightly higher than in 1986 (1987: 12 per cent; 1986: 11.2 per cent; 1985: 20.3 per cent).

In particular, the significant deceleration (by 6.6 percentage points) in the rate of increase in the CPI, at average levels in 1987, was due to the containment of price rises in all categories of goods and services, with the exception of "education and recreation", the prices of which rose faster (1987: 23.5 per cent; 1986: 21.9 per cent). A considerable deceleration was registered in the prices of "foodstuffs" (1987: 12.6 per cent; 1986: 20.3 per cent), mainly

DIAGRAM III.1
CONSUMER PRICE INDEX (NSSG)
(CHANGE OVER 4 QUARTERS)



WHOLESALE PRICE INDEX (NSSG)
(CHANGE OVER 4 QUARTERS)

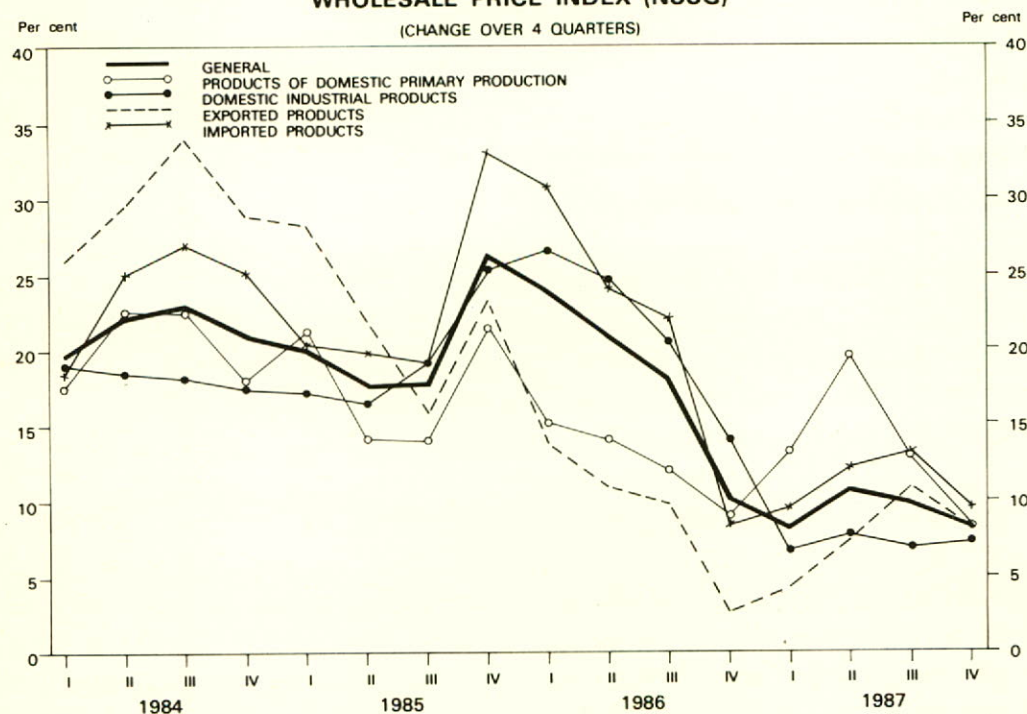
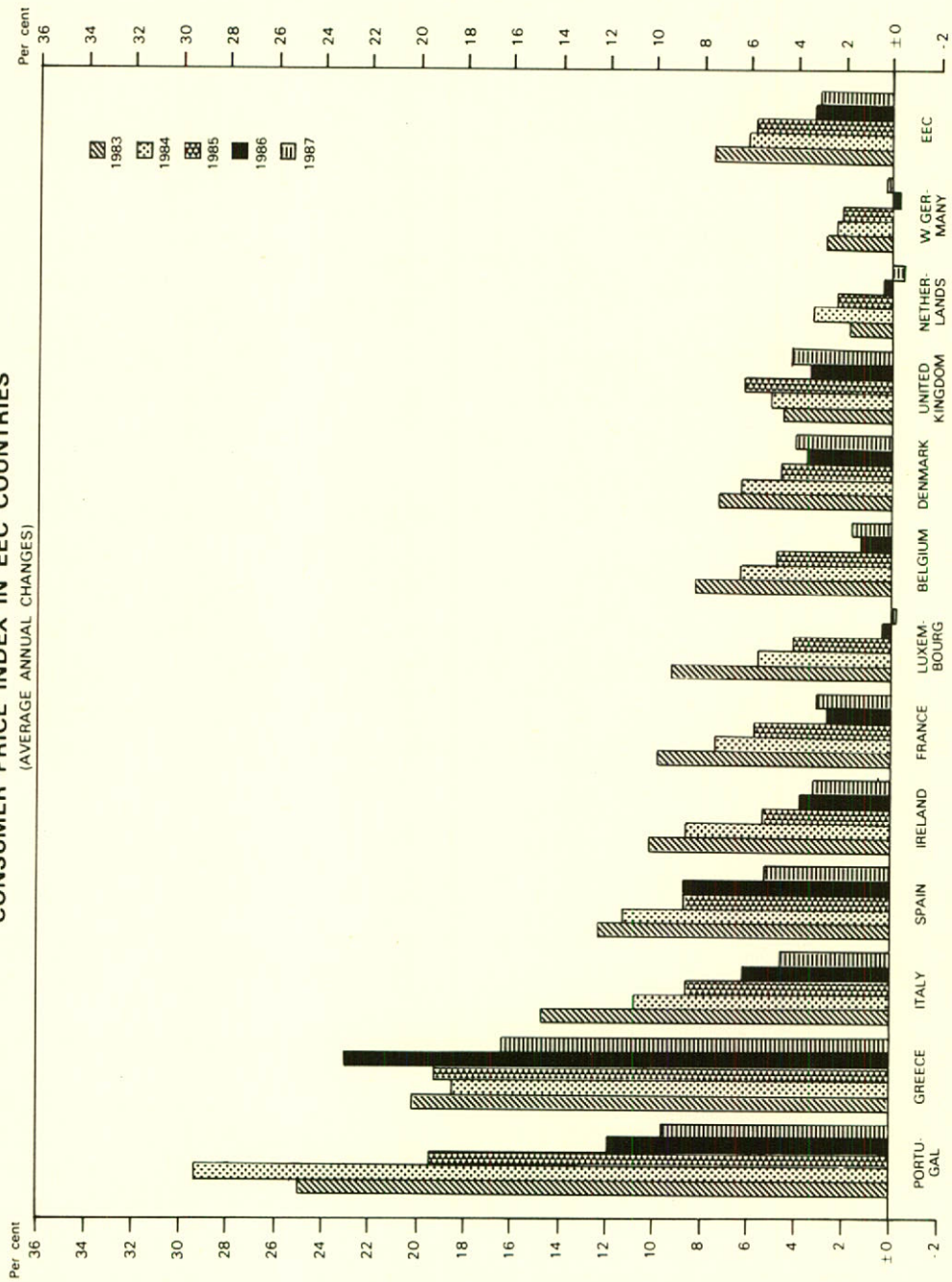


DIAGRAM III.2
CONSUMER PRICE INDEX IN EEC COUNTRIES
(AVERAGE ANNUAL CHANGES)



cereals, dairy products and meat. The deceleration was more pronounced in "transport- communications" rates (1987: 11.4 per cent; 1986: 26.7 per cent) and involved mainly fuel prices and transport fares, while the deceleration in "housing" was slower (1987: 14.6 per cent; 1986: 20.8 per cent).

At average annual levels, the prices of services increased fairly faster than those of goods (19.1 per cent against 15.5 per cent), unlike what had happened in 1986. Moreover, the divergence between the rates of increase in administratively set and market determined prices of goods and services (12.5 per cent and 17.8 per cent respectively) widened further. In 1986, the respective rates of increase had been 20.4 per cent and 24 per cent. Therefore, the deceleration of inflation was achieved despite a continuing price liberalisation policy.

The rate of increase in the WPI registered a slowdown in all categories of products included in this index, with the exception of "domestic primary products for home consumption" (1987: 13.5 per cent; 1986: 12.5 per cent). A particularly pronounced slowdown was observed in the prices of "domestic manufactured products for home consumption" (1987: 7.1 per cent; 1986: 21.2 per cent), mainly in the prices of food, oil and coal products and metal products, except machinery and vehicles. There was also a significant slowdown in the upward trend of the prices of imported goods (1987: 11 per cent; 1986: 20.6 per cent), chiefly in the prices of processed livestock products, machinery and appliances (except electrical), and of transport equipment.

Last year's containment of inflationary pressures, at average levels, in Greece, together with the upward trend of prices in major European countries and OECD member-states, contributed to a reduction in the inflation differential between Greece and those countries. Nevertheless, this differential remains significant (see Diagram III.2).

2. WAGES AND SALARIES

In 1987, the incomes policy included in the economic stabilisation programme announced in October 1985 continued virtually the same. The only change was that the first tranche under the wage indexation system (ATA) was raised from 50,000 to 60,000 drachmas. As a result, the slowdown in the growth rate of nominal labour earnings, which had started in 1986, continued during the year under review.

Specifically, according to national accounts data and estimates, the total wage bill (compensation of employees) rose by 12 per cent in 1987, compared with increases of 12.7 per cent in 1986 and 24.6 per cent in 1985¹. Unit labour cost in the urban sector also rose by 12 per cent in 1987, against 11.2 per cent in 1986 and 20.3 per cent in 1985². At the same time, the share of wages and salaries in non-agricultural GDP dropped from 58.1 per cent in 1985 to 54.6 per cent in 1986 and 53.9 per cent in 1987.

Developments in the various categories of wage earners and salaried employees were as follows:

In the public sector, total outlays for salaries (excluding pensions) rose by 14.3 per cent, i.e. at a slightly higher rate than the 1987 budget forecast (13.9 per cent). Outlays per employed person grew less (1987: 12.6 per cent; 1986: 14.6 per cent), owing to a 1.5 per cent increase in the number of employees in active service (tenured and non-tenured). As regards civilian staff working for the government, the increase in annual earnings due exclusively to the implementation of ATA ranged between 10.4 per cent for the starting pay bracket and 6.2 per cent for the top pay bracket.

According to data compiled by the General Secretariat on Public Enterprises and Public Organisations of the Ministry of National Economy, the wage bill in a total of 45 public enterprises rose by 10.9 per cent, while gross average pay grew by 10.1 per cent (1986: about 12 per cent).

According to NSSG data, the monthly earnings of bank employees in April 1987 were 8.1 per cent higher than in April 1986. In insurance companies, the corresponding increase was 8.3 per cent. For the year as a whole, the increase in bank employees' earnings was 8 per cent (1986: 9 per cent), as estimated on the basis of NSSG data and the annual statements of Greek banks.

In the private sector, the minimum pay of unskilled blue- and white-collar workers, pursuant to the National General Collective Labour Agreement, rose by 10.1 per cent, compared with 10.8 per cent in 1986. According to provisional estimates, the nominal hourly earnings of blue-collar workers in manufacturing rose by 10 per cent (1986: 12.7 per cent) and their weekly

¹ The national accounts aggregate "compensation of employees" includes (besides earnings) employers' contributions to employee insurance funds, pensions of civil servants and net labour income from abroad. The change in this aggregate is also affected by changes in the number of employees.

² This figure is calculated by comparing the change in the wage bill (nominal) with the change in non-agricultural GDP at factor cost and 1970 prices.

TABLE III.2
WAGES AND SALARIES, UNIT LABOUR COST, PRODUCTIVITY: 1982-1987
(Annual percentage change)

	1982	1983	1984	1985	1986	1987
TOTAL ECONOMY (EXCEPT AGRICULTURE) ¹						
- Compensation of employees (wages and salaries)	28.6	20.3	24.0	24.6	12.7	12.0
- Non-agricultural GDP at constant prices	0.3	2.0	2.3	3.6	1.4	0.0
- Unit labour cost	28.3	18.0	21.2	20.3	11.2	12.0
MANUFACTURING ²						
- Hourly earnings of blue-collar workers (nominal)	33.5	19.4	26.3	19.8	12.7	9.8 ³
- Hourly earnings of blue-collar workers (real)	10.4	-0.7	6.6	0.4	-8.4	-5.9 ³
- Weekly earnings of blue-collar workers (nominal)	30.3	19.2	25.3	23.1	12.5	10.2 ³
- Weekly earnings of blue-collar workers (real)	7.8	-0.8	5.7	3.1	-8.5	-5.6 ³
- Monthly earnings of white-collar workers (nominal)	22.5	14.3	24.1	23.0	8.6	8.9 ³
- Monthly earnings of white-collar workers (real)	1.2	-4.9	4.7	3.1	-11.7	-6.7 ³
- Output per worker	-2.2	-0.2	0.9	3.7	-0.7	-0.8 ³
- Output per man-hour	0.1	-0.1	1.8	1.0	-0.5	-1.2 ³
- Unit labour cost	33.3	19.5	24.1	18.7	13.3	11.1 ³
BANKS ²						
- Monthly earnings of employees (nominal)	...	...	...	...	8.0 ³	8.1 ⁶
- Monthly earnings of employees (real)	...	...	...	...	-11.4 ³	-8.1 ⁶
RETAIL TRADE ²						
- Monthly earnings of employees (nominal)	37.5	22.1	25.2	23.0	11.1	9.2 ³
- Monthly earnings of employees (real)	13.7	1.6	5.7	3.1	-9.7	-6.4 ³
MINING AND QUARRYING ²						
- Weekly earnings of blue-collar workers (nominal)	26.7	20.2	23.6	24.7	12.1	12.0 ³
- Weekly earnings of blue-collar workers (real)	4.7	0.0	4.3	4.5	-8.9	-4.0 ³
- Monthly earnings of white-collar workers (nominal)	23.2	15.3	22.7	24.3	12.0	11.3 ³
- Monthly earnings of white-collar workers (real)	1.8	-4.1	3.5	4.2	-8.9	-4.6 ³
MINIMUM WAGES AND SALARIES ⁴						
- Daily wages of unskilled blue-collar workers (nominal)	48.2	15.4	26.0	18.0	10.8	10.1
- Daily wages of unskilled blue-collar workers (real)	22.5	-4.0	6.3	-1.1	-9.9	-5.4
- Monthly salaries of unskilled white-collar workers (nominal)	53.5	15.3	25.9	17.9	10.8	10.1
- Monthly salaries of unskilled white-collar workers (real)	26.9	-4.1	6.2	-1.2	-9.9	-5.4
DOMESTIC WAGES AND SALARIES AS A PERCENTAGE OF NON-AGRICULTURAL GDP AT CURRENT PRICES ¹						
	56.7	56.7	57.6	58.1	54.6	53.9

¹ Data and estimates of National Accounts.² Calculations based on NSSG survey data.³ Data for October 1986 against October 1985.⁴ Estimated on the basis of National General Collective Labour Agreements.⁵ Data for nine-month period January-September 1987 against the same period in 1986.⁶ Data for April 1987 against April 1986.

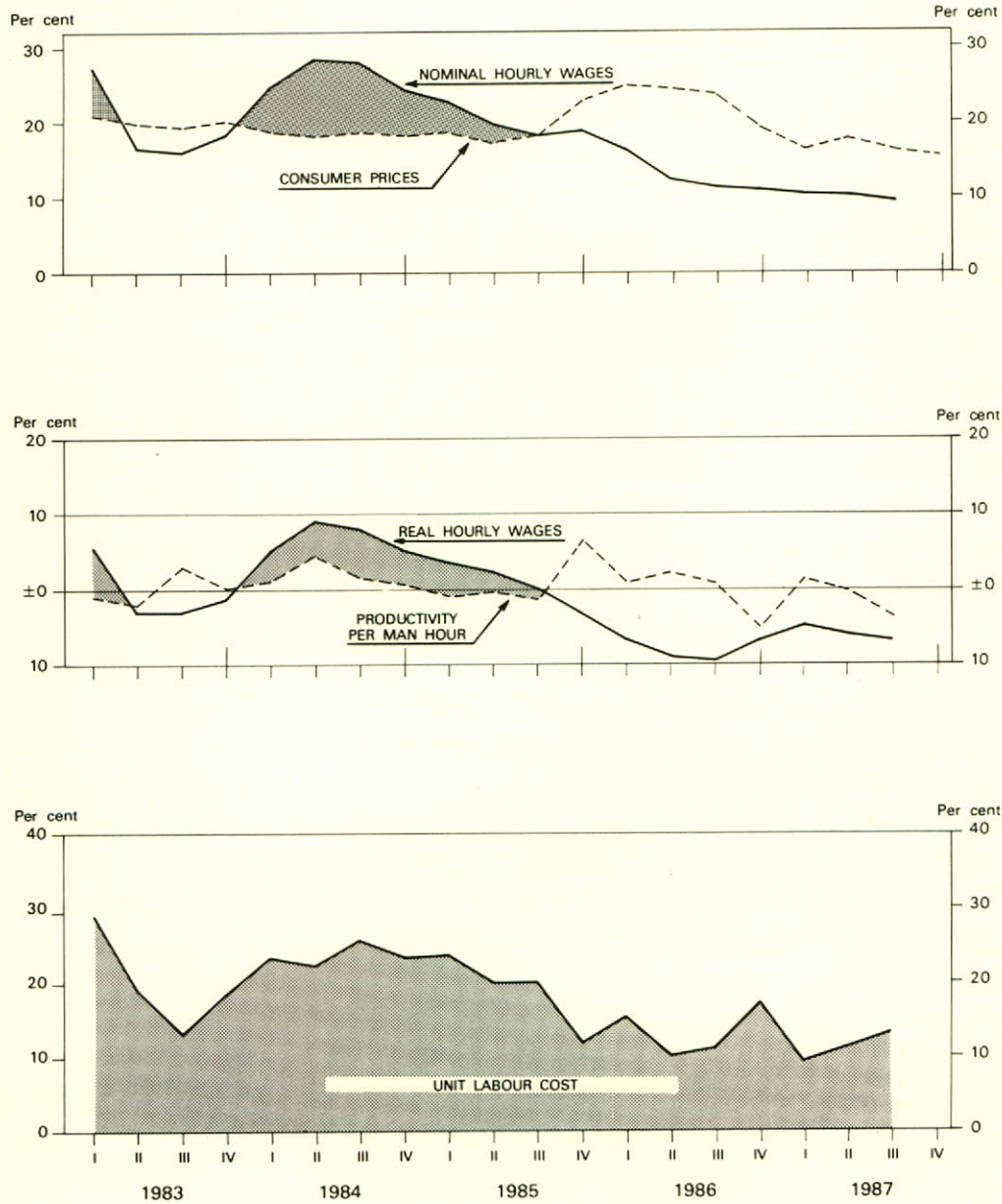
earnings by 10.5 per cent (1986: 12.5 per cent), while the monthly earnings of white-collar workers increased by 9 per cent (1986: 8.6 per cent)¹. In real terms, hourly earnings dropped by 5.5 per cent, weekly earnings by 5.1 per cent and monthly earnings by 6.4 per cent. In 1986, the respective decreases were 8.4, 8.5 and 11.7 per cent. Since productivity per man-hour fell by about 1 per cent (1986: -0.5 per cent), unit labour cost increased at a faster rate than earnings (11 per cent; 1986: 13.3 per cent), as shown in Diagram III.3. In 1987, as in 1986, unit labour cost in manufacturing grew faster than the average for Greece's competitor countries (3.7 per cent in 1986 and 2.1 per cent in 1987). The difference between the two rates, however, was more than offset by the drop in the average effective exchange rate of the drachma by 22 per cent in 1986 and 11 per cent in 1987, which improved the competitiveness of Greek products.

In retail trade, NSSG data show that the monthly earnings of employees increased by 9.2 per cent in the nine-month period January-September 1987 compared with the same period in 1986. In mining and quarrying, the weekly earnings of blue-collar workers and the monthly earnings of white-collar workers rose by 12 per cent and 11.3 per cent respectively. In 1986, the annual increases had been 11.1 per cent for retail trade employees, 12.1 per cent for blue-collar workers and 12 per cent for white-collar workers in mines and quarries.

The ATA system applied for civil servants in 1987 will be retained in 1988, but with the following two changes: (i) The effect of imported inflation will not be deducted from the first tranche of ATA; and (ii) If at the end of each four-month period the actual rate of inflation diverges from the forecast rate, the difference will be incorporated in the pay rise under ATA for the next four-month period. For those working in the rest of the public sector and in the private sector, the Government intends this system to serve as a guideline for free collective bargaining. Already, the National General Collective Labour Agreement signed in January 1988 with regard to minimum pay provides for a further rise of 1.2 per cent effective as from 1 January 1988, in addition to a corrective rise of 4.3 per cent for divergences in 1987 (which, by ministerial decision, was paid to all employees on the basis of the existing tranches), and pay rises under the ATA system.

¹ The estimates on earnings, productivity and labour cost in manufacturing were based on available NSSG data for the nine-month period January-September, as shown in Table III.2.

DIAGRAM III.3
WAGES AND UNIT LABOUR COST IN MANUFACTURING
(CHANGE IN AVERAGE LEVEL ON PREVIOUS YEAR'S QUARTER)



3. BUSINESS PROFITS

For the second consecutive year, income from property and entrepreneurship continued its upward trend. Estimates based on the financial results of business firms in 1987 indicate a further small increase in net profits, following fast growth in 1986. Specifically, the share of "income from property and entrepreneurship" in national income, which had been falling in previous years, recorded an increase in 1986, which continued in 1987.

Further indications of a rise in business profits are provided by financial results for industry as a whole, which, however, are available only up to the end of 1986. In particular, according to data compiled by the Federation of Greek Industries, profits in industry showed a substantial improvement in 1985 and a rapid increase in 1986, excluding the results of "ailing" firms. Final net profits of business firms (excluding "ailing" firms) rose from 7.3 billion drachmas in 1984 to 13.5 billion drachmas in 1985 and 42.7 billion drachmas in 1986. It should be noted that data on financial 1986 cover 3,263 firms, i.e. almost the entire manufacturing sector.

Lastly, the net profits of industrial, banking and other firms quoted in the Athens Stock Exchange showed a considerable increase between the first half of 1987 and that of 1986. Furthermore, data from published balance sheets for financial 1987 point either to an improvement compared with 1986 in terms of the amount of net profits, or to a decrease in losses for most firms. It is also worth noting that the results of "ailing" firms as a whole improved in both 1986 and 1987. According to available data on firms operating under Law 1386/83, which have been brought under the Organisation for the Economic Rehabilitation of Enterprises and are considered viable, aggregate losses fell from 39.6 billion drachmas in 1985 to 34.9 billion drachmas in 1986 and to about 15 billion drachmas in 1987. Moreover, the financial structure of some "ailing" firms improved by the conversion of part of their outstanding debts into shares.

The margins and absolute amount of profits in manufacturing were affected by keener competition indicated by the increased import penetration, by the slower growth of unit labour cost, and by the small decrease in the economy's expenditure. The growth of business profits in 1987, however, in contrast with 1986, seems to have stemmed from the commercial rather than the industrial sector of the economy. In particular, the difference between the rise in the WPI for manufactures for home consumption and exports (1987: 7.1 per cent; 1986: 18.9 per cent according to the corresponding indices of the

NSSG) and the rise in prices of raw materials, on the basis of the WPI compiled by the Bank of Greece (1987: 10.8 per cent; 1986: 16.2 per cent), did not favour higher profit margins for manufactured products in 1987.

The stabilisation policy pursued created favourable conditions for increased returns on invested capital, which improved the self-financing capacity of firms, and was the main reason for their relatively reduced dependence on bank financing. This fact, combined with the conversion into shares of a part of the debts of ailing firms in 1987, had a dampening effect on financial charges. The lowering of costs and the improvement in the financial position of industrial firms in 1986 and 1987 will have a favourable impact on prices, provided firms do not aim at higher profit margins. It is hoped that a propitious business climate and increased returns on capital will lead to further investment initiatives, which will enhance productivity and competitiveness in the industrial sector.

IV. MONETARY AND CREDIT DEVELOPMENTS

1. MONEY SUPPLY AND LIQUIDITY OF THE ECONOMY

a. Money Supply (M1)

Money supply narrowly defined (M1), namely currency in circulation plus private sight deposits, increased by 100 billion drachmas or 13.6 per cent in 1987, compared with 64 billion drachmas or 9.4 per cent in 1986 and 133 billion drachmas or 24.4 per cent in 1985. This acceleration was due to an increase in currency in circulation (14.7 per cent, against 7.2 per cent in 1986), while there was a further slowdown in the growth rate of sight deposits (10.5 per cent, compared with 16.2 per cent in 1986).

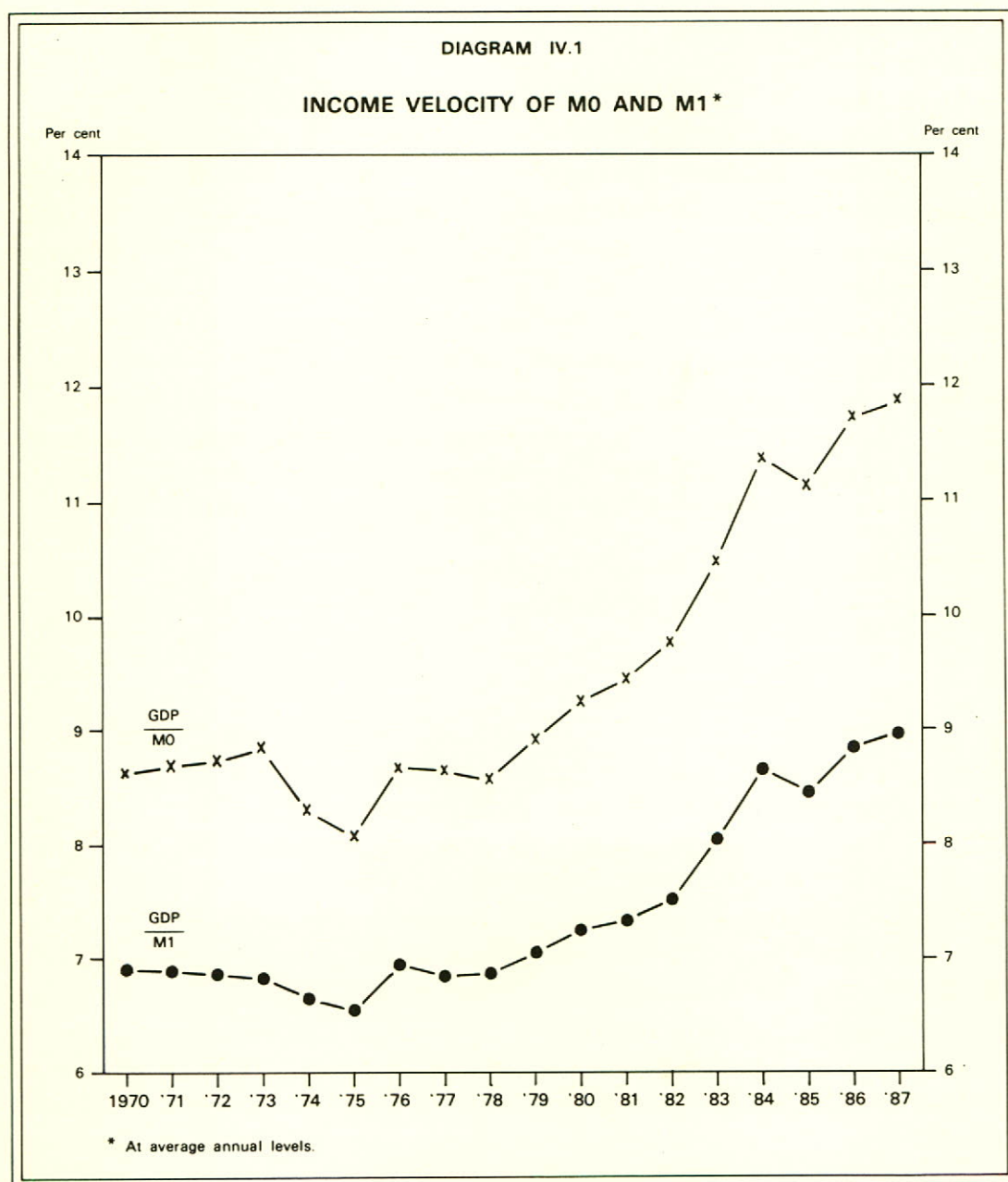
TABLE IV.1
MONEY SUPPLY, M1

	Outstanding balances on 31 Dec. 1987 (million drachmas)	Annual changes					
		Million drachmas			Percentage		
		1985	1986	1987	1985	1986	1987
Currency in circulation, M0	621,050	+104,501	+ 36,186	+ 79,604	+26.1	+ 7.2	+14.7
Private sight deposits	218,118	+ 28,037	+ 27,560	+ 20,748	+19.8	+16.2	+10.5
Money supply narrowly defined, M1 ¹	839,168	+132,538	+ 63,746	+100,352	+24.4	+ 9.4	+13.6
Time and savings deposits	4,406,413	+626,571	+612,339	+931,765	+28.0	+21.4	+26.8
Broad money supply, M3 ¹	5,245,581	+759,109	+676,085	+1,032,117	+27.3	+19.1	+24.5

¹ Not including sight deposits by public organisations and public enterprises.

The faster growth of currency in circulation in 1987 is attributable to two main factors. The first of them is the strike of public cashiers in December 1987, as a result of which taxes due in 1987 were collected in 1988 and thus the Central Government's borrowing requirements grew by an equal amount. Given that the extraordinary rise in the PSBR was initially financed with central bank funds, there was a concomitant increase in currency in circulation during the same period. Developments in banknote circulation in the period immediately after the end of the public cashiers' strike confirm that

part of the increase in currency in circulation at the end of 1987 was of a temporary nature. Specifically, in January 1988 banknote circulation



decreased more than what can be accounted for by seasonal factors. Last year's higher growth rate of currency in circulation is also explained by the

fact that this rate was very low in 1986, reflecting adjustments in cash balances in that year, following the sharp rise in currency in circulation after the introduction of the economic stabilisation programme in October 1985.

At average annual levels, the growth rate of narrow money (M1) slowed down to 12.8 per cent (1986: 15.1 per cent), while on a year-end basis it increased. This development was observed in both components of M1, i.e. sight deposits and currency in circulation. Given that the growth rate of nominal income was about 1.5 percentage points higher than that of M1, the income velocity of currency in circulation rose further in 1987, thus continuing, though at a slower rate, the rising trend established after the second oil crisis. This rising trend is related to the efforts to economise on cash balances in periods of increased opportunity cost of holding money, mainly owing to rises in interest rates on deposits. By contrast, in 1987, following the deceleration of inflation, especially in the second half of the year, and the weakening of inflationary expectations, the opportunity cost of holding money decreased and as a result the growth rate of the income velocity of currency in circulation dropped to 2 per cent, against 4.3 per cent in 1986.

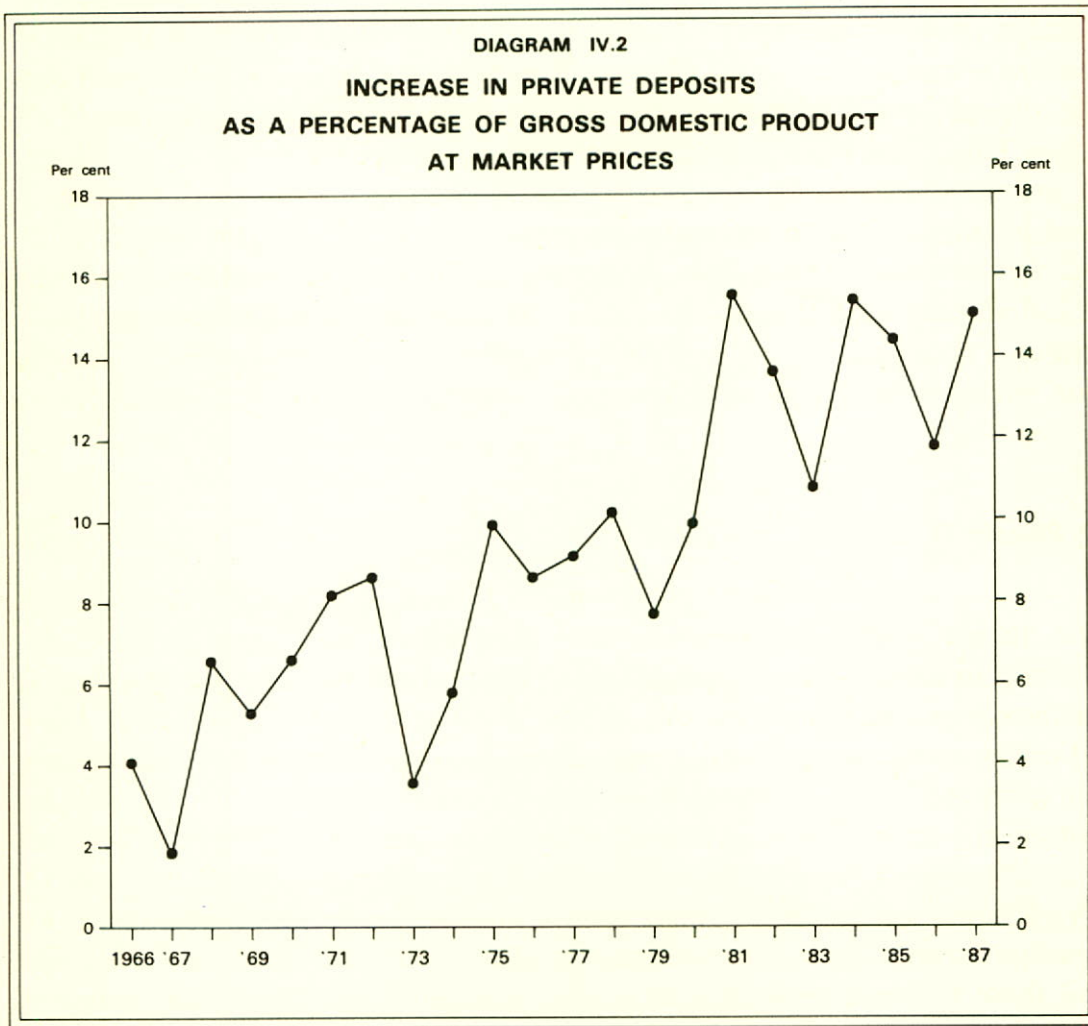
b. Private Deposits in Drachmas

The salient feature of monetary developments in 1987 was a significant increase in the growth rate of private deposits. In particular, the outstanding balance of private deposits with commercial banks and specialised credit institutions increased by 963 billion drachmas or 25.8 per cent in 1987 (1986: 21.3 per cent; 1985: 27.5 per cent), having considerably overshoot the amount forecast in the monetary programme (600 billion drachmas).

The growth rate of both savings deposits and time deposits accelerated. This acceleration was more pronounced in time deposits, which include the two new categories of time deposits introduced in 1987: 7 to 90-day term deposits and those against which certificates of deposit are issued. The other categories of time deposits (ordinary and special) grew at about the same rate as savings deposits (time deposits: 24.9 per cent; savings deposits: 25.8 per cent).

The increase, at a faster rate, in savings deposits, which constitute the larger part of private liquid assets, appears to be inconsistent with the drop in the average propensity to save, as estimated in the national accounts. In connection with these developments, it should be pointed out that, as has

happened in other countries where economic stabilisation programmes have been implemented with the main emphasis on incomes policy, that section of economic activity and incomes which is not included in official statistics may have not been affected to the same extent. For this reason, total savings in 1987 may have been larger than what national accounts data show. Indi-



cations of more favourable developments in certain categories of income are provided by changes in the composition of deposits by occupation of depositor. Relevant data show that in the categories of depositors "tradesmen-manufacturers", "professionals", and "other depositors", which account for

55 per cent of total deposits, the increase in 1987 was faster than for the other two categories ("wage earners" and "farmers").

The significant increase in deposits in 1987 is attributable to a number of factors, mainly to the positive real interest rates as a result of the gradual deceleration of inflation, and the favourable prospects as regards a further slowdown of inflation. The decrease in interest rates (by 0.85 percentage points on average) on special time deposits as from April 1987 does not seem to have perceptibly affected the inflow of these deposits into banks, as this was limited and not accompanied by any appreciable drop in real deposit rates. An upward effect on deposits was exerted by credit expansion to the public sector (as explained in the next chapter, the increase in credit to the public sector significantly deviated from the initial forecast), and by the improvement in the balance of payments, especially in the second half of the year. This improvement was largely the outcome of the establishment of positive real interest rates and of the differential between domestic and foreign interest rates, which more than offset changes in the drachma's parity. In addition, the measures to liberalise capital movements, particularly the measures concerning repatriation of capital and profits, have consolidated confidence in the economy and strengthened demand for drachma-denominated assets. Savers preferred these assets, which carry a high interest rate, to bonds denominated in foreign currency or carrying a foreign currency clause. This was manifested when ECU-linked and DM-indexed bonds were issued, the sales of which were limited.

The growth rate of deposits was also favourably affected by a slower increase in investment in housing (1987: 21.6 per cent; 1986: 40.8 per cent), the gradual release of funds in 1987 amounting to about 86 billion drachmas following the abolition of the import deposit scheme, and by the very limited volume of net sales of bank bonds for the whole year, as a result of a reduction of their interest rates by 2-3 percentage points in April 1987.

Given that the influence of some of the factors which contributed to the increase in deposits in 1987 was not uniform throughout the year, the growth rate of deposits fluctuated accordingly. Specifically, in the first five months the annualised growth rate of deposits did not exhibit any upward trend and fluctuated around 21.5 per cent. As from June, however, it rose continuously, mainly as a result of the improvement in the balance of payments and the higher PSBR, and reached 25.8 per cent by the end of the year.

Regarding developments in the various categories of deposits, only savings deposits and time deposits grew faster than in 1986 (see Table IV.2),

having increased by 932 billion drachmas in 1987 (savings deposits: 620 billion drachmas, time deposits: 312 billion drachmas). As was mentioned before, the inflow of time deposits into the banking system does not seem to

TABLE IV.2
PRIVATE DEPOSITS

Category	Outstanding balances on 31 Dec. 1987 (million drachmas)	Annual changes					
		Million drachmas			Percentage		
		1985	1986	1987	1985	1986	1987
Sight	214,514	+ 27,915	+ 27,423	+ 18,806	+19.9	+16.3	+9.6
Savings	3,021,269	+431,367	+427,418	+619,865	+28.0	+21.7	+25.8
Time	1,385,144	+195,204	+184,921	+311,900	+28.2	+20.8	+29.1
Blocked	73,390	+ 8,845	+ 15,093	+ 12,897	+24.2	+33.2	+21.3
Total	4,694,317	+663,331	+654,855	+963,468	+27.5	+21.3	+25.8

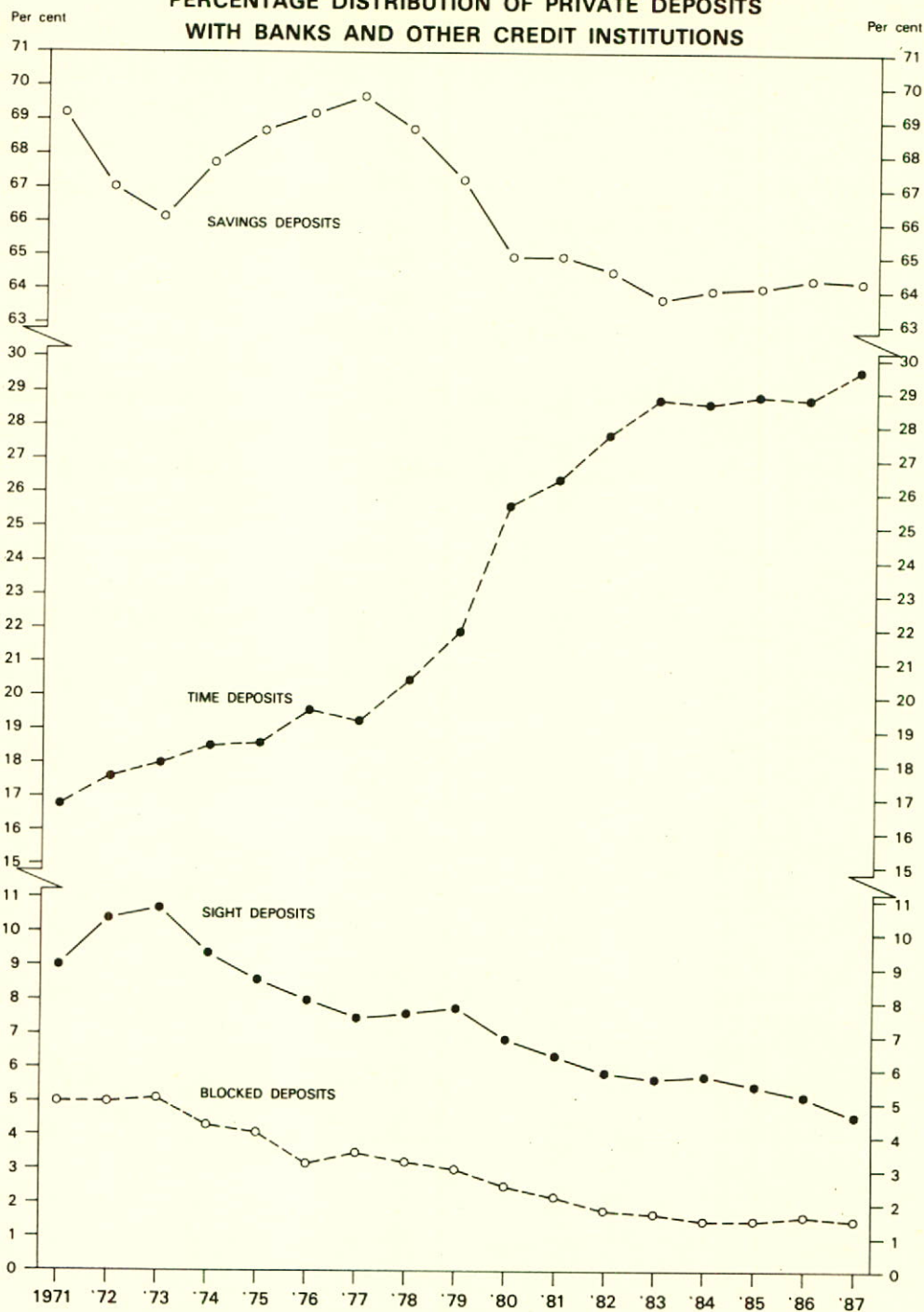
have been affected, in contrast to what happened with bank bonds, by the slight reduction in April 1987 of interest rates on special time deposits. Moreover, the introduction as from 1 March 1987 of 7 to 90-day term deposits at freely negotiable interest rates and of certificates of deposit as from 1 July

TABLE IV.3
DISTRIBUTION OF CHANGES IN PRIVATE DEPOSITS BY CREDIT INSTITUTION
(Per cent)

Credit institution	Total private deposits			Time and savings deposits		
	1985	1986	1987	1985	1986	1987
Commercial banks	70.3	72.3	70.7	69.5	72.0	71.5
Postal Savings Bank	12.8	10.0	9.5	13.5	10.7	9.8
Other	16.9	17.7	19.8	17.0	17.3	18.7
(Agricultural Bank)	(14.5)	(15.1)	(16.4)	(15.2)	(15.5)	(15.9)
Total	100.0	100.0	100.0	100.0	100.0	100.0

1987 resulted in a fairly fast increase in outstanding balances as business firms and banks moved quickly to take advantage of the new deposit categories. Subsequently, however, the growth rate of these deposits slowed down, probably because portfolios had to a considerable extent been adjusted, while inter-

DIAGRAM IV.3
PERCENTAGE DISTRIBUTION OF PRIVATE DEPOSITS
WITH BANKS AND OTHER CREDIT INSTITUTIONS



est rate liberalisation had in the meantime been extended to the other categories of time deposits and to bank bonds.

A breakdown of the increase in private deposits by credit institution shows a further decline in the share of the Postal Savings Bank, as regards both savings and total deposits, a corresponding rise in the share of the other credit institutions (mainly of the National Mortgage Bank), and a temporary increase in the Agricultural Bank's share in total deposits, following the increase in sight deposits, which however was reversed in January 1988.

c. Total Liquidity of the Economy

Money broadly defined (M3), which includes money supply (M1) plus private time and savings deposits, increased by 24.5 per cent in 1987, compared with 19.1 per cent in 1986. As in the case of savings deposits, which account

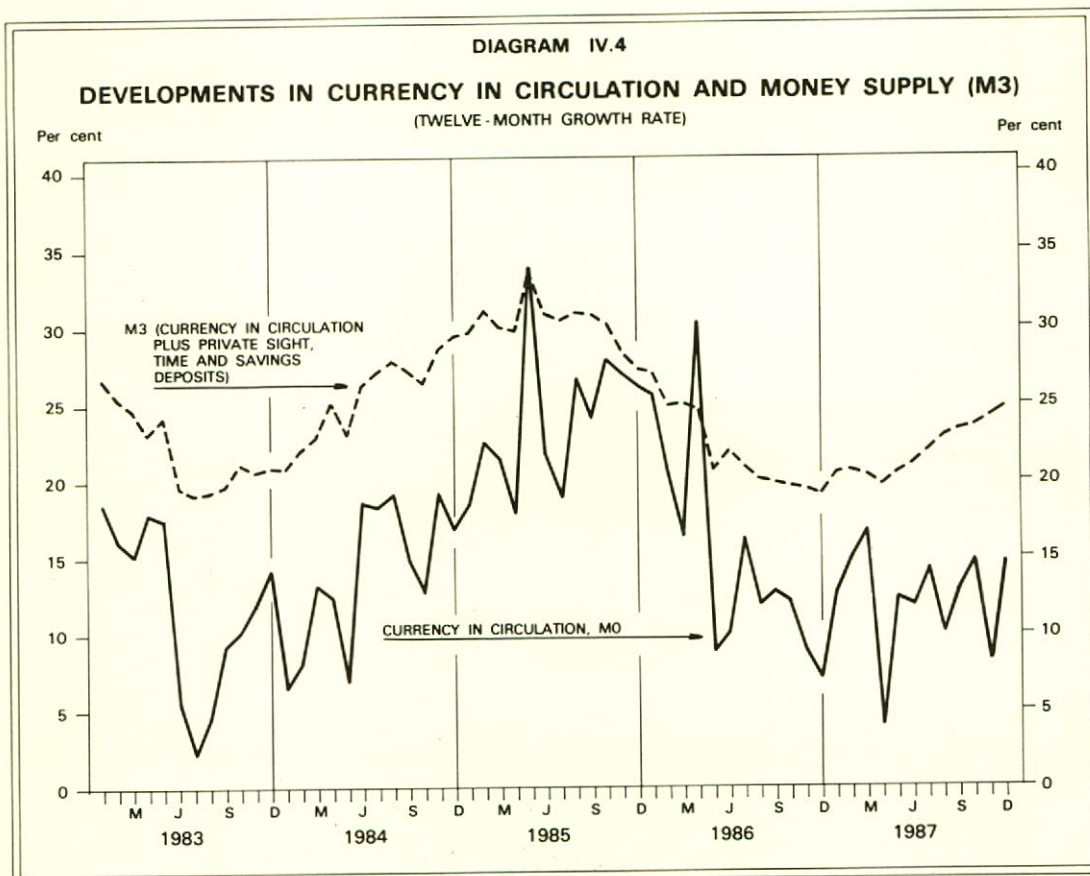


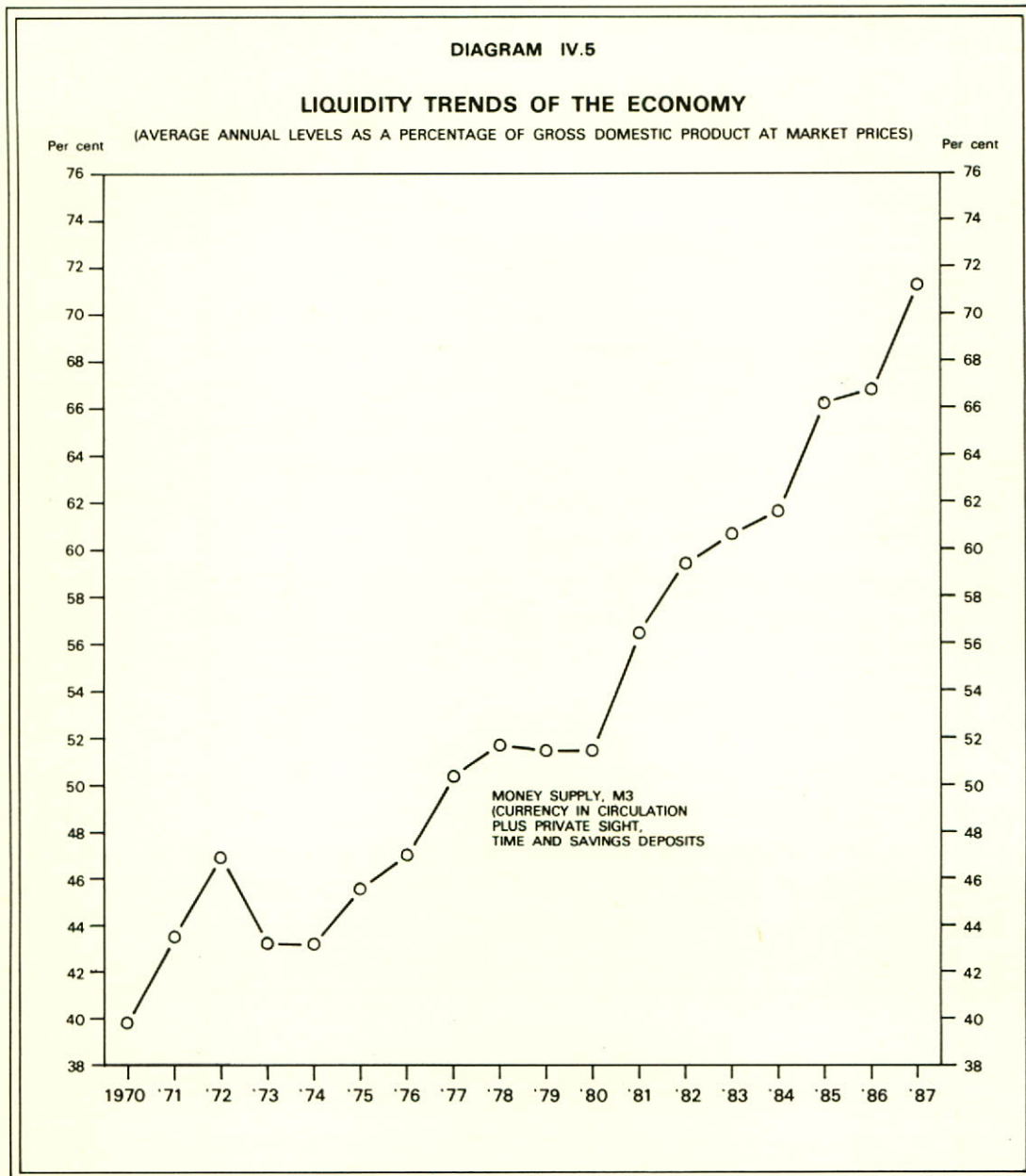
TABLE IV.4
FACTORS AFFECTING MONEY SUPPLY
(+) Money supply increase (-) Money supply decrease
(Million drachmas)

Sectors	1986 ¹	1987*
A. PUBLIC SECTOR	+759,138	+813,677
I. <i>Central Government</i>	+525,973	+564,032
1. Loans and advances ²	+ 84,579	+ 45,642
2. Treasury bills	+218,901	+316,082
3. Bonds and other securities	+ 11,285	+ 68,700
4. Deposits	+ 6,688	- 25,349
5. Other accounts ³	- 5,352	+ 36,802
6. Foreign borrowing (net)	+209,872	+122,155
II. <i>Public organisations</i>	+132,323	+136,100
1. Local authorities	+ 15,437	- 133
2. Social security	+110,896	+124,713
3. Other	+ 5,990	+ 11,520
III. <i>Public enterprises</i>	+100,842	+113,545
1. Loans and advances	+103,045	+116,058
2. Bonds	- 198	+ 1,000
3. Time deposits	- 2,005	- 3,513
B. PRIVATE SECTOR	-395,014	-608,398
I. <i>Loans and advances</i> ⁴	+305,652	+170,010
1. Agriculture	+ 91,527	+ 90,045
2. Manufacturing	+118,902	+ 15,254
3. Other	+ 95,223	+ 64,711
II. <i>Securities</i>	+ 68,360	+ 88,251
III. <i>Deposits</i>	-694,560	-859,367
1. Savings	-427,418	-619,865
2. Time	-184,921	-311,900
3. Blocked	- 82,221	+ 72,398
IV. <i>Bank bonds</i>	- 74,466	- 7,292
C. FOREIGN SECTOR	-207,642	- 63,248
1. Change in foreign exchange reserves	+ 25,045	+135,381
2. " " clearing accounts	- 5,158	- 841
3. " " foreign exchange sight liabilities	- 8,257	- 75,559
4. " " long-term foreign exchange liabilities	-209,872	-122,155
5. " " foreign exchange deposits by Greek workers and seamen	- 87,407	- 63,819
6. Loans in convertible drachmas	+ 43	- 5,623
7. Valuation differences in Bank of Greece foreign exchange accounts	+ 77,964	+ 69,368
D. OTHER ITEMS	- 74,239	+ 5,940
CHANGE IN MONEY SUPPLY, M1	+ 82,243	+147,971
1. <i>Currency in circulation</i>	+ 36,186	+ 79,604
a) Banknotes	+ 35,012	+ 78,421
b) Coin	+ 1,174	+ 1,183
2. <i>Sight deposits</i>	+ 46,057	+ 68,367
a) Private	+ 27,560	+ 20,748
b) Public organisations	+ 21,645	+ 33,566
c) Public enterprises	- 3,148	+ 14,053

¹ Revised data.² Including interest on long-term drachma loans.³ Coin in circulation and special management accounts of the State.⁴ The change is reduced by the amount of bank loans converted into shares and included in "Securities".

* Provisional data.

for about 85 per cent of broad money, M3 did not increase at a uniform rate throughout the year. In the first five months, the annualised growth rate of



M3 stabilised around 20.5 per cent, which was the December 1986 level (see Diagram IV.4). Subsequently, however, it gradually accelerated and by the

end of the year was 9 percentage points higher than the target set in the monetary programme.

At average annual levels, the growth rate of broad money in 1987 was considerably faster than that of nominal GDP. As a result, the liquidity ratio, i.e. the ratio of the average annual level of M3 to GDP at market prices, increased faster than in 1986. The sustained upward trend of the liquidity ratio (see Diagram IV.5) is associated mainly with the inadequate development of domestic financial markets, which restricts the portfolio choices of the public mainly to bank deposits. It should be noted that the growth rate of M3 would have been even faster in 1987 had there not been a shift of savings to government paper.

The factors that led to the accelerated growth of M3 in 1987, and thus to a relatively fast increase in the liquidity ratio, were mentioned in section "b" of this chapter, entitled "private deposits in drachmas". To a significant extent, the rise in the liquidity ratio reflects an increased accumulation of drachma deposits, which was combined with the favourable developments in the balance of payments and the slow but steady deceleration of inflation. The different conditions, as compared with previous years, that prevailed in domestic credit markets last year are reflected in Table IV.5, which shows the contribution of each sector of the economy to the creation of liquidity, i.e. to the growth of M3. While in the previous years total credit to the public and private sectors of the economy had increased faster than M3, in 1987 total credit expansion was approximately equal to the increase in M3. Thus, the foreign sector's persistently large negative contribution to broad money growth was significantly reduced in 1987, as the balance of payments left a surplus.

The contribution of the public sector was smaller than in 1986, despite the widening of the net PSBR from 776 billion drachmas in 1986 to 860 billion drachmas in 1987. The considerable increase in financing from non-bank sources (142 billion drachmas, against 21 billion drachmas in 1986) resulted in lower credit expansion to the public sector (1987: 718 billion drachmas; 1986: 755 billion drachmas).

In order to promote sales of government paper directly to the public, a variety of financial instruments were offered throughout the year. In February and May, three-year bonds with an ECU clause were issued, and in July the Public Power Corporation issued a seven-year DM-indexed bond. Sales of these securities fell short of expectations owing to a significant deceleration in the drop of the foreign exchange parity of the drachma, especially in the first half of the year, as a result of which the rate of return (in drachmas) on these

securities was lower than domestic interest rates. In October and December, the Government issued two-year drachma bonds carrying a fixed interest rate of 20 per cent, which achieved higher sales. Sales of treasury bills were low in the first half of the year, mainly owing to the fact that their yield was main-

TABLE IV.5
FACTORS AFFECTING MONEY SUPPLY BROADLY DEFINED (M3)
(Million drachmas)

	1986 ¹	1987*
<u>A. PUBLIC SECTOR</u>	+755,120	+717,748
a. <u>Net borrowing requirements²</u>	+776,150	+859,993
- Central Government	+577,980	+736,633
- Public organisations	+ 76,027	+ 41,496
- Public enterprises	+122,143	+ 81,864
b. <u>Financing of the deficit by private savings</u>	- 21,030	-142,245
<u>B. CREDIT TO THE PRIVATE SECTOR</u>	+217,325	+323,367
a. Loans and advances ³	+305,652	+170,010
b. Securities	+ 68,360	+ 88,251
c. Blocked deposits ⁴	- 82,221	+ 72,398
d. Bank bonds	- 74,466	- 7,292
<u>C. FOREIGN SECTOR</u>	-218,354	- 15,821
<u>D. OTHER ITEMS</u>	- 78,006	+ 6,823
<u>CHANGE IN MONEY SUPPLY (M3)</u>	+676,085	+1,032,117

¹ Revised data.

² Including foreign borrowing by public enterprises.

³ The change is reduced by the amount of bank loans converted into shares and included in "Securities".

⁴ Including advance deposit requirements on imports.

* Provisional data.

tained lower than the interest rate of bank bonds and special time deposits in medium and large amounts. The bulk of the treasury bills sold in that period were of a three-month term, while the quantity of treasury bills purchased by banks on their own account was limited. The short term of the treasury bills sold indicates that bills were purchased mainly by business firms. The situ-

ation changed radically following a rise in rates on treasury bills in June 1987. In the second half of the year, average monthly sales of treasury bills to the public amounted to about 25 billion drachmas, the share of twelve-month treasury bills in total sales almost tripled, and banks started to invest in them a significant part of their cash balances. Eventually, the share of the PSBR financed through the sale of government paper to the public rose to 16.5 per cent in 1987, against 2.7 per cent in 1986.

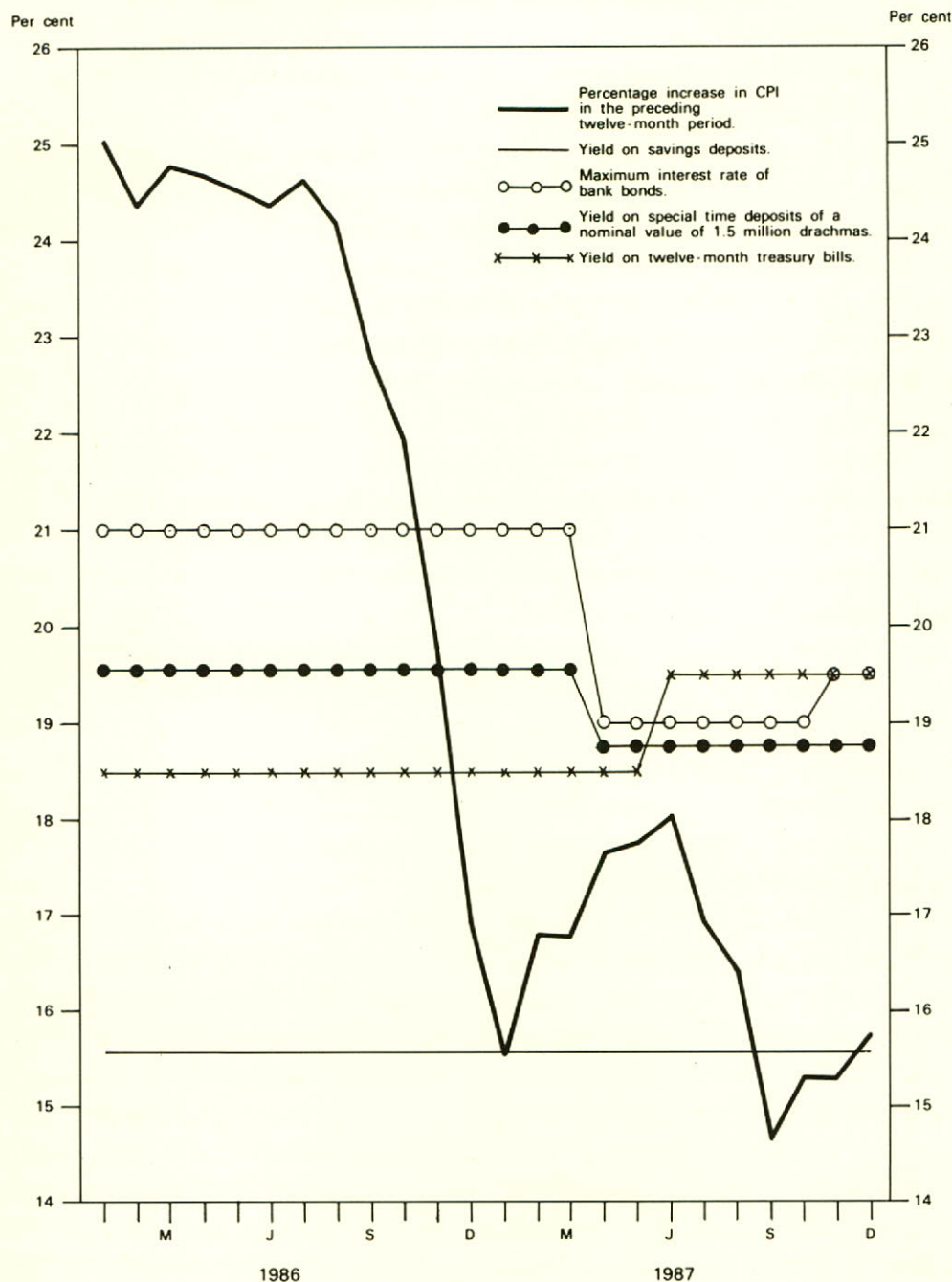
In 1987, the private sector's total contribution to M3 growth was larger than in the previous year (323 billion drachmas, compared with 217 billion drachmas in 1986), despite the slower expansion of bank credit to business firms. This larger contribution was due to the fact that in 1987 the effect of the import deposit scheme was negative, whereas in 1986 it had been positive, and that the amount of funds drawn from the capital market through bank bond issues was very small.

d. Interest Rates on Deposits and Treasury Bills

In 1987, significant steps were taken towards liberalisation of interest rates and the establishment of positive real rates. Following the deceleration of inflation and the weakening of inflationary expectations, the actual return on special time deposits, as measured by the difference between nominal interest rate and the rate of increase in the consumer price index in the previous twelve months, remained positive throughout 1987. Similarly, in the last four months of the year, the actual yield of savings deposits became positive, for the first time after the upsurge of inflation in the early 1970s (see Diagram IV.6). These developments were the outcome of the interest rate policy pursued by the Bank of Greece and aiming at the gradual abolition of administratively determined interest rates and of the strengthening of the Government's effort to finance a larger proportion of the PSBR from nonbank sources. Thus, despite the substantial deceleration of inflation, in the first quarter of 1988 the nominal interest rates on time deposits remained unchanged, and this led to the establishment of attractive real interest rates. In April, the Bank of Greece reduced the nominal interest rates on special time deposits and bank bonds in order to narrow the gap between the return on treasury bills and that on respective time deposits from a maximum of 2.5 percentage points to half a percentage point. Despite this reduction, the real interest rates on time deposits remained positive and higher than those on treasury bills.

DIAGRAM IV.6

NOMINAL INTEREST RATES AND INFLATION



The competitiveness of treasury bills, especially those with a 12-month maturity, improved appreciably following the increase in their interest rates by one percentage point at the end of June 1987. Another measure taken at the same time and aiming at maintaining the competitiveness of credit institutions was the introduction of certificates of deposit, with maturities ranging from 3 to 18 months, at negotiable interest rates. The response of the banks to this partial liberalisation of interest rates was very slow and had no significant effect on the level of nominal interest rates, while as a result of the continuous deceleration of inflation the real interest rates on special time deposits reached about 4 per cent by the end of the year. In November, the Bank of Greece fully liberalised the interest rates on all categories of time deposits, as well as those on savings deposits subject to notice.

The establishment of positive real interest rates on deposits was combined with a slowdown in the depreciation of the drachma against the major foreign currencies and an appreciation against the US dollar. As a result, domestic interest rates reached levels comparable to those of foreign interest rates. The improvement of domestic interest rates and the restoration of confidence in the economy had a direct effect on the balance of payments, and was manifested mainly in reduced capital flight and increased inflow of capital.

2. FINANCING OF THE PRIVATE SECTOR

a. Credit Expansion by Institution

The growth rate of bank credit to the private sector moved at a relatively low level since the first months of 1987 and, with the exception of a slight acceleration in the third quarter, remained low throughout the year. Specifically, bank credit to the private sector grew by 10 per cent, compared with a target of 11 per cent. In 1986, it had increased by 15.6 per cent and in 1985 by 18.8 per cent. It should be noted that in 1987 considerable debts of overindebted firms to commercial and development banks were converted into shares. As a result, there was a corresponding decrease in the outstanding balances of bank credit to the private sector and an increase in banks' investments in securities. In order to make the figures comparable, the amounts and rates of bank credit expansion for 1986 and 1987 appearing in this Report include the amount of bank credit that has been converted into shares.

The slowdown of bank credit expansion was more pronounced in credit extended to the private sector by commercial banks, which increased by 6.6 per cent, about 3.5 percentage points below the monetary target. In 1986, commercial bank credit had increased by 14.7 per cent and in 1985 by 18.2 per cent. Last year's developments were not due to a shortage of commercial bank loanable funds. Bank liquidity was favourably affected by a faster than forecast increase in private deposits and by the abolition of the requirement that commercial banks earmark 15 per cent of their deposits for financing medium- and long-term loans, which led to the release of funds amounting to

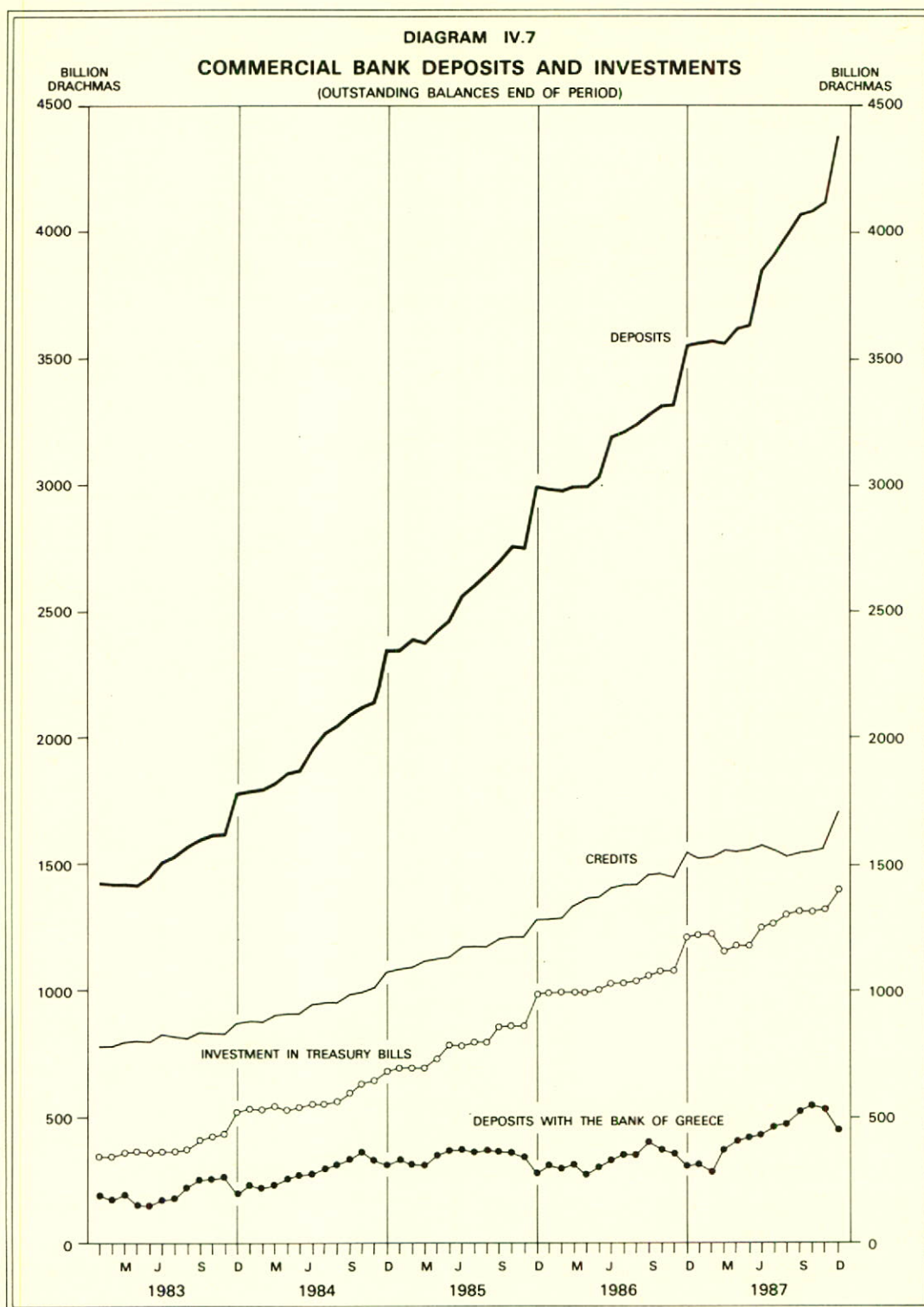
TABLE IV.6
BANK CREDIT TO THE PRIVATE SECTOR
(Changes in outstanding balances)

Year	Total			Long-term		Short-term	
	Million drachmas	Percentage	As a proportion of GDP	Million drachmas	Percentage	Million drachmas	Percentage
1978 ¹	+117,002	+24.3	10.1	+ 48,160	+24.1	+ 68,842	+24.4
1979 ¹	+113,864	+19.4	8.0	+ 58,939	+23.7	+ 54,925	+16.2
1980 ¹	+145,238	+20.8	8.5	+ 61,206	+19.9	+ 84,032	+21.5
1981 ¹	+258,287	+30.8	12.6	+ 91,272	+24.8	+167,015	+35.6
1982 ¹	+274,429	+25.3	10.7	+128,858	+28.0	+145,571	+23.3
1983	+238,495	+17.6	7.7	+118,213	+20.1	+120,282	+15.7
1984 ¹	+341,432	+21.5	9.0	+143,671	+20.3	+197,761	+22.4
1985	+359,855	+18.8	7.8	+151,773	+17.8	+208,082	+19.6
1986 ²	+355,152	+15.6	6.4	+160,303	+16.0	+194,849	+15.3
1987 ²	+258,261	+10.0	4.1	+125,825	+11.0	+132,436	+ 9.2

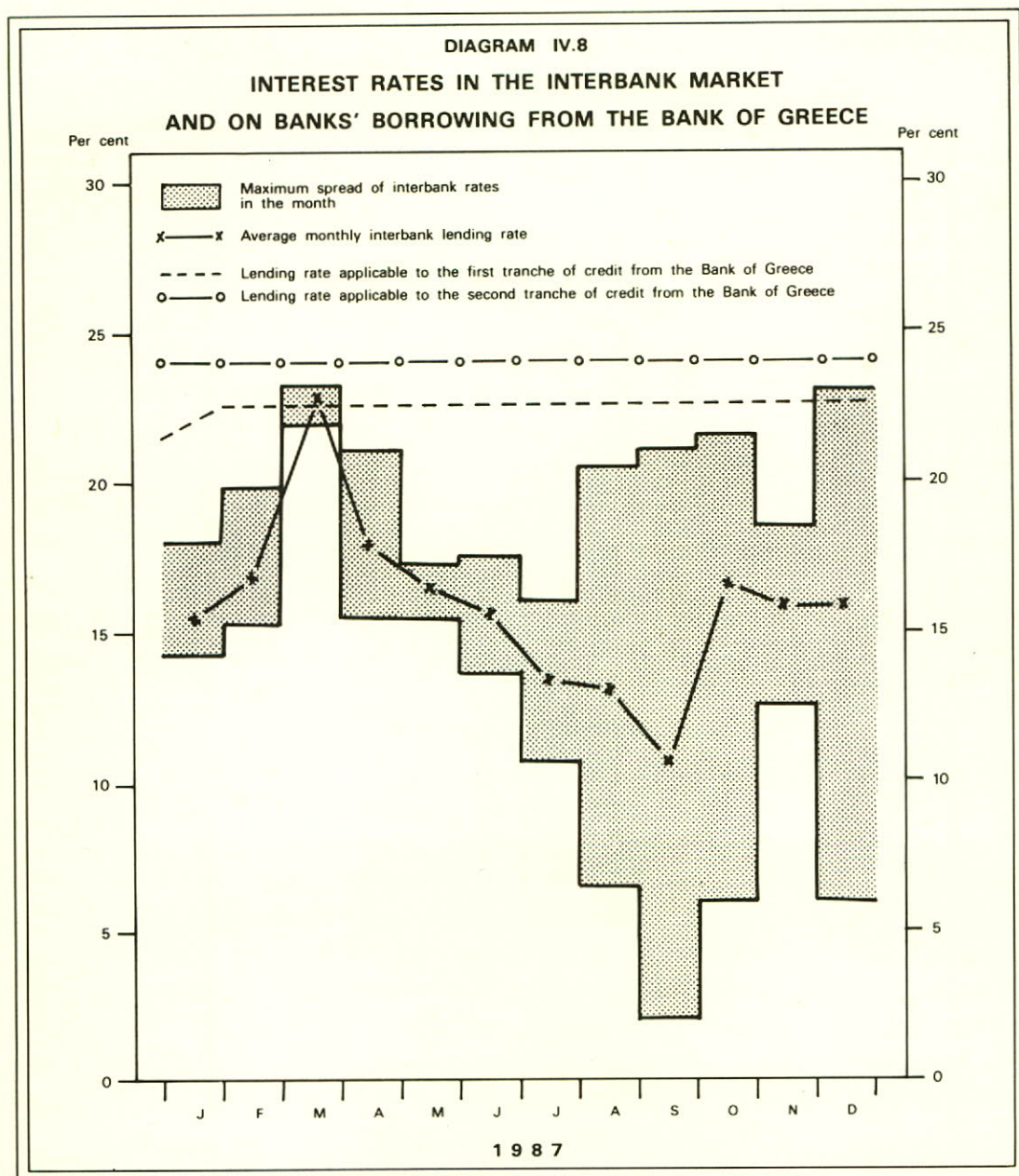
¹ Excluding the effect of the settlement of deficits in the agricultural supplies account and in the accounts of agencies purchasing agricultural productions.

² Excluding the effect of the conversion into shares of the debts of overindebted enterprises.

89 billion drachmas. By contrast, bank liquidity was adversely affected, though to a lesser extent, by (a) the reduction (from 5 to 3 per cent) as from 1 April 1987 of the interest refund to exporters in respect of export proceeds converted into drachmas, (b) the gradual increase by 2.5 percentage points in the percentage of commercial bank deposits that is earmarked for financing public enterprises and organisations, and (c) the increase by 2 percentage points as from June 1987 in the percentage earmarked in respect of special time deposits. It should be noted in this connection that in the second half of 1987 banks invested in treasury bills substantial amounts of cash balances,



further to their usual obligations. In particular, banks' investment in this category of treasury bills increased by 71 billion drachmas in 1987. Further



evidence of increased commercial bank liquidity in 1987 is provided by developments in the interbank rate, which moved at relatively low levels (below 17

per cent) throughout the year, with the exception of March 1987, when some banks faced a shortage of liquidity, and in the first days of each month, when the banks transfer to the Bank of Greece the required reserves on their deposits and loans, and when treasury bills are issued for sale to the public. In particular, in the second half of September 1987, the interbank rate dropped to very low levels (below 5 per cent). To contain the liquidity of commercial banks, their primary reserve requirements on deposits were raised in October by one percentage point (from 6.5 to 7.5 per cent).

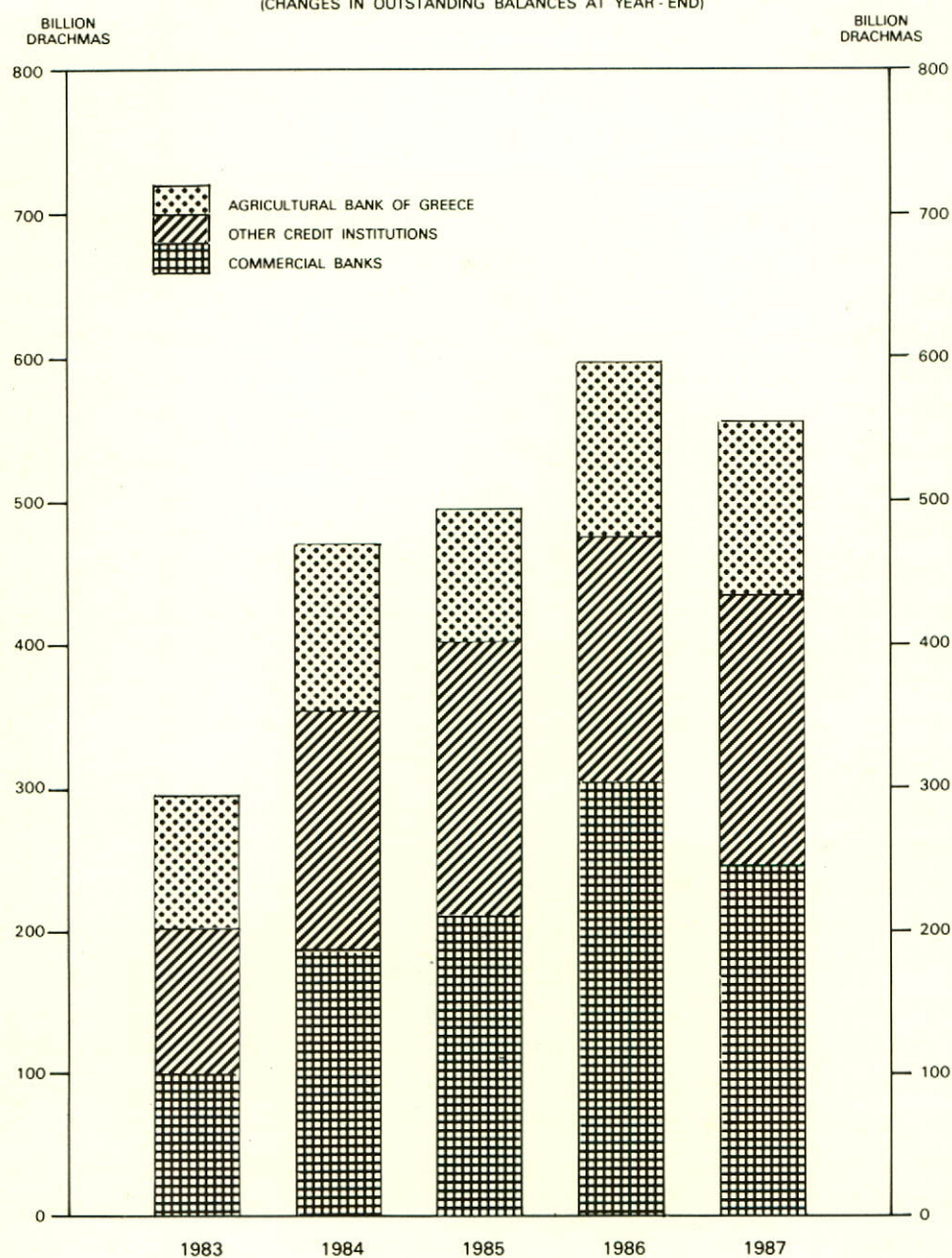
The slower expansion of commercial bank credit in 1987 basically reflects a decline in demand for credit by business firms. In particular, the borrowing requirements of business firms were affected by the abolition of the import deposit scheme and the gradual release of the relevant funds (about 86 billion drachmas), the decline in manufacturing production, and their improved profitability. Another factor that contributed to restrained demand for credit was the increase in real interest rates in 1987. High real interest rates together with weakening expectations of a drachma devaluation led to a substitution of domestic borrowing with borrowing from abroad. It is characteristic in this respect that in 1987 the net inflow of entrepreneurial capital plus suppliers' credit (net) was \$ 217 million or 29.5 billion drachmas larger than in 1986. Furthermore, business firms were more interested in drawing funds from the capital market through share issues, especially in the second half of the year.

Unlike credit extended to the private sector by commercial banks, credit by specialised credit institutions grew faster than the target set in the annual monetary programme (13.5 per cent, against a target of 12 per cent). A faster growth rate was recorded in credit extended by the Agricultural Bank and the investment banks, while the growth rate of credit provided by the other specialised credit institutions was roughly equal to the target. In particular, credit extended by the Agricultural Bank to the private sector, including loans to agricultural marketing boards and cooperatives, amounted to 92.2 billion drachmas, against 116.3 billion drachmas in 1986. As from mid-year, the Agricultural Bank achieved a containment of its credit at a level lower than the target set in the monetary programme. This was facilitated by timely payment of State and Community subsidies to the agricultural sector. In the second half of the year, credit extended to agricultural cooperatives grew faster, owing to smaller sales from their stocks and smaller purchases of agricultural products (tobacco mainly) by private trade. The accelerated growth of credit to agricultural cooperatives was partly offset by a reduction in

DIAGRAM IV.9

A BREAKDOWN OF LENDING BY CREDIT INSTITUTION

(CHANGES IN OUTSTANDING BALANCES AT YEAR-END)



the other categories of Agricultural Bank credit. Specifically, in the second half of 1987, the ceiling on credit to agricultural marketing boards and cooperatives was raised by 32 billion drachmas, while that on other categories of credit was lowered by 22 billion drachmas.

In 1987, access of the Agricultural Bank to private savings remained at a high level. The large increase in the bank's private deposits (158 billion drachmas) not only enabled it to finance its credit expansion with own funds, but also to reduce the outstanding balance of its refinancing with central bank

TABLE IV.7
BANK CREDIT TO THE PRIVATE SECTOR BY INSTITUTION

Credit institution	Outstanding balances on 31 Dec. 1987 ^{1,2} (million drachmas)	Changes in outstanding balances at year-end					
		Million drachmas			Percentage		
		1985	1986 ²	1987 ²	1985	1986 ²	1987 ²
<i>Bank of Greece</i>	6,408	+ 2,759	+ 1,073	- 6,141	+31.7	+ 9.3	-48.9
<i>Commercial banks</i>	1,442,268	+182,144	+173,794	+ 86,547	+18.2	+14.7	+ 6.6
<i>Specialised credit institutions</i>	1,439,236	+174,952	+180,285	+177,855	+19.3	+16.7	+14.1
Agricultural Bank	819,953	+ 98,851	+116,297	+ 92,217	+19.3	+19.0	+12.7
National Mortgage Bank	290,949	+ 30,286	+ 31,040	+ 31,766	+15.3	+13.6	+12.3
Hellenic Industrial Development Bank	176,871	+ 19,671	+ 17,421	+ 38,268	+19.4	+14.4	+27.9
Postal Savings Bank	55,094	+ 16,670	+ 6,690	+ 5,846	+64.4	+15.7	+11.9
Deposits & Loans Fund	27,089	+ 4,693	+ 3,902	+ 2,906	+30.1	+19.2	+12.0
Private investment banks	59,947	+ 4,136	+ 4,253	+ 5,833	+ 9.0	+ 8.5	+11.0
National Housing Bank	9,333	+ 645	+ 682	+ 1,019	+ 9.2	+ 8.9	+12.3
<i>Total</i>	2,887,912	+359,855	+355,152	+258,261	+18.8	+15.6	+10.0

¹ Provisional data.

² Excluding the effect of the conversion into shares of the debts of overindebted enterprises.

funds by 9.5 billion drachmas, despite the fact that considerable reserve requirements were imposed on its deposits in 1987. Specifically, reserve requirements (2 per cent in the second half of 1987, rising to 3 per cent as from 1 January 1988) were imposed on deposits with the Agricultural Bank. As a result, an amount of 12.7 billion drachmas was compulsorily deposited with the Bank of Greece in 1987, while another 10.4 billion drachmas was also compulsorily deposited with the Bank of Greece during the same period on the basis of the currently applicable reserve/rebate system.

The growth rate of credit extended by investment banks also accelerated (1987: 44.1 billion drachmas; 1986: 21.7 billion drachmas). This devel-

opment reflects mainly the faster expansion of credit extended by the Hellenic Industrial Development Bank (1987: 38.3 billion drachmas; 1986: 17.4 billion drachmas), though credit extended by the other investment banks also accelerated (1987: 5.8 billion drachmas; 1986: 4.3 billion drachmas). The growth rate of credit extended by the mortgage banks, the Postal Savings Bank, and the Deposits and Loans Fund was virtually equal to the target set in the monetary programme.

In 1987, funds raised by the mortgage and investment banks through the issue of bank bonds were roughly equal to redemptions of bonds from previous issues. As was pointed out before, this development was due to the fact that interest rates on bank bonds were reduced in March 1987 and that in the second half of the year the public sector offered securities with more attractive terms. In November 1987, however, credit institutions authorised to issue bank bonds were granted permission to determine the respective interest rates and other terms of issue; as a result, there was an increase in the funds raised through the issue of bank bonds. It should be stressed, however, that the significant decline in bank bond sales had no adverse effect on the lending programmes of the credit institutions that raise funds through the issue of such securities. Their lending programmes were financed through liquidation of part of their surplus funds invested in treasury bills and interest bearing time deposits with the Bank of Greece.

b. Sectoral Breakdown of Credit

As Table IV.8 shows, in 1987 there was a slowdown in credit expansion to virtually all sectors, with the exception of credit to domestic and import trade, which grew faster than in 1986. The slowdown was more pronounced in credit to industry for working capital, while credit to agriculture increased faster than credit to other sectors.

In particular, credit to industry (for reasons of comparability, the relevant figure includes the balances of loans that have been converted into shares) expanded by 8.1 per cent in 1987, compared with 14.5 per cent in 1986. The deceleration stemmed from short-term credit for working capital, which increased by 4.4 per cent, against 13.9 per cent in 1986, while long-term credit grew at a rate only slightly lower than in 1986. As was mentioned earlier, this deceleration reflects reduced demand for bank credit.

TABLE IV.8
CHANGES IN TOTAL BANK CREDIT BY SECTOR

	Outstanding balances on 31 Dec. 1987 ^{1,2} (million drachmas)	Changes in outstanding balances at year-end					
		Million drachmas			Percentage		
		1985	1986 ²	1987 ²	1985	1986 ²	1987 ²
I. PRIVATE SECTOR	2,887,912	+359,855	+355,152	+258,261	+18.8	+15.6	+10.0
Long-term loans	1,288,441	+151,773	+160,303	+125,825	+17.8	+16.0	+11.0
Short-term loans	1,599,471	+208,082	+194,849	+132,436	+19.6	+15.3	+ 9.2
1. Agriculture	677,149	+82,865	+91,527	+90,045	+20.1	+18.5	+15.3
Long-term loans	210,359	+29,355	+31,609	+11,380	+21.3	+18.9	+ 5.7
Short-term loans	278,992	+50,694	+40,848	+40,550	+34.5	+20.7	+17.0
Agricultural supplies	54,677	+ 5,757	+ 2,591	+ 5,913	+14.2	+ 5.6	+12.1
Organisations purchasing and marketing agricultural products	133,121	-2,941	+16,479	+32,202	- 3.4	+19.5	+31.9
2. Large-scale manufacturing and mining	1,103,116	+140,455	+129,505	+78,999	+18.6	+14.5	+ 8.1
Long-term loans	436,481	+49,838	+51,621	+52,296	+17.6	+15.5	+14.3
Short-term loans	666,635	+90,617	+77,884	+26,703	+19.2	+13.9	+ 4.4
3. Small-scale manufacturing	277,336	+41,060	+38,897	+24,506	+23.8	+18.2	+ 9.7
Out of "earmarked" funds	(224,419)	(+33,318)	(+39,116)	(+22,218)	(+25.7)	(+24.0)	(+11.0)
4. Trade	194,868	+26,136	+22,183	+ 2,605	+18.2	+13.0	+ 1.4
Domestic	150,242	+17,032	+9,470	+21,777	+16.7	+ 8.0	+17.0
Import	11,325	+ 1,952	+ 1,098	+ 1,784	+30.1	+13.0	+18.7
Export	15,740	- 1,109	+ 3,801	+ 1,914	- 7.4	+27.4	-10.8
Tobacco	17,561	+ 8,261	+ 7,814	-19,042	+40.2	+27.1	-52.0
5. Other	635,443	+69,339	+73,040	+62,106	+16.1	+14.6	+10.8
Long-term loans	543,028	+57,968	+57,225	+53,051	+15.5	+13.2	+10.8
—Housing	(387,927)	(+48,050)	(+45,825)	(+35,345)	(+18.6)	(+14.9)	(+10.0)
—Tourism	(100,659)	(+ 4,798)	(+10,741)	(+11,942)	(+ 6.6)	(+13.8)	(+13.5)
—Shipping	(25,571)	(+ 3,868)	(+ 211)	(+ 2,967)	(+20.9)	(+ 0.9)	(+13.1)
—Other	(28,871)	(+ 1,252)	(+ 448)	(+ 2,797)	(+ 5.1)	(+ 1.7)	(+10.7)
Short-term loans	92,415	+11,371	+15,815	+ 9,055	+20.2	+23.4	+10.9
II. PUBLIC SECTOR	1,118,236	+134,739	+245,567	+294,749	+30.4	+42.5	+35.8
Public enterprises	580,146	+69,767	+100,148	+116,058	+23.7	+27.5	+25.0
Public organisations	503,715	+71,754	+138,769	+150,103	+50.1	+64.6	+42.4
Special management accounts of the State	34,375	- 6,782	+ 6,650	+28,588	-100.0	...	+494.0
Total	4,006,148	+494,594	+600,719	+553,010	+21.0	+21.1	+16.2

¹ Provisional data.² Excluding the effect of the conversion into shares of the debts of overindebted enterprises.

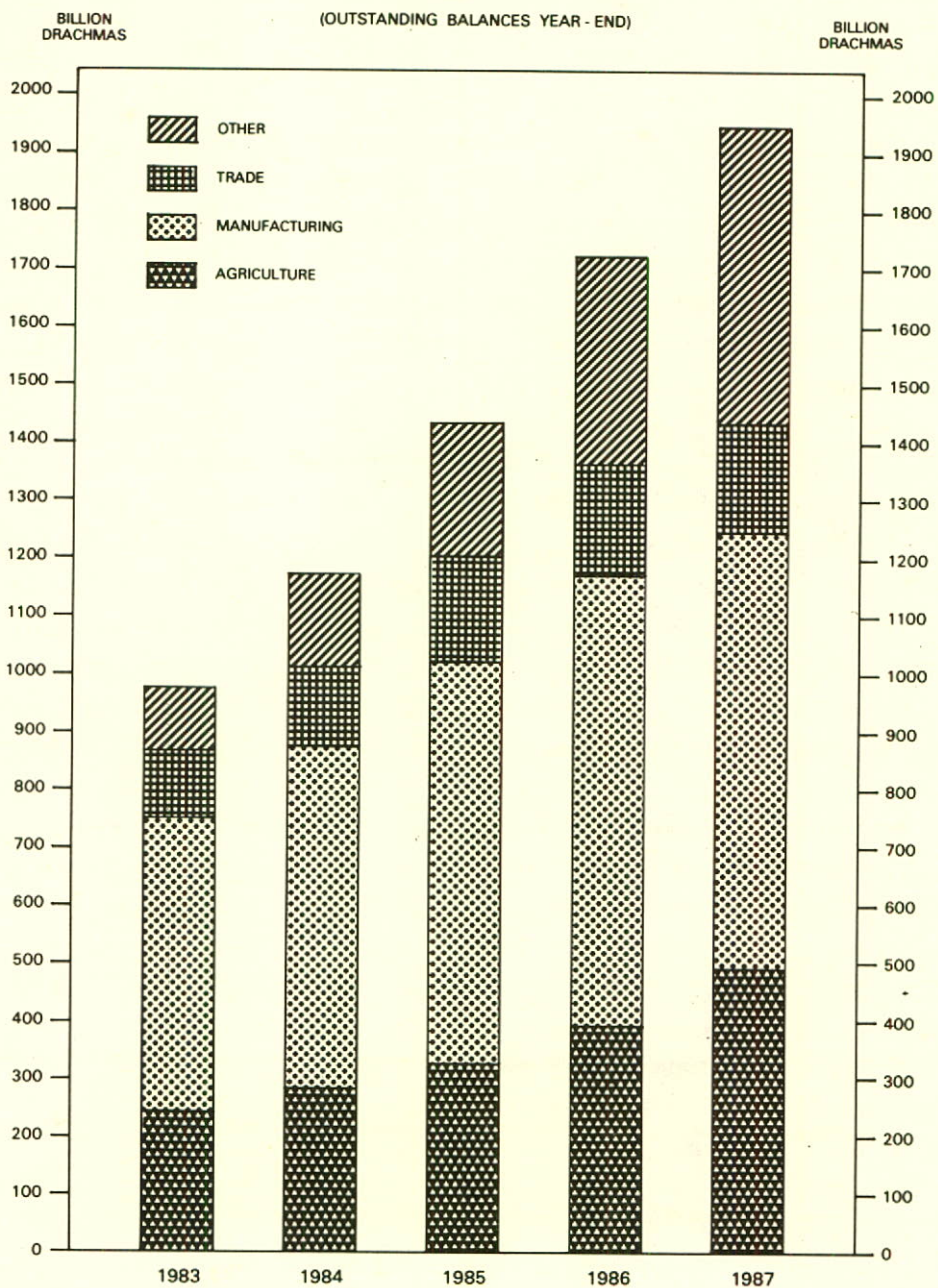
Developments in long-term credit extended to industry by all credit institutions were not significantly different from those in previous years, despite the satisfactory level of investment activity in manufacturing. It should be noted that, in the context of the policy of the Bank of Greece to simplify the system of credit controls and improve the flexibility of banks in managing their portfolios, as from June 1987 commercial banks are no longer required to earmark 15 per cent of their deposits for financing fixed investment by private enterprises. In practice, this regulation had failed to promote private investment, given that substantial amounts of both commercial and development bank funds earmarked for this purpose remained unused at the Bank of Greece. Following the abolition of this regulation, an amount of 89 billion drachmas, which was previously required to be deposited with the Bank of Greece, was gradually released.

Credit to agriculture, excluding changes in the supplies account of the Agricultural Bank and loans to organisations purchasing agricultural products, increased by 11.9 per cent in 1987, compared with 19.9 per cent in 1986. The slowdown was more pronounced in long-term loans. The Agricultural Bank gave higher priority to financing projects included in development programmes and increased its short-term credit to agricultural cooperatives, while the increase in cultivation loans was contained at a lower level than in 1986. A significantly accelerated growth rate was recorded in loans to organisations purchasing agricultural products (1987: 31.9 per cent; 1986: 19.5 per cent).

Credit to small-scale industry increased by 9.7 per cent in 1987, against 18.2 per cent in 1986. Specifically, low-interest loans, which account for more than 80 per cent of total credit to small-scale industry, increased by 11 per cent compared with 24 per cent in 1986. In 1987, the ceiling per borrower in respect of credit out of funds earmarked "for loans to small-scale industry" to trading companies and professionals for cash purchases of products directly from manufacturers was raised from 20 million drachmas to 40 million drachmas. Furthermore, as from mid-year the maximum average amount of annual turnover per person employed set for deciding whether a manufacturing firm can be included in the "small and medium-size" category was abolished. Despite these arrangements, however, no significant increase was recorded in loans under this category. In addition, the increase in the outstanding balance of these loans was considerably smaller than the amount of bank funds earmarked for loans to small-scale industry. As a result, the unused balances of these funds deposited with the Bank of Greece rose from

DIAGRAM IV.10

CREDIT FOR WORKING CAPITAL *

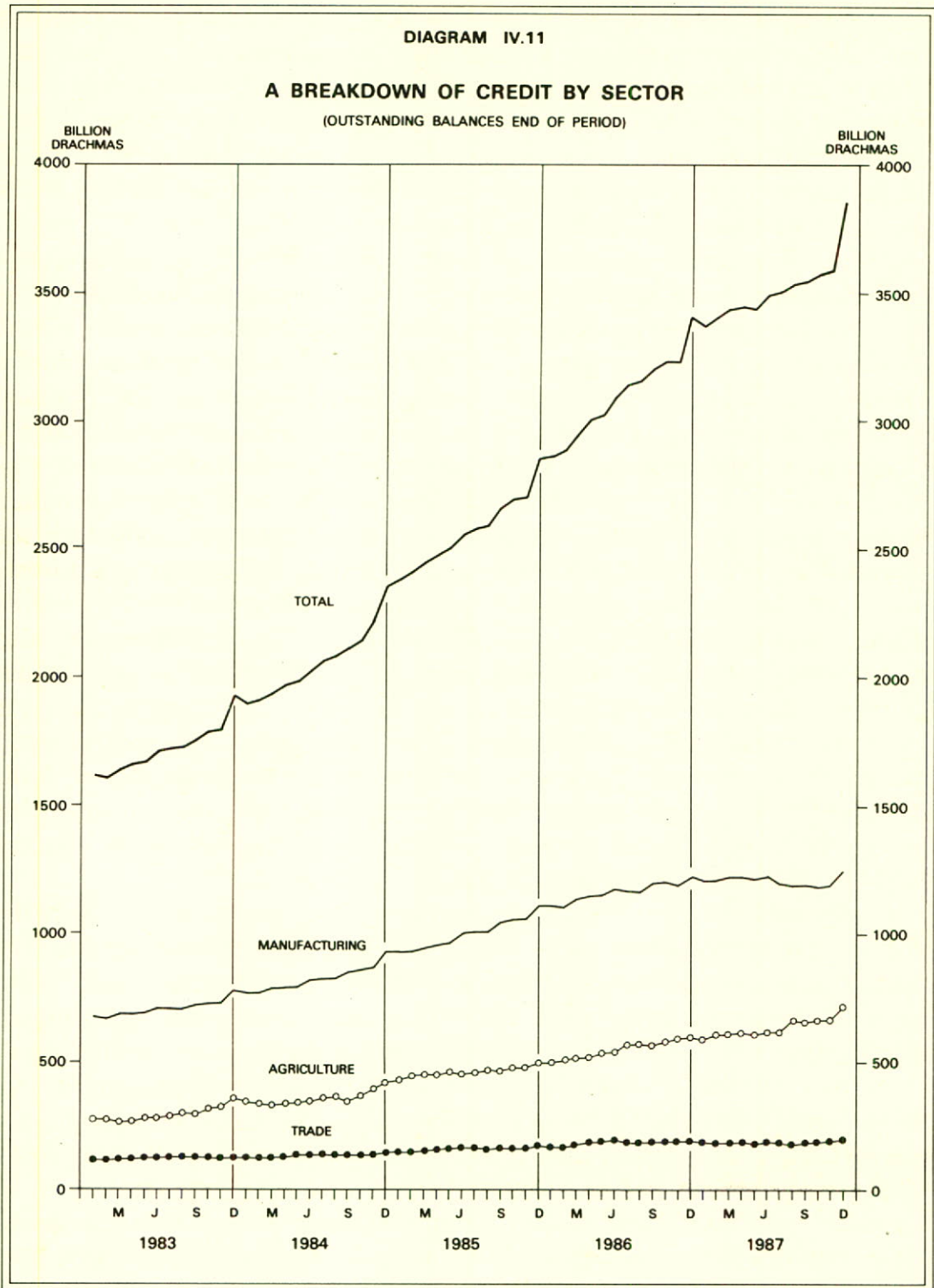


* Excluding credits to public enterprises.

58 billion drachmas at the end of 1986 to 103 billion drachmas at the end of 1987. The slow rate of growth of this special category of loans and the marked variation per bank in unused balances held at the Bank of Greece imply that the earmarking of 10 per cent of commercial bank deposits yields considerably larger funds than those required to meet respective demand, although to some extent which is not easy to determine, this could be attributed to the reluctance of some banks to meet the credit requirements of small manufacturing firms. This reluctance is also reflected in the fact that the commercial banks have shown no interest in creating an appropriate technical and economic infrastructure, which would contribute not only to meeting the borrowing requirements of small manufacturing firms more fully and to the more effective utilisation of the loans involved, but also to reducing the risks assumed by the State in guaranteeing these loans. As has been stressed on several occasions, meeting the borrowing requirements especially of very small and new firms more fully, requires that credit be accompanied by appropriate technical and economic assistance from the banks making loans to small-scale industry. Cooperation with the Hellenic Organisation of Small and Medium-Size Handicraft Enterprises could be useful, as could a higher degree of specialisation of certain smaller banks in lending to small-scale industry, provided that banks acquire the technical and economic infrastructure required.

The recent raising of the ceiling on loans to small and medium-size manufacturing firms out of earmarked funds and the extension of this facility to larger enterprises are expected to contribute to an increase in loans under this category. But if the banks involved fail to proceed to the parallel creation of appropriate technical and economic infrastructure, it seems rather doubtful whether the access of very small and new enterprises to bank credit will improve substantially. It should be pointed out that following the increase as from 1 January 1988 in the interest rate on commercial bank funds deposited with the Bank of Greece and earmarked for financing small and medium-size manufacturing firms, bank lending to very small enterprises may be further discouraged.

Last year's slower growth of total credit to trade (1987: 1.4 per cent; 1986: 13 per cent) stemmed from a decrease in credit to tobacco trade (1987: -52 per cent; 1986: 27.1 per cent) and to export trade (1987: -10.8 per cent; 1986: 27.4 per cent), while credit to domestic and import trade expanded faster than in 1986. The decrease in credit to tobacco trade was due to the reluctance of private agencies to purchase tobacco from the 1986 crop, while



the decrease in credit to export trade, which mainly consists of credit for purchasing and exporting agricultural products, was related to decreased agricultural production owing to adverse weather conditions in 1987. The faster growth of credit to domestic trade (1987: 17 per cent; 1986: 8 per cent) is related mainly to improved terms on credit to tradesmen for meeting extraordinary requirements, though a faster growth rate was also recorded in credit for cash purchases from manufacturers.

Housing loans increased at a lower rate than the target set in the monetary programme (10 per cent, against a targeted rate of 12 per cent). This development was mainly due to smaller disbursements of loans granted by the Agricultural Bank and, to a lesser extent, by the Postal Savings Bank and the Deposits and Loans Fund. By contrast, disbursements under the National Mortgage Bank's housing programme were normal, and no particularly increased disbursements under specific categories of loans were recorded. Disbursements under the workers' housing loan scheme totalled 7.4 billion drachmas, having absorbed most of the 8 billion drachmas allotted by the National Mortgage Bank for this purpose, while housing loans carrying a freely negotiable interest rate recorded a faster increase again in 1987 (11.1 billion drachmas, compared with 7 billion drachmas in 1986). In connection with loans granted under the workers' housing scheme, it should be pointed out that a serious problem still exists as regards their servicing. To the extent these loans are financed with bank deposits, delays in servicing are a serious stumbling block for the expansion of this scheme. A very large amount of funds disbursed under the workers' housing loan scheme has already been immobilised, and this has an adverse effect on both the liquidity and the financial status of the National Mortgage Bank.

Lastly, as Table IV.8 shows, a slowdown was also recorded in the growth rate of short-term credit to other private sector activities, despite a considerable increase in consumer credit, especially through the use of credit cards. In particular, loans under the latter category increased by 6.5 billion drachmas in 1987, against 3.7 billion drachmas in 1986, while the number of credit card holders increased by 125,000 (1986: 72,000) and totalled 391,000 at the end of the year. These developments were due to the considerable improvements introduced by the Bank of Greece in the operation of the credit card system, and to the keen interest shown by banks in promoting it. In February 1987, each bank's overall ceiling on credit extended through credit cards was raised from 4 billion to 6 billion drachmas, while in November 1987 ceilings per bank were abolished. In addition, the ceiling on credit per

card holder was doubled (from 75,000 drachmas to 150,000 drachmas), and authorisation was granted to interested banks to issue credit cards.

3. CAPITAL MARKET

In 1987, there were particularly significant developments in both the primary and the secondary capital markets. In the primary market, a variety of financial instruments offered by the Government on attractive terms met with a satisfactory response from savers. As a result, a substantial part of the PSBR was financed from nonbank sources.

Total net funds drawn from the capital market amounted to 341 billion drachmas in 1987, against 114 billion drachmas in 1986. This increase stemmed almost entirely from sales of treasury bills and government bonds to the public, while the amount of funds drawn by specialised credit institutions through bank bond issues was very small. The remainder came from a DM-indexed bond issue of the Public Power Corporation (PPC) in the amount of 4.6 billion drachmas, and from increases mainly in the share capital of banks and industrial firms, in the amount of 11.5 billion drachmas (1986: 6 billion drachmas).

These developments underline the possibilities of the Greek capital market for financing both public agencies and private enterprises. In 1987, four new companies were listed, while in the last two months of the year the listing of other new companies was postponed, as was also postponed an increase in the share capital of companies already listed. The reason for this was the downward trend of share prices, following the October upheaval in world financial markets.

At the end of 1987, the value of outstanding fixed income securities amounted to 634 billion drachmas, of which 252 billion drachmas (39.7 per cent) represented bank bonds, 240 billion drachmas (37.9 per cent) treasury bills purchased by the nonbank public, 133 billion drachmas (21 per cent) government bonds, and 9 billion drachmas (1.4 per cent) bonds issued by public enterprises (PPC).

Transactions on the Athens Stock Exchange were very brisk in 1987 and their total value amounted to 61.6 billion drachmas, against 5.4 billion drachmas in 1986. This increase stemmed almost entirely from transactions in shares, which accounted for 97 per cent of total transactions, against 84 per cent in 1986.

Both the volume of transactions and prices exhibited wide fluctuations during the year. In the last months of 1986, transactions on the Athens Stock Exchange started to increase gradually, and this continued into 1987. It is remarkable in this connection that in the period January-June 1987 transactions averaged 1.1 billion drachmas a month, while the share price index rose by 65.4 per cent.

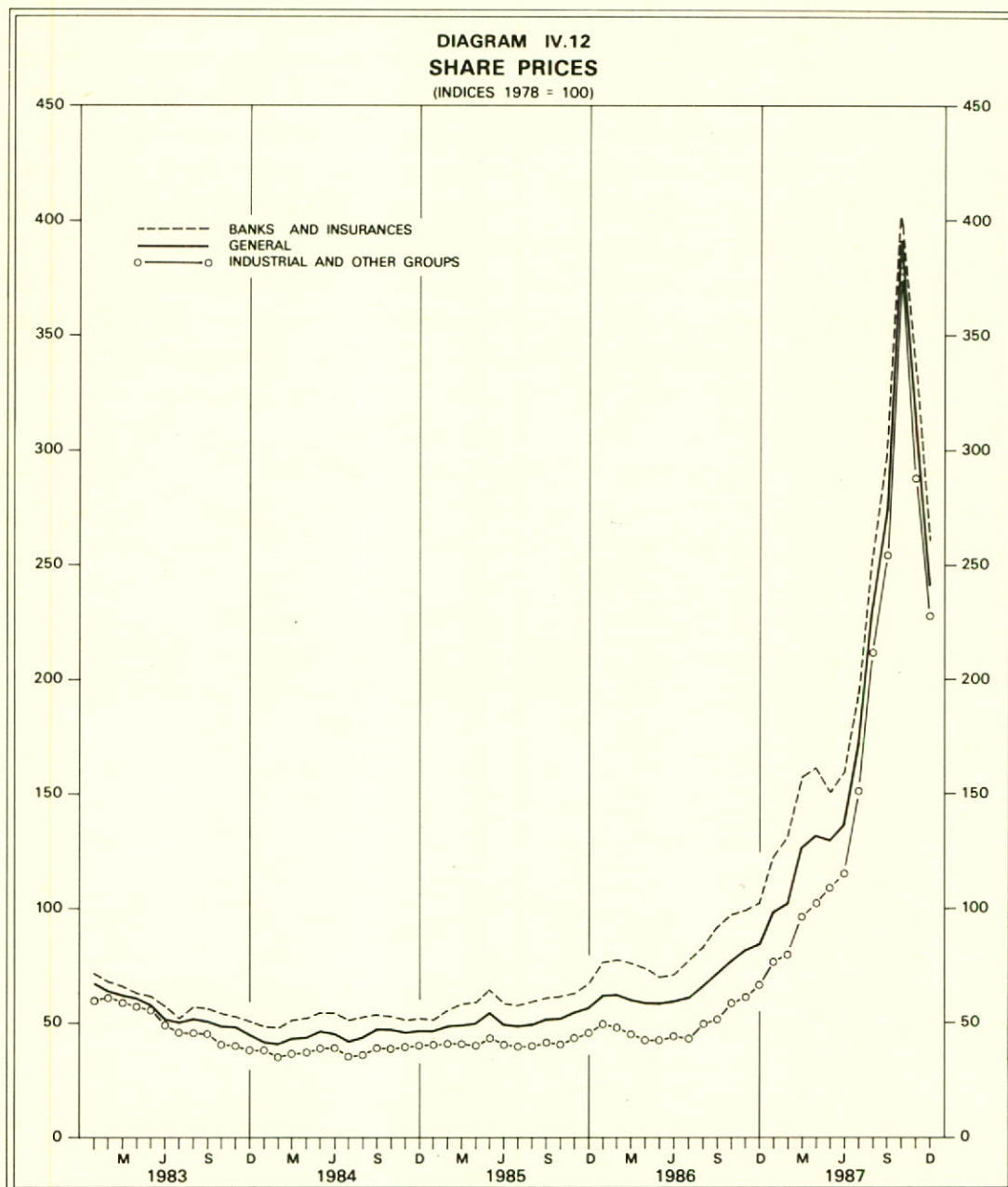
The publication of the balance sheets of enterprises which showed considerable profits, combined with the speculative trends that had in the meantime started to strengthen and the decrees issued by the Bank of Greece in order to improve the terms and procedures for the acquisition by non-residents of domestic securities dealt in on the Athens Stock Exchange, contributed to an increase in demand for shares over the months that followed. In the period July-September 1987, average monthly transactions increased to 5.5 billion drachmas, and in October to 21 billion drachmas. The share price index rose by 116.5 per cent in the period July-October. Immediately after the October upheaval in world financial markets, the Athens Stock Exchange suspended operations for 4 working days. Subsequently, share prices declined, and in the two-month period November-December they fell by 26.7 per cent. In the early months of 1988, however, the stock market recovered and the share price index rose by 12.3 per cent in the period January-March.

In 1987, the price index compiled by the Bank of Greece for industrial shares rose by 239.5 per cent, and the price index for bank and insurance company stock rose by 153.8 per cent. By contrast, price indices dropped by 2.2 per cent for long-term government bonds and by 21.5 per cent for bonds issued by public enterprises (PPC).

The total current value of securities traded on the Athens Stock Exchange amounted to 1,355 billion drachmas at the end of 1987, compared with 601 billion drachmas in 1986. This substantial increase (125.4 per cent) was mainly due to higher share prices and to the new government bond issues traded on the Athens Stock Exchange.

Last year's developments in the Athens Stock Exchange highlight existing weaknesses and especially the very slow adjustment of supply to sharp increases in demand. These weaknesses result in higher prices in the secondary capital market and disrupt its smooth operation, besides giving rise to speculative trends. A new law bill has been proposed for the more efficient operation and modernisation of the Athens Stock Exchange; the same law bill provides for the introduction of new services better suited to investors' requirements.

Furthermore, given that the stock market is the main alternative source of funds and potentially an important channel through which foreign capital



will be attracted by Greek enterprises, the authorities have taken a number of measures aimed at enhancing, directly or indirectly, the efficiency of the stock

market. These measures include: i) an increase in the tax-exempt portion of income from dividends (from 30,000 drachmas to 50,000 drachmas if dividends derive from a single company, and from 120,000 drachmas to 200,000 drachmas if they derive from several companies), ii) an adjustment in the value of land and buildings on the basis of their market value, iii) exemption from corporate income tax of 50 per cent of retained profits in respect of the financial year 1987, provided these tax-exempt profits are used for financing productive investment to be realised within the next three years, and iv) exemption from corporate income tax of 50 per cent of profits in respect of financial year 1988, provided these profits derive from export activity. Parallel to the above, the Bank of Greece has issued a number of decrees setting the terms and procedures for the acquisition by non-residents of domestic securities dealt in on the Athens Stock Exchange, as well as for the repatriation of income and proceeds from the liquidation and redemption of these securities.

APPENDIX TO CHAPTER IV

CHRONOLOGY OF MONETARY AND CREDIT POLICY MEASURES

1 9 8 7

7 January

The special licences required by law are granted for the establishment of three leasing companies, subsidiaries of an equal number of banks.

8 January

— With effect as from 1 January 1987, the percentages of interest refunds to exporters, granted according to Decision 1574/70 of the Currency Committee, are lowered to 45 per cent of the previous rates for exports to EC member countries and to 60 per cent for exports to non-EC countries.

— With effect as from 1 February 1987, the advance deposit requirements on imports in the two categories, 80 per cent and 40 per cent respectively, are reduced by half (40 per cent and 20 per cent respectively).

19 January

The Agricultural Bank is authorised to finance fixed investment by private firms processing agricultural products; the interest rate and other terms will be the same with those on commercial bank credit to these firms.

26 January

With effect as from 31 January 1987, commercial banks' primary reserve requirements with the Bank of Greece are raised by half a percentage point to 4.5 per cent for special time deposits and 6.5 per cent for the other categories of private deposits in drachmas and foreign currency.

27 January

Commercial banks are permitted to invest in three-month treasury bills part of their compulsory deposits with the Bank of Greece, not exceeding 2.5 per cent of their deposits.

29 January

The interest refund to exporters in respect of export proceeds to be converted into drachmas between 1 April 1987 and 31 December 1987 is reduced from 5 per cent to 3 per cent. As from 1 January 1988 no interest refund to exporters is granted.

2 February

With effect as from 9 February 1987, the interest rate on the debit balances of banks' current accounts with the Bank of Greece for the part up to 15 per cent of each bank's own funds, or 0.25 per cent of each bank's total drachma and foreign exchange deposits at the end of the previous year, is set at 22.5 per cent p.a.

6 February

— A uniform framework is formulated for the financing by the commercial banks and the Agricultural Bank of private and cooperative enterprises and cooperative agencies for purchasing, marketing, standardising and processing the main agricultural products.

— The overall ceiling on credit extended by the National Bank and the Commercial Bank through the system of credit cards is raised from 4 to 6 billion drachmas for each of the two banks.

13 February

The Agricultural Bank is authorised to extend credit for fixed investment and working capital to firms engaged in manufacturing activity related to the processing, standardisation, packing or marketing of agricultural and live-stock products.

27 February

Commercial banks and specialised credit institutions are permitted to accept 7 to 90 day term-deposits, at freely negotiable rates, from individuals, legal entities in private law, and public and municipal enterprises.

4 March

Arrangements are made for the transfer abroad of locally derived profits of foreign banks operating in Greece.

10 March

— Commercial banks operating in Greece or their specially established subsidiaries are permitted to engage in non-recourse factoring/forfaiting on behalf of Greek exporters.

— Commercial banks are authorised to approve and grant foreign exchange to Greeks travelling abroad for health reasons or studies.

27 March

— With effect as from 1 April 1987, interest rates on bank bonds and special time deposits are set as follows:

For bank bonds with a nominal value:

— up to 1 million drachmas, 17 per cent.

— from 1 million drachmas to 3 million drachmas, 18 per cent.

— 3 million drachmas and over, 19 per cent.

For special time deposits:

— for the part of the deposit up to 1 million drachmas, 17 per cent.

— for the part of the deposit from 1 million drachmas to 5 million drachmas, 18 per cent.

— for the part of the deposit over 5 million drachmas 19 per cent.

— With effect as from 1 April 1987, the interest rate on non-compulsory time deposits in drachmas with the Bank of Greece by banks issuing bonds is set at 14 per cent (previously 16 per cent) for 30-day deposits, 14.5 per cent (previously 16.5 per cent) for 60-day deposits and 15 per cent (previously 17 per cent) for 90-day deposits.

22 April

— Manufacturing, mining and hotel enterprises are permitted to contract loans in foreign exchange with foreign and domestic credit institutions, under certain terms and conditions, without prior approval by the Bank of Greece.

— Insurance and other public organisations, governed by the provisions of Law 1611/50, are permitted to invest in treasury bills and bond issues by the Government and public enterprises, without prior approval by the Bank of Greece.

4 May

— Commercial and investment banks are permitted to finance domestic shipping firms for purchasing passenger ships in Greece or abroad. The loan may amount up to 75 per cent of the purchase value and the interest rate is set at 21.5 per cent. The other terms of the loans are determined by the lending bank.

— Commercial banks are permitted to finance legal entities and non-profit associations for purchasing equipment and for working capital purposes. The interest rate is 21.5 per cent, other terms being determined by the lending bank.

8 May

With effect as from 11 May 1987, the interest rate on commercial banks' non-compulsory time deposits in drachmas with the Bank of Greece is set at 14 per cent (previously 16 per cent) for 30-day deposits, 14.5 per cent (previously 16.5 per cent) for 60-day deposits and 15 per cent (previously 17 per cent) for 90-day deposits.

15 May

The Agricultural Bank or its specially established subsidiary is permitted to engage in factoring/forfaiting on behalf of Greek exporters, under the terms and conditions applying to commercial banks.

9 June

Commercial banks are permitted to finance firms for the payment of the Value Added Tax corresponding to cash purchases of domestic products and to fixed asset investments. The Agricultural Bank is permitted to finance firms for the payment of the VAT corresponding to specific investments in the agricultural sector.

23 June

- The total amount of credit per firm, extended out of the earmarked funds for small-scale enterprises, to trading companies and professionals, for cash purchases of domestic products directly from small-scale manufacturing firms, is raised from 20 to 40 million drachmas.
- Commercial banks are permitted to finance leasing companies from own funds on freely negotiable terms.

29 June

- With effect as from 30 June 1987, a minimum interest rate of 21 per cent is set on all working capital loans to which maximum interest rates of 20 per cent to 21.5 per cent previously applied.
- As from the same date, the minimum interest rates on short-term and long-term loans are raised by one percentage point to 17 per cent and 16 per cent respectively.
- With effect as from 30 June 1987, primary reserve requirements on special time deposits with commercial banks are increased by two percentage points and thus brought in line with the rates applicable to all categories of deposits.
- With effect as from 1 July 1987, the requirement on commercial banks to earmark 15 per cent of their deposits for financing fixed investment by private enterprises is abolished. Banks are still required to allocate a proportion of their deposits for the financing of public enterprises and organisations. This proportion is to be raised gradually from 8 per cent to 10.5 per cent of bank deposits by the end of November 1987.
- Financial institutions are allowed to offer certificates of deposit with a minimum denomination of 5 million drachmas and maturities of 3, 6, 12 and 18 months, at freely negotiable interest rates.

7 July

- As from 30 June 1987, the interest rate on temporary deposits of commercial banks with the Bank of Greece, out of the funds earmarked for compulsory investment in treasury bills, is raised from 17 to 17.5 per cent.
- The limit of financing commercial firms to meet exceptional needs is adjusted to 15 per cent of turnover up to 50 million drachmas and to 10 per cent of turnover over 50 million. The credit limit per firm is increased from 7.5 to 25 million drachmas.

9 July

With effect as from 10 July 1987, loans by commercial banks for new fixed investment of manufacturing, handicraft, mining and hotel enterprises are exempted from the contribution to the joint account of banks for supporting export firms. The rebate for these loans is set at 5 per cent.

10 July

With effect as from 15 July 1987, the refinancing limit of the Agricultural Bank by the Bank of Greece for loans to the private sector is reduced from 64.5 to 35 billion drachmas. The interest rate is raised from 16 to 17 per cent for the amount exceeding 10 billion drachmas.

20 July

The criterion of 10 million drachmas turnover per person employed, for the financing of small and medium-size handicraft firms out of the earmarked funds under Currency Committee decision 197/3 April 1978, is abolished.

21 July

With effect as from 22 July 1987, the penalty rate on bank loans in drachmas is set 4 percentage points higher than the contractual interest rate, provided the contractual rate is lower than the minimum rate of 21 per cent set by Bank of Greece decision 1087/29 June 1987. The penalty rate is freely negotiable up to 4 percentage points over the contractual rate for loans extended at the minimum interest rate of 21 per cent and over.

3 August

Manufacturing, mining and hotel enterprises, which are contracting or have already contracted loans in foreign exchange, are permitted, without prior approval by the Bank of Greece, to extend the loan's maturity, to convert the loan into a currency other than the contractual one and to repay the loan before maturity, provided six months at least have lapsed since the conversion of the relevant foreign exchange into drachmas.

31 August

With effect as from 1 September 1987, the interest rate on non-compulsory time deposits of commercial banks with the Bank of Greece is set at 12 per cent (previously 14 per cent) for 30-day deposits, 12.5 per cent (previously 14.5 per cent) for 60-day deposits and 13 per cent (previously 15 per cent) for 90-day deposits.

1 September

— Part of the primary reserves of commercial banks, corresponding to 2 per cent of their deposits, becomes non-interest bearing, while on the remaining part (4.5 per cent of deposits) the interest rate is reduced from 15.5 per cent to 14 per cent.

— Credit card holders may temporarily exceed their credit limit, provided they pay the overrun not later than 30 days after being billed.

2 September

The terms of sale of durable goods to final consumers on credit are also applied to second-hand goods, with the exception of second-hand private vehicles which continue to be sold on a cash basis.

11 September

Commercial banks are permitted to finance legal entities and non-profit associations for fixed investment purposes. The interest rate and the other terms of the loans will be determined by the lending bank (minimum rate 21 per cent).

17 September

With effect as from 21 September 1987, the interest rates on non-compulsory time deposits of specialised credit institutions with the Bank of Greece are brought in line with the rates applicable to commercial banks.

22 September

— Commercial banks and specialised credit institutions (except investment banks) are permitted to extend loans to owners for the repair and maintenance

of their buildings, on freely negotiable terms and at a minimum interest rate of 21 per cent.

— The ceiling per borrower and per bank on housing loans at a freely negotiable interest rate is abolished.

— The Agricultural Bank and the commercial banks are permitted to finance the Special Account of Guarantees of Agricultural Products (SAGAP) for the payment of agricultural subsidies and grants covered by the EEC.

— The Agricultural Bank is included in the system of reserve requirements on deposits. The proportion of its deposits that has to be placed with the Bank of Greece is set at 2 per cent.

— The limit of credit expansion by the Agricultural Bank to the private sector is reduced by 15 billion drachmas; the limit of credit expansion to the public sector is raised by an equal amount.

— The total amount of foreign exchange allowed for tourist or family reasons to travellers to non-EC countries is increased from USD 250 to USD 600 or its equivalent in another currency.

— Credit-card issuers are permitted to issue corporate credit cards covering expenses abroad by business executives travelling for professional reasons.

25 September

Firms contracting loans under Bank of Greece decision 1011/22 April 1987 are permitted to use these loans directly abroad, without prior approval by the Bank of Greece, for the settlement of obligations accruing from loans in foreign exchange for the purchase of mechanical equipment, raw materials and know-how.

5 October

Individuals and legal entities are allowed to invest in government bonds funds which are not compulsorily converted into drachmas. The proceeds from the redemption or sale of the securities and their coupons are freely transferable abroad or deposited in a foreign exchange account.

6 October

The extension of bank loans on collateral of government bonds is permitted.

8 October

With effect as from 10 October 1987, primary reserve requirements of commercial banks with the Bank of Greece are raised from 6.5 to 7.5 percentage points. The non-interest bearing part is raised from 2 to 3 percentage points.

9 October

The ceiling of 5 billion drachmas for Agricultural Bank borrowing from the interbank market is abolished.

16 October

Banks are permitted to invest in bonds issued by the Government, public enterprises and organisations, credit institutions and private firms, without prior approval by the Bank of Greece.

Credit institutions are allowed to invest in shares only after prior approval by the Bank of Greece.

5 November

The transfer and acceptance of loans between banks operating in Greece is permitted.

11 November

Mortgage banks are permitted to extend loans for fixed investment to commercial firms and professionals, under the same terms and conditions applicable to commercial banks.

12 November

— It is permitted to transfer abroad coupons, dividends and the proceeds from the liquidation of securities listed on the Athens Stock Exchange, provided these are obtained through the import and conversion into drachmas of foreign exchange by non-EC residents.

— Ceilings per bank on credit extended through credit cards are abolished.

20 November

— With effect as from 23 November 1987, the interest rate and other terms of time deposits and savings deposits on notice are freely determined by the banks. As from the same date, the interest rate on savings deposits with the Agricultural Bank is brought in line with that of commercial banks.

— With effect as from 23 November 1987, financial institutions, authorised to issue bank bonds, are allowed to negotiate freely the interest, maturity (one year minimum) and other terms of issue and sale of these bonds.

— With effect as from 23 November 1987, banks' non-compulsory time deposits in drachmas with the Bank of Greece are non-interest bearing.

27 November

With effect as from 30 November 1987, financial institutions are authorised to extend loans for fixed investment to manufacturing, mining, tourist and shipping enterprises at freely negotiable interest rates. The penalty rate may be fixed up to 4 percentage points higher than the contractual one.

30 November

— The refinancing limit of the Agricultural Bank by the Bank of Greece for financing organisations purchasing agricultural products and EEC agricultural subsidies and grants is raised by 10 billion drachmas.

— With effect as from 1 December 1987, investment and mortgage banks are permitted to participate in the interbank market, with a 500 million drachma ceiling for each credit institution.

— Investment banks are allowed to underwrite the issue of new shares by enterprises, without prior approval by the Bank of Greece, provided that these enterprises are not subsidiaries of the respective banks.

— Banks are permitted, under certain terms and conditions, to extend loans in foreign exchange to shipping firms for purchases from abroad of passenger vessels and ferry-boats scheduled for Greek coastal shipping.

3 December

With effect as from 1 December 1987, the existing balances of loans granted by investment banks to manufacturing, mining and hotel enterprises for construction, rebuilding and repair of vessels in Greek shipyards, are exempted

from the required contribution to the joint account of banks for assisting export firms.

4 December

— The credit limit per credit card holder is raised from 75,000 to 150,000 drachmas. The cash payment limit to card holders is raised from 5,000 to 20,000 drachmas per month.

— Manufacturing firms and manufacturing cooperatives are allowed to use hedging techniques and to engage in options in foreign commodity markets.

— Firms are permitted, irrespective of whether they are financed or not by the banking system, to invest in securities listed on the Athens Stock Exchange.

7 December

Legal entities, except those under Law 1611/50, are permitted to invest in bank bonds, irrespective of whether they are financed or not by the banking system.

14 December

The financing limit of the Agricultural Bank to marketing boards, agencies and cooperatives for purchasing agricultural products is raised by 17 billion drachmas, whereas the ceiling of its other loans is reduced by 7 billion drachmas. The refinancing limit of the Agricultural Bank by the Bank of Greece is raised by 10 billion drachmas.

21 December

With effect as from 1 January 1988, the foreign exchange allowed for travel to Cyprus is equalised to that allowed for travel to EC countries.

30 December

— Firms which have received loans in foreign exchange from a foreign bank are permitted to replace the lending bank with another one, with a simultaneous transfer or acceptance of non-matured and due commitments.

With effect as from 1 January 1988:

— The minimum interest rate of 21 per cent applicable to short-term bank

loans is abolished. The respective required reserves are reduced from 20 to 18 per cent, effective as from 31 January.

— The discount rate is reduced from 20.5 to 19 per cent.

— Interest rates on the interest-bearing part of commercial banks' primary reserve requirements and on the unused balance of their reserves for financing small and medium-size enterprises are unified at 12.5 per cent.

— Interest rates on the outstanding balance in the accounts for the refinancing of the Agricultural Bank by the Bank of Greece are raised and unified at 19 per cent.

— With effect as from 10 January 1988, reserve requirements on deposits with the Agricultural Bank are raised from 2 to 3 per cent.

1988

2 February

With effect as from 31 January 1988, the interest rate on temporary deposits of commercial banks with the Bank of Greece out of the funds earmarked for compulsory investments in treasury bills is reduced from 17.5 to 17 per cent.

18 February

— The unused balances of compulsory deposits of commercial banks earmarked for financing small-scale industry will bear interest at a unified rate of 15 per cent for the financial year 1987.

— With effect as from 1 March 1988, the mortgage banks, the Postal Savings Bank and the Deposits and Loans Fund are obliged to deposit in a non-interest bearing account with the Bank of Greece amounts equal to 18 per cent of their housing loans extended at freely negotiable interest rates.

2 March

The National Mortgage Bank and the National Housing Bank are permitted to determine freely the terms of loans under the housing loan deposit scheme, provided that, for the housing loans in drachmas, the interest rate must exceed the respective deposits' rate by at least 2.5 percentage points while, for the housing loans against deposits in foreign exchange, the minimum interest rate will be equal to the minimum interest rate on medium and long-term loans. The

loan ceiling per depositor is raised from 4 to 10 million drachmas in the case of housing loans in drachmas, while the respective ceiling of 5 million drachmas on housing loans against deposits in foreign exchange is abolished.

31 March

New criteria are set for identifying manufacturing firms eligible for financing out of funds earmarked for credit to small and medium-size enterprises. Specifically, the following two conditions must be met:

a) The average annual turnover in the preceding three years must not exceed 350 million drachmas (previously 250 million drachmas).

b) The average annual number of employees over the preceding three years must not exceed 100 persons (previously 50 persons).

The maximum amount a firm can borrow out of earmarked funds is increased from 80 to 100 million drachmas.

1 April

Financial institutions are permitted to reschedule, apart from debts of manufacturing, mining and hotel enterprises, debts in drachmas and foreign exchange of cooperatives and organisations. Respective terms will be determined by these institutions, under certain conditions.

V. PUBLIC FINANCE

1. PUBLIC SECTOR BORROWING REQUIREMENTS AND THEIR FINANCING

The public sector's net borrowing requirements, on a cash basis, are estimated to have decreased to 13.5 per cent of GDP in 1987, compared with 14 per

TABLE V.1
NET BORROWING REQUIREMENTS OF THE PUBLIC SECTOR¹
(In million drachmas)

	1983	1984	1985	1986	1987*
1. Central Government	297,903	479,840	664,673	577,980	736,633
- Government budget	300,531	409,418	638,111	582,549	678,475
(Ordinary budget)	(150,719)	(229,129)	(401,867)	(325,484)	(405,833)
(Public investment budget)	(149,812)	(180,289)	(236,244)	(257,065)	(272,642)
- Special management accounts of the State ¹	-2,628	70,422	26,562	-4,569	58,158
(Oil account)	(-8,948)	(65,658)	(49,985)	(-12,033)	(28,581)
(AMMS etc.)	(6,320)	(4,764)	(-23,423)	(7,464)	(29,577)
Percentage of GDP	9.7	12.6	14.4	10.4	11.6
2. Public organisations ²	-35,461	1,488	33,627	76,027	41,496
- Financing of local insurance organisations	24,906	37,327	59,253	116,708	130,034
- Financing of local authorities	1,193	5,495	10,307	11,563	7,421
- Financing of other organisations	1,528	4,700	2,194	10,498	12,648
- Cash balances	-63,088	-46,034	-38,127	-62,742	-108,607
Broader Central Government (1+2)	262,442	481,328	698,300	654,007	778,129
Percentage of GDP	8.5	12.7	15.1	11.8	12.2
3. Public enterprises ³	88,190	103,946	130,121	122,143	81,864
- Public utilities	71,200	73,200	107,426	81,180	47,119
(Financing)	(62,138)	(77,921)	(107,850)	(82,494)	(48,692)
(Cash balances)	(9,062)	(-4,721)	(-424)	(-1,314)	(-1,573)
- Other enterprises	16,990	30,746	22,695	40,963	34,745
(Financing)	(11,233)	(34,291)	(24,720)	(39,406)	(46,760)
(Cash balances)	(5,757)	(-3,545)	(-2,025)	(1,557)	(-12,015)
Public sector (1+2+3)	350,632	585,274	828,421	776,150	859,993
Percentage of GDP	11.4	15.4	17.9	14.0	13.5

¹ Results from the movement of respective accounts with the Bank of Greece, the Agricultural Bank, and the commercial banks.

² Estimates on the basis of their investment in securities and bank deposits and of the change in their liabilities to the banking system.

³ Bank of Greece data.

* Provisional data.

cent in 1986. This decrease would have been larger by about one percentage point if central government revenue had not been adversely affected by a

change in the timing of EEC payments of agricultural subsidies, and the strike called by public cashiers.

As Table V.1 shows, in 1987 the borrowing requirements of central government recorded an increase, both in absolute figures and as a percentage of GDP. This increase stemmed from the ordinary budget and the special management accounts, while borrowing requirements under the public investment budget declined from 4.6 per cent of GDP in 1986 to 4.3 per cent in 1987.

Borrowing requirements under the ordinary budget¹ (minus amortisation payments) rose to 6.4 per cent of GDP in 1987, against 5.9 per cent in 1986. This was the outcome of the lower growth of revenue than in 1986, and the inability to contain the expansion of expenditure. The 58 billion drachma increase in transfers out of the ordinary budget to the Social Insurance Institute (IKA) and to public transport organisations for financing their deficits and the larger expenditure for interest payments on the public debt were the main factors that contributed to the inelasticity of expenditure. By contrast, the drop in the dollar rate had a mild contractionary effect on the growth of expenditure.

The results of the special management accounts reversed from a small surplus in 1986 to a deficit approaching 1 per cent of GDP in 1987. This was due to both the oil accounts and the account of Community agricultural subsidies and grants managed by the Agricultural Markets Management Service (AMMS). The larger borrowing requirements under the oil account were due to an accumulation of stocks and to the deficit run in 1987 as a result of the spread between cost and selling price of oil products, partly owing to the rise in world oil prices. The increase in the borrowing requirements of AMMS was due to the change in the system of payment of Community guarantees, which as from last October are paid on an *ex post* basis, and not in advance as was done previously. It should be noted that the results of special management accounts include the results of accounts financed mainly by the Government or managed on its behalf. By contrast, they do not include credit expansion to agricultural marketing boards and cooperatives, such as the Association of Sultana Growers Cooperatives, the Central Agency for Handling Home Prod-

¹ Borrowing requirements under the government budget, on a cash basis, differ from its deficit on an accrual basis. This is due to the extension of the fiscal year, which affects the fiscal result, and to time lags between the recording of revenue and expenditure in the budget and the realisation of respective receipts and payments.

ucts, the AGREX, the Cooperative of Fertiliser Companies, etc. Any claims of these agencies on the Government, in the context of their operations, are financed with transfers from the government budget. Changes in the outstanding balance of credit to these agencies are included in credit expansion to the private sector.

The borrowing requirements of social insurance organisations, local authorities and other public organisations fell from 1.4 per cent of GDP in 1986 to 0.6 per cent in 1987. This was due to two main factors: (i) the containment of the upward trend in credit to public organisations, which reflects a 9 billion drachma reduction in borrowing by IKA, following the increase by 50 billion drachmas in transfers out of the ordinary budget to finance its deficits, and (ii) the increase by 73.1 per cent in the surpluses of public organisations deposited with banks or invested in treasury bills and other types of government paper.

The decrease in the net borrowing requirements of public organisations, as a percentage of GDP, offset part of the increase in the borrowing requirements of central government. As a result, the net borrowing requirements of the public sector broadly defined, which includes central government, social insurance organisations, local authorities and other public organisations, were contained at 12.2 per cent of GDP (1986: 11.8 per cent).

The net borrowing requirements of public enterprises decreased by 40 billion drachmas to 1.3 per cent of GDP (1986: 2.2 per cent). This was mainly due to a decrease in their operating deficit, following the slower growth rate of their current expenditure, while there was a slight increase in the growth rate of their current revenue. The reduction in the borrowing requirements of public enterprises was also due to larger transfers to them out of the ordinary budget, for financing the operating deficits of public transport organisations, as well as to a decrease in investment expenditure. The containment of the borrowing requirements of public enterprises was mainly due to public utilities.

As Table V.2 shows, over two-thirds of the net PSBR was financed with the proceeds from the sale of treasury bills to commercial banks and specialised credit institutions, and with loans and advances extended by credit institutions mainly to public organisations and enterprises. In 1987, the share of credit institutions in the financing of the PSBR was larger than in 1986 and above the average level (about 59 per cent) for the four-year period 1983-1986. A significant increase was recorded in the financing of the PSBR through the sale of treasury bills and medium-term government bonds to the non-bank public. Funds from this source financed 16.5 per cent of the PSBR,

compared with only 2.7 per cent in 1986. In addition to the regular monthly issues of treasury bills during the year, there were also two issues of 3-year ECU-linked bonds and two issues of 2-year drachma bonds. The success of

TABLE V.2
SOURCES OF FINANCING THE PUBLIC SECTOR BORROWING REQUIREMENTS
(In million drachmas)

	1983		1984		1985		1986		1987*	
	Amount	Per-centage of total	Amount	Per-centage of total	Amount	Per-centage of total	Amount	Per-centage of total	Amount	Per-centage of total
<i>Domestic borrowing</i>	229,089	65.3	416,209	71.1	558,091	67.4	555,566	71.6	785,265	91.3
-Treasury bills purchased by banks and specialised credit institutions	180,217	51.4	195,905	33.5	336,086	40.6	211,942	27.3	267,864	31.2
-Treasury bills and bonds purchased by private savers and enterprises	-1,340	-0.4	-219	—	8,852	1.1	21,030	2.7	142,244	16.5
-Loans and advances from specialised credit institutions and commercial banks	65,931	18.8	139,075	23.7	84,744	10.2	250,071	32.2	318,957	37.1
-Bank of Greece	-15,719	-4.5	81,448	13.9	128,409	15.5	72,523	9.4	56,200	6.5
<i>Foreign borrowing</i>	121,543	34.7	169,065	28.9	270,330	32.6	220,584	28.4	74,728	8.7
Total	350,632	100.0	585,274	100.0	828,421	100.0	776,150	100.0	859,993	100.0

* Provisional data.

these issues was due to their competitive interest rates. By contrast, the share of foreign borrowing in financing the PSBR dropped to 8.7 per cent, against 28.4 per cent in 1986 and an average of 31 per cent in the four-year period 1983-1986. Lastly, financing by the Bank of Greece decreased to 6.5 per cent of the PSBR, compared with 9.4 per cent in 1986.

2. FISCAL MAGNITUDES BY SECTOR

a. The Government Budget

According to provisional data and estimates of the State's General Accounting Office, in 1987 the overall government budget ran a deficit of 801 billion drachmas (excluding prepayments of external debt obligations maturing

beyond 1987 and redemptions of treasury bills held by commercial banks), against 595 billion drachmas in 1986. As a percentage of GDP, the deficit in the government budget rose to 12.6 per cent, against 10.7 per cent in 1986. This increase derived exclusively from the ordinary budget deficit, which amounted to 526 billion drachmas against 322 billion drachmas in 1986, whereas the public investment budget deficit was restrained to 275 billion drachmas (1986: 273 billion drachmas). The ordinary budget deficit rose to 8.2 per cent of GDP (1986: 5.8 per cent), while the public investment budget deficit dropped to 4.3 per cent of GDP (1986: 4.9 per cent). As compared with the initial budget forecast, the ordinary budget deficit was 172 billion drachmas higher, while the deficit in the public investment budget was 39 billion drachmas lower.

As can be seen in Table V.3, ordinary budget revenue expanded by 18.8 per cent (1986: 31.2 per cent) and totalled 1,732 billion drachmas. This figure was 108 billion drachmas lower than the budget forecast. Revenue was adversely affected by tight incomes policy, the considerable shortfall in the yield of tax arrears, and the strike called by public cashiers in December 1987. By contrast, revenue was favourably affected by (i) the large increase in business profits in 1986, which was manifested mainly in the yield of corporate income tax, (ii) the introduction of value added tax, and (iii) the larger than forecast increase in nominal GDP and in the drachma value of non-oil imports.

As in 1986, indirect tax receipts grew faster than revenue from direct taxes. Thus, the share of indirect taxation in total tax revenue rose to about 72 per cent, compared with an average of 70.3 per cent for the two-year period 1984-1985.

Revenue from direct taxes increased by 14.8 per cent, against 27.7 per cent in 1986, but in that year revenue had included almost the entire amount collected from the special tax surcharge imposed late in 1985. If that amount is excluded, the rate of increase in revenue from direct taxes changes to 22.1 per cent for 1987 and 21.2 per cent for 1986. Last year's higher growth rate of revenue from direct taxes originated almost exclusively in revenue from corporate income tax, which increased by 71.1 per cent, mainly owing to the substantially larger profits of sociétés anonymes in 1986. By contrast, revenue from personal income tax was adversely affected, as in 1986, by strict incomes policy and recorded a limited increase. It should be noted in this connection that revenue from income tax withheld at source, which is directly affected by incomes policy, increased by 5.7 per cent, whereas revenue from "main tax"

TABLE V.3
ORDINARY BUDGET REVENUE
(In million drachmas)

	Annual magnitudes			Percentage changes	
	1985	1986	Provisional outturn 1987*	1986/85	Provisional outturn 1987/86
I. DIRECT TAXES	302,891	386,691	444,000	27.7	14.8
1. Income tax	237,868	290,692	370,000	22.2	27.3
- Personal	196,081	225,129	261,500	14.8 ¹	16.2
- Corporate	36,975	60,185	103,000	62.8 ¹	71.1
- Special categories of income tax (Tax on shipping)	4,812 (3,452)	5,378 (3,691)	5,500 (3,700)	11.8 (6.9)	2.3 (0.2)
2. Wealth taxes	14,136	18,431	22,000	30.4	19.4
3. Direct taxes collected on behalf of third parties	8,874	11,021	12,000	24.2	8.9
4. Tax arrears	31,136	31,098	24,000	-0.1	-22.8
5. Extraordinary and other direct taxes	10,877	35,449	16,000	225.9	-54.9
II. INDIRECT TAXES	722,233	971,786	1,163,000	34.5	19.7
1. Customs duties and special contributions on imports-exports	20,927	20,142	22,000	-3.8	9.2
2. Consumption taxes on imports	178,316	212,045	293,000	18.9	38.2
- Turnover tax on imports	49,894	61,212	2,000	22.7	—
- VAT	—	—	170,500	—	—
- Cars	44,245	56,048	39,500	26.7	-29.5
- Regulatory tax	72,278	77,686	64,000	7.5	-17.6
- Special consumption tax	11,137	16,001	16,000	43.7	—
- Other taxes on imports	762	1,098	1,000	44.1	-8.9
3. Consumption taxes on domestic products	304,475	465,947	662,000	53.0	42.1
- Turnover tax	85,716	109,716	33,000	28.0	-69.9
- VAT	—	—	326,000	—	—
- Consumption tax on fuels	100,894	223,106	184,200	121.1	-17.4
- Tax on cars assembled in Greece	6,267	1,749	6,000	-72.1	243.1
- Special levies and contributions on cars	16,061	14,026	13,000	-12.7	-7.3
- Other consumption taxes on domestic products ²	95,537	117,350	99,800	22.8	-15.0
4. Transaction taxes	201,614	254,598	167,000	26.3	-34.4
- Capital transfers	17,557	24,843	28,500	41.5	14.7
- Stamp duties	184,057	229,755	105,000	24.8	-54.3
- Banking business	—	—	33,500	—	—
5. Other indirect taxes	16,901	19,054	19,000	12.7	-0.3
III. TOTAL TAX REVENUE	1,025,124	1,358,477	1,607,000	32.5	18.3
Non tax revenue	85,695	99,424	125,000	16.0	25.7
IV. TOTAL ORDINARY BUDGET REVENUE	1,110,819	1,457,901	1,732,000	31.2	18.8

¹ The withholding of tax on dividends from sociétés anonymes has exerted a negative effect on the first of these two rates and a positive effect on the second one. This is because up to 1985 corresponding revenue was included in revenue from personal income tax while as from 1986 it is included in revenue from corporate income tax.

² Including the special consumption tax on domestic products.

* Estimates on the basis of data available up to 15 April 1988.

and "advance payment of income tax" grew by 33.8 per cent and 31.2 per cent respectively. It should be pointed out, however, that revenue from income tax withheld at source was adversely affected by the introduction of a new tax scale, which is more favourable for salaried employees and wage earners, and of other arrangements aimed at relieving their tax burden.

Revenue from taxation on inheritances, donations and parental gifts to children was favourably affected by an increase in the State-determined starting-off prices of real estate as from January 1987, and the extension of the system of objectively determined real estate value to other cities in Greece. Lastly, revenue from tax arrears, taxes collected in favour of third parties, and extraordinary taxes decreased, with a negative effect on the growth rate of total revenue from direct taxes.

In 1987, revenue from indirect taxes was significantly affected by the introduction of value added tax, though this is not apparent in some categories of revenue. The rate of increase in indirect tax receipts fell from 34.5 per cent in 1986 to 19.7 per cent in 1987. These figures, however, include the effect of the significant increase in liquid fuel consumption tax in 1986 and successive small reductions in this tax over 1987. If this effect is excluded, the rate of increase was about 20 per cent in both years. The principal factors that had a favourable impact on revenue from indirect taxes in 1987 were the introduction of value added tax and an increase in GDP at current prices.

Revenue from VAT on imported goods was 55 per cent larger than the budget forecast, which had been made on the basis of revenue from turnover tax and from stamp duties. This overshooting can be attributed mainly to two factors: First, VAT rates were slightly higher than those required to ensure an amount of revenue equal to the amount that replaced taxes would have yielded. Second, the increase in the drachma value of non-oil imports was larger than the budget forecast. The performance of VAT levied on the distribution of goods and provision of services within Greece cannot be evaluated on the basis of respective revenue in fiscal 1987. This is because the revenue from VAT levied at customs houses refers to a twelve-month period, while the amounts of VAT assessed by tax authorities and collected by public cashiers refer to a nine-month period, because 1987 was the first year that VAT was applied and also because of the strike called by public cashiers late in 1987. It should be stressed that there is very little possibility of tax evasion at customs houses, while tax evasion in respect of VAT levied on the domestic distribution of goods and provision of services is always possible, especially in 1987, the first year VAT was applied.

The growth rate of revenue from capital transfer tax was lower than in 1986, despite an increase in the State-determined starting-off prices of real estate as from January 1987 and the extension of the system of objectively determined real estate value to other cities in Greece. This slowdown is attributable to an increased volume of real estate transactions over the last months of 1986, in view of the forthcoming increase in starting-off prices, as well as to a reduction in the volume of such transactions in the early months of 1987. Revenue from the special consumption tax on cars decreased, because part of this tax was incorporated in VAT, but mainly because of a significant drop in car sales, especially as from the autumn of 1987, owing to expectations of a reduction in the special consumption tax. The same factors caused a decrease in revenue from special levies and contributions imposed on cars. Revenue from the regulatory tax also decreased, because its initial rates were lowered by 20 percentage points as from 1 March 1987. It should be noted that, following this reduction, the regulatory tax rates were lowered by about 33 per cent as compared with those applicable in 1986. The steep drop in revenue from turnover tax on imported and locally produced goods, from the special liquid fuel consumption tax and from stamp duties was exclusively due to the replacement of these taxes, partly or wholly, by VAT. In the case of liquid fuel consumption tax, besides the fact that an amount of about 61 billion drachmas was included in revenue from VAT, a slight reduction was made in the special tax to offset the increase in ex-factory prices following the rise in world oil prices. Total revenue from liquid fuel consumption tax, including VAT, grew by 10.1 per cent, against 121.1 per cent in 1986.

Lastly, the faster growth rate of non-tax revenue was exclusively due to the refund of an uncalled for payment of about 20 billion drachmas to the EC in 1986.

Ordinary budget expenditure, excluding external debt prepayments and redemption of treasury bills held by commercial banks, increased by 26.8 per cent against 18.9 per cent in 1986 and a budget forecast of 23.3 per cent. The accelerated growth rate of expenditure was mainly due to the large increase in public debt servicing payments, grants, payments in respect of government guarantees forfeited, and tax refunds. On the other hand, a contractionary effect on the growth of expenditure was exerted by a lower level of payments of own resources to the EEC, and of payments for interest rate subsidies and export rebates. If total outlays for amortisation payments are excluded, the growth rate of ordinary budget expenditure in 1987 drops to 23.4 per cent, against 18.9 per cent in 1986.

The faster growth of expenditure for interest payments was due to the continuous expansion of the outstanding public debt and to the increase in

TABLE V.4
OUTLAYS UNDER THE ORDINARY BUDGET AND THE PUBLIC INVESTMENT BUDGET
(In million drachmas)

	Annual magnitudes			Percentage changes	
	1985	1986	Provisional data 1987*	1986/85	Provisional data 1987/86
I. OUTLAYS UNDER THE ORDINARY BUDGET	1,497,277	1,823,299	2,372,939	21.8	30.1
1. Personnel outlays	570,329	668,703	782,000	17.2	16.9
2. Interest payments ³	235,265 ¹	279,818 ¹	411,611	26.6	38.2
3. Amortisation payments ³	44,846 ¹	95,909 ^{1 2 4}	242,161 ^{2 4}	113.9	152.5
4. Servicing of debt related to national defence	39,620	49,238	66,800	24.3	35.7
5. Payments to the European Communities	39,659	91,405	74,346	130.5	-18.7
6. Payment of revenue collected on behalf of third parties	75,713	83,635	81,200	10.5	-2.9
7. Tax refunds	37,125	45,828	66,000	23.4	44.0
8. Rebates on export financing costs	63,470	78,900	71,266	24.3	-9.7
9. Subsidies to farmers	91,727	93,271	107,243	1.7	15.0
10. Grants	165,063	184,534	292,000	11.8	58.2
11. Guarantees	2,203	823	30,562	-62.7	—
12. Other	132,257	133,235	147,700	0.7	10.9
II. OUTLAYS UNDER THE PUBLIC INVESTMENT BUDGET	274,197	309,835	315,000	13.0	1.7
1. Project implementation	217,002	229,096	221,090	5.6	-3.5
2. Grants	20,854	51,797	72,717	148.4	40.4
3. Administration expenditure	5,764	1,473	1,383	-74.4	-6.1
4. Interest payments ³	8,810	442	792	—	79.2
5. Amortisation payments ³	21,767	27,027	19,018	24.2	-29.6
III. TOTAL I+II	1,771,474	2,133,134	2,687,939	20.4	26.0

¹ Including outlays for servicing the 70 billion drachma loan of 1978 (5,254 million drachmas in 1985 and 5,172 million drachmas in 1986) granted by the Bank of Greece to the Greek State.

² Excluding outlays for the repayment of treasury bills held by the private sector, which are renewed virtually within the same time period.

³ Total outlays for public debt servicing are derived by summing up these two sets of figures.

⁴ Including redemption of treasury bills held by commercial banks (1986: 30.7 billion drachmas; 1987: 65.8 billion drachmas) and prepayment of interest and amortisation payments on the country's external debt (1986: 12.5 billion drachmas; 1987: 49.3 billion drachmas).

* Estimates based on data available up to 15 April 1988.

the average interest rate at which the Government borrows funds, owing to the increased share of domestic borrowing in the public debt through the

issue of treasury bills and government bonds carrying positive and rising real interest rates. By contrast, the decline of interest rates in the world money markets and the fall in the dollar rate had a contractionary effect on the growth of expenditure for interest payments on the public debt. Following the continuous increase in outlays for public debt servicing over the past five years, their share in total ordinary budget expenditure tripled in 1987 to 27.6 per cent, from 8.9 per cent in 1982. The high growth rate of expenditure for grants was mainly due to a large increase in transfers to IKA and public transport organisations for financing their deficits, as well as to Farmers' Insurance Organisation (FIO) in respect of revenue properly belonging to FIO but incorporated in VAT as from 1 January 1987 and collected by the State. Similarly, outlays relating to government guarantees forfeited grew considerably, following a decision of the Ministry of Finance to settle relevant liabilities of the Government to commercial banks and other credit institutions. Lastly, the large increase in tax refunds stemmed mainly from increased payments for the settlement of outstanding obligations in respect of stamp duties and turnover tax refunds. By contrast, a negative growth rate was recorded in payments of own resources to the EEC, which in 1986 had reached a high level owing to the miscalculation of Greece's contribution to the EC budget. Payments for interest rate subsidies and export rebates also decreased. This decrease stemmed from a gradual reduction as from 1 January 1987 of the percentages of interest refunds to exporters. These subsidies will be abolished by 1990. On the other hand, payments for interest rate subsidies under Law 128/1975 were affected by developments in outstanding bonds issued by specialised credit institutions and in special time deposits with commercial banks and the other credit institutions and recorded an increase, despite reductions as from late March in the respective interest rate subsidies. The expansion of outlays for subsidies to agriculture stemmed mainly from orientation and crop restructuring grants and from financial support to farmers whose crops were damaged by adverse weather conditions in March 1987. The growth rate of outlays for wages, salaries and pensions was roughly the same as in 1986, but 3 percentage points higher than the budget forecast. Lastly, the growth rate of the remaining categories of expenditure was contained at a low level, owing to a reduction in authorised disbursements out of budget appropriations, and to efforts aimed at a drastic curtailment of the Government's elastic expenditure.

Following its reduction by about 50 billion drachmas in mid-year (in order to contain the PSBR within the budget forecast), expenditure under the

public investment budget totalled 315 billion drachmas, against 310 billion drachmas in 1986. At constant prices, it was about 13 per cent lower than in 1986. This figure drops to 10 per cent if outlays for public debt servicing out of the public investment budget are deducted from total expenditure under that budget. A breakdown of expenditure shows that, as in the previous two years, special emphasis was placed on social undertakings (in the sectors of health, welfare and education). In addition, a considerable increase was recorded, both in terms of growth rate and as a percentage of total expenditure, in outlays in connection with the sector "industry-energy", owing to increased outlays for investment grants to the private sector, in the context of development Law 1262/1982, and for implementation of the programme of economic rehabilitation of ailing enterprises.

Expenditure under the public investment programme was financed in 1987 out of own revenue of 5 billion drachmas and EC grants totalling 35 billion drachmas, while the remainder was covered with borrowed funds.

Lastly, the overall government budget deficit, including the prepayment of external debt and the redemption of treasury bills held by commercial banks, amounted to 916 billion drachmas and was financed out of foreign borrowing (32 per cent) and the issue of government bonds (11 per cent), while the remainder was covered with proceeds from the sale of treasury bills.

b. Social Insurance Organisations

According to estimates of the General Secretariat of Public Enterprises and Organisations of the Ministry of National Economy and data given in the Report of the Minister of Finance on the 1988 budget, total expenditure of social insurance organisations amounted to 751 billion drachmas in 1987 against 611 billion drachmas in 1986, having increased by 22.9 per cent, against 25.5 per cent in 1986 (see Table V.5). After the deduction of receipts, the social insurance organisations ran a deficit of 275 billion drachmas (1986: 199 billion drachmas), of which 69 per cent stemmed from the operating account and 31 per cent from the capital account. This deficit was financed to the extent of 54 per cent with grants from the ordinary budget, the public investment programme and the EEC's Regional Development Fund, while the remainder was financed out of domestic borrowing. In particular, grants from the ordinary budget recorded a significant rise, owing to an increase in transfers to IKA from 7 billion drachmas in 1986 to 58 billion drachmas in 1987, and to FIO from 44

TABLE V.5
DEFICITS OF SOCIAL INSURANCE ORGANISATIONS^(a) AND THEIR FINANCING
(In million drachmas)

	Annual magnitudes			Percentage changes	
	1985	1986	1987*	1986/85	1987*/86
A. Management account					
1. Revenue	367,055	412,591	476,020	12.4	15.4
2. Expenditure	451,635	548,329	665,667	21.4	21.4
3. Result (1-2)	<u>-84,580</u>	<u>-135,738</u>	<u>-189,647</u>	<u>60.5</u>	<u>39.7</u>
B. Capital account					
4. Revenue	—	—	—	—	—
5. Expenditure	35,386	62,886	85,199	77.7	35.5
(Investment)	(8,182)	(8,214)	(13,688)	(0.4)	(66.6)
(Amortisation payments on loans)	(17,519)	(33,280)	(44,451)	(90.0)	(33.6)
(Repayment of credits)	(—)	(—)	(—)	(—)	(—)
(Other)	(9,685)	(21,392)	(27,060)	(120.9)	(26.5)
6. Result (4-5)	<u>-35,386</u>	<u>-62,886</u>	<u>-85,199</u>	<u>77.7</u>	<u>35.5</u>
TOTAL RESULT (3+6)	<u>-119,966</u>	<u>-198,624</u>	<u>-274,846</u>	<u>65.6</u>	<u>38.4</u>
FINANCING					
1. Grants	<u>41,413</u>	<u>62,565</u>	<u>148,629</u>	<u>51.1</u>	<u>137.6</u>
(Ordinary budget)	(38,493)	(54,031)	(140,797)	(40.4)	(160.6)
(Public investment programme)	(2,710)	(5,755)	(4,400)	(112.4)	(-23.5)
(European Regional Development Fund)	(210)	(2,779)	(3,432)	(—)	(23.5)
2. Depreciation	<u>212</u>	<u>217</u>	<u>208</u>	<u>2.4</u>	<u>-4.2</u>
3. Special resources	<u>10,411</u>	<u>4,885</u>	<u>—</u>	<u>-53.1</u>	<u>—</u>
4. New credits	<u>—</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>—</u>
5. Loans ^(b)	<u>67,930</u>	<u>130,957</u>	<u>126,009</u>	<u>92.8</u>	<u>-3.8</u>
TOTAL FINANCING	<u>119,966</u>	<u>198,624</u>	<u>274,846</u>	<u>65.6</u>	<u>38.4</u>

Source: Data from the General Secretariat on Public Enterprises and Public Organisations of the Ministry of National Economy and the Report of the Minister of Finance on the 1988 budget.

(a) Including 6 Social Insurance Organisations (IKA, FIO, MEA, Workers' Housing Organisation, Workers' Fund, and National Welfare Organisation).

(b) Gross domestic borrowing.

* Estimates.

billion drachmas in 1986 to 78 billion drachmas in 1987. This increase in transfers was the main reason for the drop in borrowing by social insurance organisations (1987: 126 billion drachmas; 1986: 131 billion drachmas).

Total receipts of social insurance organisations grew by 15.4 per cent in 1987, against 12.4 per cent in 1986. In particular, the receipts of IKA expanded by 24.9 per cent, compared with 14.1 per cent in the previous year. On the other hand, FIO's receipts fell from 72 billion drachmas in 1986 to 47 billion drachmas in 1987, as revenue it received from taxes was incorporated in VAT and replaced by transfers out of the ordinary budget. In 1987, 71 per cent of the total receipts of social insurance organisations was contributed by IKA, 10 per cent by FIO and 13 per cent by the Manpower Employment Agency (MEA). The operating expenditure of these organisations increased at the same rate as in 1986. This was due to a slowdown in the growth rate of FIO's expenditure (1987: 6.3 per cent; 1986: 13.6 per cent) and a faster growth rate of IKA's expenditure (1987: about 26 per cent; 1986: 24.4 per cent). The share of IKA in total expenditure of social insurance organisations was about 69 per cent, of FIO 19 per cent and of MEA 11 per cent. As a result of these developments in the receipts and expenditure of social insurance organisations, the deficit in their current operating account amounted to about 190 billion drachmas, compared with 136 billion drachmas in 1986. After the deduction of government transfers, the remaining deficit to be financed drops to 49 billion drachmas, against 82 billion in 1986.

Expenditure under the capital account grew by 35.5 per cent, compared with 77.7 per cent in 1986. This was due to a slower growth rate of IKA's amortisation payments (1987: 33.6 per cent; 1986: 90 per cent) and of other capital expenditure of IKA and of the Workers' Housing Organisation (1987: 26.5 per cent; 1986: 120.9 per cent). By contrast, investment expenditure expanded by 66.6 per cent in 1987, whereas in 1986 it had remained unchanged.

c. Public Enterprises

As Table V.6 shows, total expenditure of public enterprises amounted to 1,203 billion drachmas in 1987 (1986: 1,007 billion drachmas), having increased by 19.5 per cent, against 12.3 per cent in 1986. After the deduction of receipts, public enterprises ran a deficit of 426 billion drachmas (1986: 360 billion drachmas), of which 98 per cent stemmed from the capital account. This deficit was financed to the extent of 30.6 per cent with grants from the

TABLE V.6
DEFICITS OF PUBLIC ENTERPRISES^(a) AND THEIR FINANCING
(In million drachmas)

	Annual magnitudes			Percentage changes	
	1985	1986	1987*	1986/85	1987*/86
A. Operating account					
1. Revenue	539,991	646,161	776,973	19.7	20.2
2. Expenditure	606,833	701,340	784,843	15.6	11.9
3. Result (1-2)	<u>-66,842</u>	<u>-55,179</u>	<u>-7,870</u>	<u>-17.4</u>	<u>-85.7</u>
B. Capital account					
4. Revenue	—	—	—	—	—
5. Expenditure	289,851	305,359	418,555	5.4	37.1
(Investment)	(211,075)	(218,418)	(212,914)	(3.5)	(-2.5)
(Amortisation payments on loans)	(58,652)	(74,603)	(133,384)	(27.2)	(78.8)
(Repayment of credits)	(4,436)	(4,499)	(4,187)	(1.4)	(-6.9)
(Other)	(15,688)	(7,839)	(68,070)	(-50.0)	(768.4)
6. Result (4-5)	<u>-289,851</u>	<u>-305,359</u>	<u>-418,555</u>	<u>5.4</u>	<u>37.1</u>
TOTAL RESULT (3+6)	<u>-356,693</u>	<u>-360,538</u>	<u>-426,425</u>	<u>1.1</u>	<u>18.3</u>
FINANCING					
1. Grants	103,222	100,321	130,330	-2.8	29.9
(Ordinary budget)	(23,916)	(11,258)	(15,890)	(-52.9)	(41.1)
(Public investment programme)	(58,651)	(59,430)	(74,814)	(1.3)	(25.9)
(European Regional Development Fund)	(20,655)	(29,633)	(39,626)	(43.5)	(33.7)
2. Depreciation	37,618	55,972	58,490	48.8	4.5
3. Special resources ^(b)	38,140	37,635	37,941	-1.3	0.8
4. New credits	16,920	24,445	6,125	44.5	-74.9
5. Loans ^(c)	160,793	142,165	193,539	-11.6	36.1
TOTAL FINANCING	<u>356,693</u>	<u>360,538</u>	<u>426,425</u>	<u>1.1</u>	<u>18.3</u>

Source: Data from the General Secretariat on Public Organisations and Public Enterprises of the Ministry of National Economy, and the Report of the Minister of Finance on the 1988 budget.

(a) Including 45 public enterprises mentioned in the Report of the Minister of Finance on the 1988 budget, p. 119.

(b) Special resources include advances by PPC consumers, lump sum payments by HTO subscribers, participation of individuals in Water Supply and Sewerage Company projects, reserves of PPC's Personnel Pension Fund, and own assets (from surpluses) of certain public enterprises.

(c) Gross borrowing (domestic + foreign).

* Estimates.

ordinary budget, the public investment programme and the EEC's Regional Development Fund, 13.7 per cent through depreciation allowances, 8.9 per cent out of special receipts, and 1.4 per cent out of suppliers' credit, while the remaining 45.4 per cent represents the overall borrowing requirements of public enterprises and was financed with domestic and foreign loans. Unlike gross borrowing requirements, which increased considerably, net borrowing requirements decreased by 7 billion drachmas or 11 per cent.

Operating revenue expanded at a slightly faster rate than in 1986. About 60 per cent of this revenue came from six public enterprises: the Public Power Corporation (PPC), the Hellenic Telecommunications Organisation (HTO), the Hellenic Railways Organisation (HRO), the Hellenic Post Office (HPO), the Urban Transport Organisation (UTO), and the Water Supply and Sewerage Company (WSSC). The services provided by these enterprises are included in the special price index compiled by the National Statistical Service of Greece (NSSG) for goods and services. In 1987, this index recorded average increases ranging between 3.4 per cent for WSSG and 26.7 per cent for HPO. These rates of increase were lower than in 1986 and had a negative impact on the growth rate of receipts of the latter two enterprises. The adverse effect, however, on total revenue was offset by a faster rate of increase in the revenue of the other public enterprises. By contrast, the growth rate of operating expenditure slowed down significantly, dropping to 11.9 per cent compared with 15.6 per cent in 1986. This was mainly due to the strict incomes policy pursued and to the overall policy of containing the expenditure and improving the productivity of public enterprises. It was also due, however, to a decrease in the growth rate of outlays for interest payments from 19.7 per cent in 1986 to 15.7 per cent in 1987. Thus, in 1987 the operating revenue of public enterprises increased at a rate that was almost twice as fast as that of operating expenditure. As a result, their operating deficit fell to about 8 billion drachmas, against 55 billion drachmas in 1986. This decline was the outcome mainly of increased surpluses of PPC and HTO, as well as of smaller deficits run by Olympic Airways (OA) and HPO. If operating results are made to include grants out of the ordinary budget to finance current expenditure, the deficit in 1987 changes into a surplus of 8 billion drachmas, compared with a deficit of 44 billion drachmas in 1986.

Expenditure on capital account expanded by 37.1 per cent, compared with 5.4 per cent in 1986, exclusively owing to a steep rise in amortisation payments on loans and to a large increase in "other capital expenditure" (relating mainly to working capital employed), while investment expenditure

decreased slightly. This decrease stemmed from 14 public enterprises, which reduced their total investment expenditure by about 30 billion drachmas, whereas the other public enterprises increased their investment spending by about 25 billion drachmas. Among the public enterprises that reduced their investment outlays were the Aspropyrgos Oil Refineries (by 13 billion drachmas), the State Oil Prospecting Company (by 8 billion drachmas) and OA (by 5 billion drachmas). These reductions were mainly due to the fact that some major investment projects, such as the catalytic cracking plant and other modernisation works at the Aspropyrgos Oil Refineries (AOR), are nearing completion. In 1987, six public enterprises accounted for about 80 per cent of total investment outlays of the 45 public enterprises, namely: PPC, HTO, AOR, HRO, National Roadbuilding Fund, and School Buildings Organisation.

3. THE OVERALL GOVERNMENT BUDGET FOR 1988

The rates of increase in revenue and expenditure under the overall government budget for 1988 are expected to lead to a deficit larger than that in 1987, as the latter is reckoned on the basis of provisional data and estimates. The increase in the deficit would have been larger if the growth rate of total appropriations had not been contained at a level about 6 percentage points lower than the expected growth rate of revenue, despite an increase of about 125 billion drachmas in transfers from the ordinary budget to IKA and public transport organisations for financing their deficits, and grants to local authorities.

Revenue under the ordinary budget is expected to increase at a rate higher than both that in 1987 and the expected growth rate of national income at current prices in 1988. This increase will stem mainly from an expected broadening of the tax base, as a result of a more effective application of tax legislation and of the reform of income taxation, and from a speeding up of the settlement of tax cases pending from previous fiscal years. Moreover, revenue will be favourably affected by an increase in the taxation on tobacco, by the special tax surcharge on corporate profits earned in 1986, and by a more effective application of VAT, on the basis of the experience gained in the first year after its introduction and of amendments made to it.

In particular, according to budget forecasts, the large increase in revenue from direct taxes will stem from personal and corporate income tax, the special tax surcharge on corporate profits, and tax arrears. As regards revenue from indirect taxes, a large increase is expected in receipts from VAT, mainly

as regards domestic goods and services, taxation on tobacco, capital transfer tax and indirect tax arrears. Non-tax revenue, excluding refunds in 1987 and 1988 of uncalled for payments to the EC in 1986, is expected to increase by about 20 per cent. Lastly, the significant increase in revenue under the public investment budget is expected to stem almost exclusively from increased grants from the EEC, mainly the Regional Development Fund and the Inte-

TABLE V.7
REVENUE, EXPENDITURE AND DEFICIT
UNDER THE OVERALL GOVERNMENT BUDGET
(In million drachmas)

	1986	1987*	Budgeted 1988	Percentage changes		
				1986/85	1987/86	1988/87
Revenue	1,682,839	1,977,326	2,464,500	35.4	17.5	24.6
1. Ordinary budget	1,457,901	1,732,000	2,145,000	31.2	18.8	23.8
- Direct taxes	(386,691)	(444,000)	(616,440)	(27.7)	(14.8)	(38.8)
- Indirect taxes	(971,786)	(1,163,000)	(1,392,830)	(34.6)	(19.7)	(19.8)
- Other revenue	(99,424)	(125,000)	(135,730)	(16.0)	(25.7)	(8.6)
2. SAGAP	187,991	205,326	250,000	55.6	9.2	21.8
3. Public investment budget	36,947	40,000	69,500	225.6	8.3	73.8
Expenditure	2,321,125	2,893,265	3,421,530	22.7	24.6	18.3
1. Ordinary budget ²	1,823,299 ¹	2,372,939	2,801,530	21.8	30.1	18.1
2. SAGAP	187,991	205,326	250,000	55.6	9.2	21.8
3. Public investment budget	309,835	315,000	370,000	13.0	1.7	17.5
Deficit	638,286	915,939	957,030	-1.7	43.5	4.5
1. Ordinary budget	365,398	640,939	656,530	-5.4	75.4	2.4
2. SAGAP	—	—	—	—	—	—
3. Public investment budget	272,888	275,000	300,500	3.8	0.8	9.3

(a) Including outlays of 5,172 million drachmas for servicing the 70 billion drachma loan of 1978 granted by the Bank of Greece to the Greek State.

(b) Excluding outlays for the repayment of treasury bills held by the private sector, which are renewed virtually within the same period.

* Estimates based on data available up to 15 April 1988

grated Mediterranean Programmes. The large increase forecast in grants from the Integrated Mediterranean Programmes will also be due to deferred payments of 1987 grants.

In view of the forecast growth rates of the two basic categories of tax revenue, it is expected that, despite lower direct tax rates, the ratio

of direct to indirect taxes will improve compared with the previous two years.

Budget appropriations, on the basis of their estimated final level for 1987, will increase by 18.1 per cent, compared with a 30.1 per cent growth of expenditure in 1987. Specifically, ordinary budget expenditure is forecast to receive an expansionary influence from a large increase in grants, mainly to

TABLE V.8
FINANCIAL ACCOUNT OF GREECE WITH THE EUROPEAN COMMUNITIES
(In million drachmas)

	Annual magnitudes			Percentage changes	
	1986	1987	Budgeted 1988	1987/86	1988/87
<i>A. Receipts from the European Communities</i>	<i>273,601</i>	<i>318,980</i>	<i>391,000</i>	<i>16.6</i>	<i>22.6</i>
1. Flat rate (10%) repayment of expenditure incurred in collecting Communities' own resources	1,734	1,018	3,200	-41.3	214.3
2. Social Fund	10,247	20,383	23,000	98.9	12.8
3. EAGGF—Guidance Department	17,281	13,333	18,500	-22.9	38.7
4. Integrated Mediterranean Programmes	1,357	10,702	25,500	—	—
5. Regional Fund	50,507	47,134	55,000	-6.7	16.7
6. EAGGF—Guarantees Department	187,871	204,765	250,000	9.0	22.1
7. Other interventions	3,640	—	5,000	—	—
8. Other receipts	657	1,051	1,000	60.0	-4.8
9. Food aid	120	561	—	—	—
10. Refund of uncalled for payments made in 1986	187	20,033	9,800	—	-51.1
<i>B. Payments to the European Communities</i>	<i>91,460</i>	<i>74,700</i>	<i>80,000</i>	<i>-18.3</i>	<i>7.1</i>
1. Agricultural levies and duties	3,207	2,978	3,700	-18.3	24.2
2. Sugar levies	2,360	1,970	3,200	-7.1	62.4
3. Customs duties under the Common External Tariffs provision	11,730	14,373	15,500	22.5	7.8
4. Contribution on the basis of revenue from VAT	68,771	53,232	52,000	-22.6	-2.3
5. Other contributions	3,080	—	2,000	—	—
6. Financing of the Community Budget deficit with contributions which are to be repaid	1,072	600	500	-44.0	-16.7
7. Contributions other than to the Community Budget	1,240	1,547	3,100	24.8	100.4
<i>Net receipts from the European Communities (A - B)</i>	<i>182,141</i>	<i>244,280</i>	<i>311,000</i>	<i>34.2</i>	<i>27.3</i>

IKA and public transport organisations for financing their deficits, and to local authorities. A similar effect will be exerted on expenditure by increased outlays for tax refunds, especially of VAT refunds to farmers and exporters, as well as for income tax refunds in respect of tax-exempt amounts of rent paid

by wage earners, salaried employees and pensioners. Lastly, an increase is forecast in appropriations for payments of interest on the public debt and for servicing the armed forces' debt.

Expenditure under the public investment budget, which remained unchanged in 1987, is forecast to increase at a rate higher than the predicted rate of inflation.

The overall government budget deficit is expected to amount to 957 billion drachmas, of which 200 billion drachmas will be financed from foreign sources and the remainder from domestic sources. It should be noted that in 1988 the sale of treasury bills and medium-term bonds to the non-bank public will be a significant source of funds for financing the government budget deficit.

Lastly, net transfers from the EEC are expected to increase by 27.3 per cent and total 311 billion drachmas. The increase in these transfers amounts to 77 billion drachmas or 34 per cent, if the refund in 1987 and 1988 of an uncalled for payment in 1986 to the European Communities is not included. The increase in net transfers will stem mainly from larger receipts of the public investment budget from the Community's Funds, as well as from increased receipts from EAGGF-Guarantees Department for the payment of agricultural subsidies. It should be noted, however, that the increase in receipts from EAGGF is partly due to a change, in the last months of 1987, in the system of payment of EEC agricultural subsidies. As a result of this change, the respective amount for 1987 is reckoned on a ten-month basis.

APPENDIX TO CHAPTER V

TAX POLICY MEASURES

Law 1731/1987 "re: arrangements in direct and indirect taxation and other provisions" made some changes in taxation, and Minister of Finance decisions were issued to cope with certain problems that arose during the first year of application of VAT.

The principal changes in personal income taxation as regards income earned in 1987 were the following:

a) A new tax scale was introduced under which the tax burden on incomes earned by wage earners, salaried employees and pensioners is reduced.

b) The 300,000 drachma ceiling on the 50 per cent reduction of declared incomes from wages and salaries was raised to 340,000 drachmas.

c) A rent subsidy (negative tax) was introduced for wage earners, salaried employees and pensioners, as an alternative to the currently applicable deduction from their income for the same purpose.

d) The amounts of tax credit for the children of invalids and for the fourth child and beyond were increased.

The same law provides for increased amounts of imputed income of professionals, as follows: for taxable persons running personal firms, from 450,000 drachmas to 550,000 drachmas, and for taxable persons pursuing liberal professions, from 550,000 and 450,000 drachmas to 700,000 and 550,000 drachmas respectively. The amounts set for expenditure indicators (for income assessment purposes) were raised to higher levels, and at the same time expenditure indicators were extended to farmers in respect of ownership of private passenger cars of more than 10 taxable horsepower, pleasure craft, etc. Furthermore, for gross rental income from dwellings an additional deduction was granted for repairs, maintenance etc. (on the basis of receipts for the purchase of materials and services).

The above law also provides for an optional adjustment of the value of mechanical equipment of enterprises keeping class C accounting books, and the resulting excess value is made exempt from taxation to the extent it is paralleled by investment in new mechanical equipment.

As regards corporate income taxation, the same law provides for a reduction in the tax rate on retained profits from 49 per cent to 44 per cent for domestic industrial, handicraft, mining and quarrying firms. Moreover, in case the shares of the above firms are dealt in on the stock exchange, or the firms have been brought under Law 1262/1982 as from 1 January 1987

because they carried out productive investment projects worth more than 50 million drachmas, or the firms had been brought under the above law up to 31 December 1986, irrespective of the amount spent for productive investment, the tax rate on retained profits is reduced to 39 per cent.

As regards capital taxation, Law 1731/1987 stipulates:

a) In the case of real property transfer tax, the additional tax-exempt amount for the purchase of a first dwelling is raised from 800,000 drachmas to 1,000,000 drachmas for each of the purchaser's first three children.

b) In the case of real property tax, the tax-exempt amounts for natural and legal persons were raised from 30 and 25 million drachmas to 40 and 35 million drachmas respectively; if both spouses own real estate, the tax-exempt amount was set at 35 million drachmas for the spouse owning real estate of higher value and at 15 million drachmas for the other spouse.

The increased tax-exempt amounts will be in force as from fiscal 1988. In addition, by a Minister of Finance decision the State-determined starting-off prices of real estate were increased as from 5 January 1987, and the system of objectively determined real estate value was extended to other areas of the country.

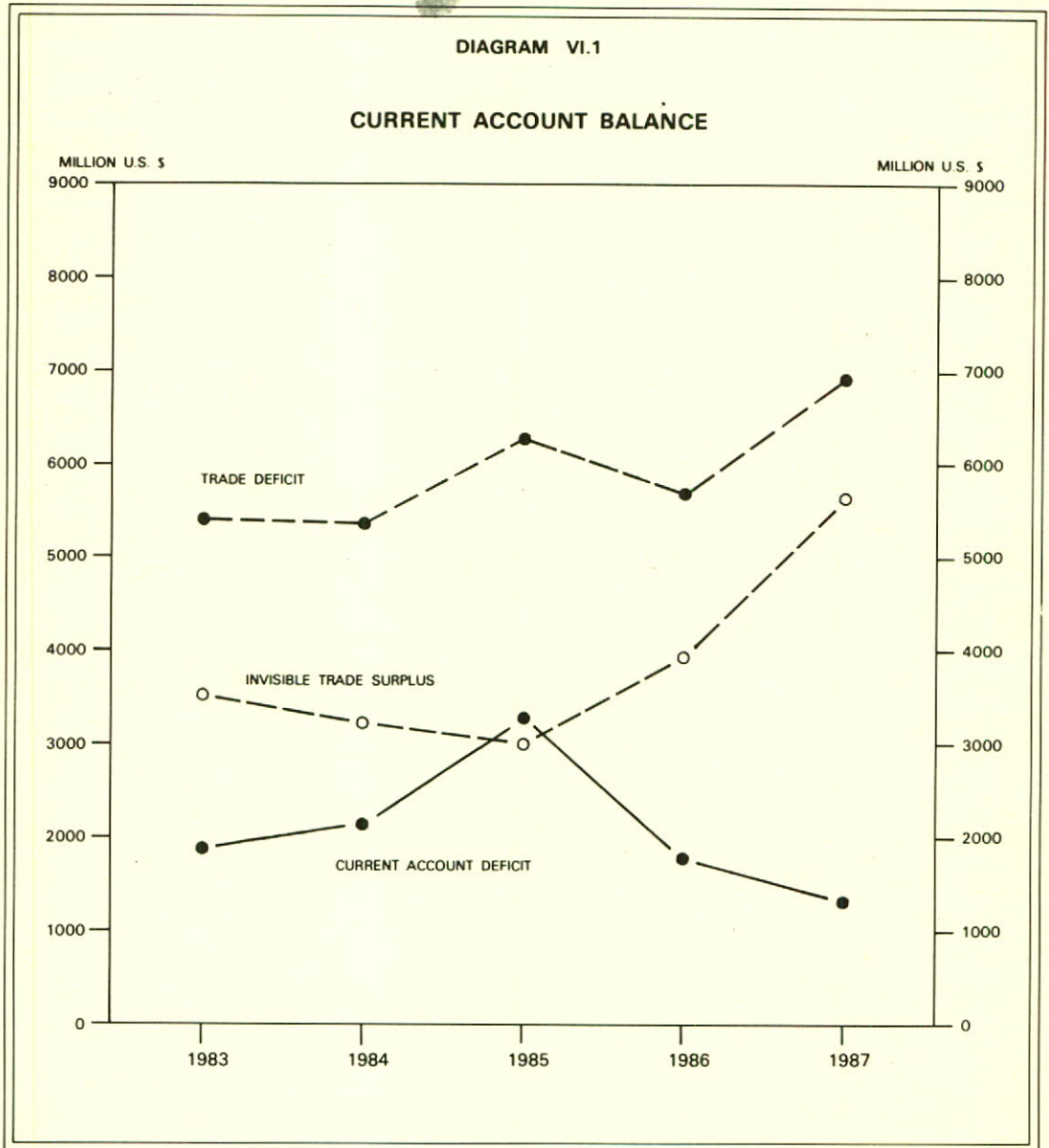
With regard to indirect taxation, the same law set tax refund rates for farmers at 3.5 per cent, 2 per cent and 1 per cent for livestock, farming and forestry-fishing activities respectively. These rates will be the basis for calculating refunds of the VAT which burdens inputs for the above activities. In addition, the amounts of the special liquid fuel consumption tax were adjusted.

Pursuant to Minister of Finance decisions, practices and procedures were amended and supplemented, aiming at the improved application of VAT. The most important changes were the following: (i) some products (disinfectants, insecticides, etc.) and services were moved from the 18 per cent tax rate to the 6 per cent tax rate, while other products (photographic equipment for enlargement or reduction, motorcycles of up to 250 cc., etc.) were moved from the 36 per cent tax rate to the 18 per cent tax rate, (ii) description of the supporting documents required for exemption from VAT of exports and export-related services, as well as of transactions under special customs regimes; similarly, a method was established for refunds of VAT levied on the inputs of enterprises in the above cases, and (iii) deferment of the payment of VAT on purchases of mechanical equipment by enterprises.

Lastly, pursuant to the relevant agreement between Greece and the EEC, in 1987 the initial regulatory tax rates were reduced by another 20 percentage points.

VI. BALANCE OF PAYMENTS

The balance of payments showed a further substantial improvement in 1987, following that of the previous year. The current account deficit fell by 26.9 per



cent and was fully financed by increased net private capital inflow. The current account deficit decreased to \$1,296 million, compared with \$1,772 million and

\$3,276 million in 1986 and 1985 respectively. The improvement was more pronounced in the deficit to GDP ratio, which dropped to 2.7 per cent, against 4.5 per cent in 1986 and 9.8 per cent in 1985. Net private capital inflow, most of which represents non-debt creating capital, increased by 81.8 per cent, totalling \$1,525 million. The "errors and omissions" item was positive, reaching \$309 million, which implies that the reported figures on the current account and the net inflow of private capital underestimate the improvement observed in 1987. This improvement is more accurately reflected in the balance of payments (before official foreign borrowing), which left a surplus of \$538 million in 1987, compared with deficits of \$1,014 million and \$2,507 million in 1986 and 1985 respectively. This surplus was used to strengthen foreign exchange reserves, which were also boosted by net official borrowing of \$278 million in 1987 against \$1,257 million in 1986. The favourable developments in the balance of payments enabled gross official foreign borrowing to remain at the 1986 level, despite much larger amortisation payments (1986: \$958 million; 1987: \$1,997 million), which include \$430 million of prepayments of obligations maturing beyond 1987.

At the end of 1987, foreign exchange reserves totalled \$3,738 million, against \$2,360 million in 1986, having increased by \$1,378 million. Of this increase, an amount of \$559 million represents valuation differences of foreign exchange and gold.

Monetary and foreign exchange policies pursued in Greece contributed substantially to last year's significant improvement in the balance of payments. The gradual weakening of inflationary expectations and pressures, combined with the liberalisation of bank interest rates and the establishment of positive real interest rates, improved confidence in the economy and contributed to a slowdown in the rate of depreciation of the drachma. These developments made it unprofitable to withhold funds in foreign exchange, a fact which had a particularly strong impact on capital flight and was instrumental in starting the repatriation of funds. Foreign exchange inflows were favourably affected also by the gradual easing of exchange controls on invisible payments and capital movements. The restoration of confidence in the economy and the establishment of real interest rates comparable to those prevailing in foreign capital markets are considered to have exerted a particularly favourable influence on invisible transactions and private capital inflow.

Developments in the balance of payments were quite favourable in the second half of 1987, owing to both the seasonal pattern of invisible earnings and the monetary policy measures taken at the end of June. In the first half

of the year the current account deficit was slightly higher than in the same period of 1986 (1987: \$1,500 million; 1986: \$1,460 million) and was financed by net private capital inflow to the extent of 46 per cent, against 36 per cent in the same period of 1986. These developments, together with the positive "errors and omissions" item, led to a drop in the balance of payments deficit (before foreign borrowing) to \$667 million (1986: \$1,064 million). Although net official foreign borrowing was slightly less than in the corresponding period of the previous year (1987: \$917 million; 1986: \$948 million), it not only financed the deficit, but was also utilised to increase official reserves by \$247 million. Gross official foreign borrowing amounted to \$1,980 million (1986: \$1,323 million), owing to increased amortisation payments, a considerable part of which was accounted for by prepayments of obligations maturing beyond 1987. In the second half of the year, the current account left a surplus of \$205 million, net private capital inflow more than doubled and "errors and omissions" were positive (\$169 million). As a result of these developments, the balance of payments (before official foreign borrowing) left a surplus of \$1,205 million, against a surplus of \$50 million in the second half of 1986. Gross official foreign borrowing amounted to \$295 million, amortisation payments totalled \$934 million, and foreign exchange reserves rose by a further \$566 million.

1. CURRENT TRANSACTIONS

The improvement in the balance on current account by \$476 million in 1987 resulted from a \$1,733 million increase in the surplus on invisibles, which more than offset the \$1,257 million increase in the trade deficit. The surplus on invisibles financed 81 per cent of the trade deficit, which is the largest percentage in the last twenty years.

a. Visible Trade Balance

The widening of the trade deficit by 22.1 per cent was due to an increase in both the oil and the non-oil trade deficits by 42.4 per cent and 16.2 per cent respectively. The upsurge in the oil deficit resulted from an increase in both oil prices and volume for stockpiling.

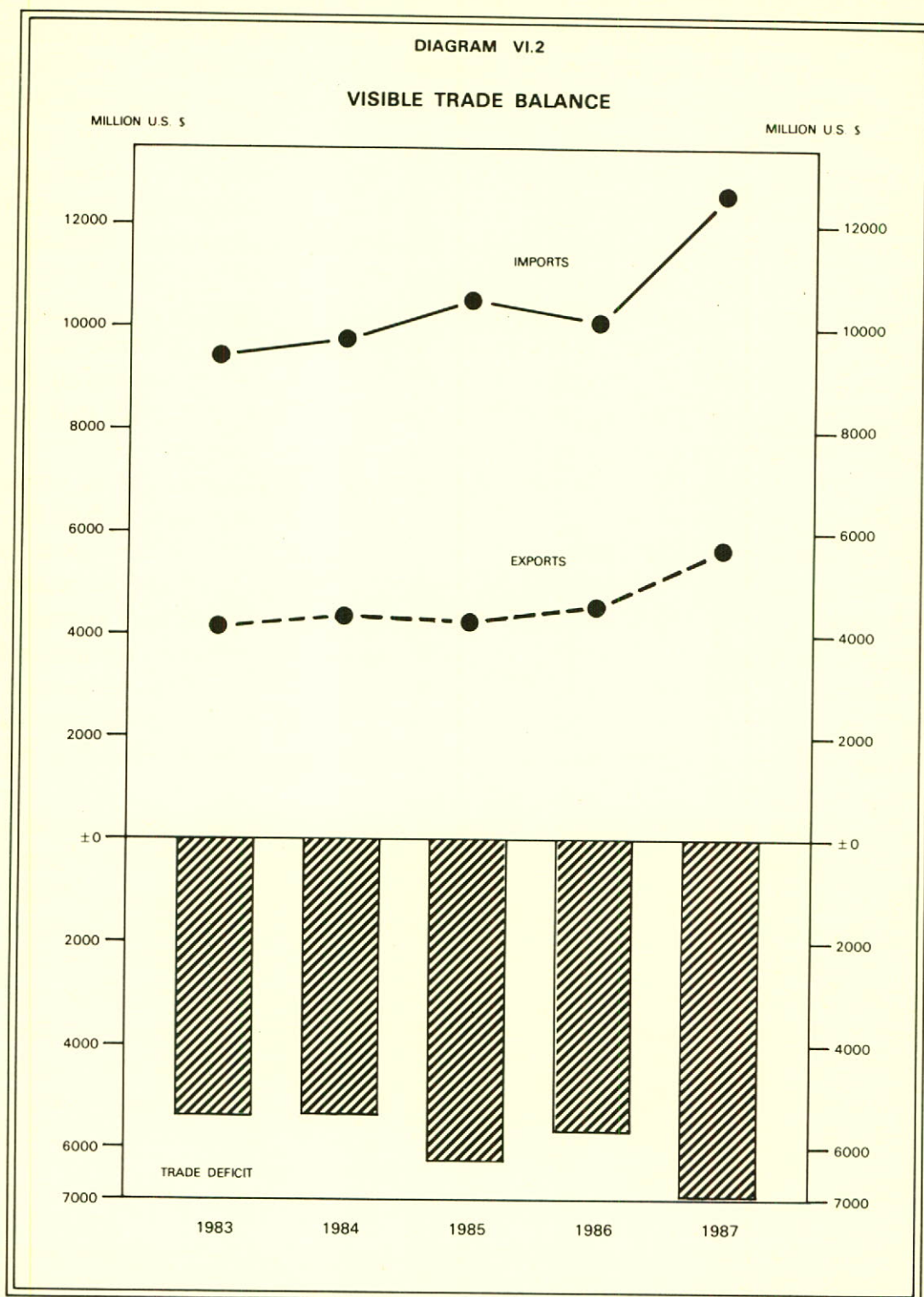
The widening of the non-oil trade deficit originated mainly from a further deterioration in the terms of trade. Given that merchandise export

TABLE VI.1
BALANCE OF PAYMENTS

Items	Million U.S. dollars			% change	
	1985	1986	1987	1986	1987
MERCHANDISE (cif) IMPORTS	10,561.1	10,198.3	12,556.1	- 3.4	23.1
Oil	3,188.1	1,786.5	2,360.2	-44.0	32.1
Non-oil	7,373.0	8,411.8	10,195.9	14.1	21.2
MERCHANDISE (fob) EXPORTS	4,293.2	4,512.5	5,613.6	5.1	24.4
Oil	833.8	511.7	544.4	-38.6	6.4
Non-oil	3,459.4	4,000.8	5,069.2	15.7	26.7
Visible Trade Balance	-6,267.9	-5,685.8	-6,942.5	- 9.3	22.1
INVISIBLE RECEIPTS	5,260.5	6,511.7	8,490.2	23.8	30.4
INVISIBLE PAYMENTS	2,268.3	2,598.0	2,843.3	14.5	9.4
Invisible Trade Balance	2,992.2	3,913.7	5,646.9	30.8	44.3
Current Account Balance	-3,275.7	-1,772.1	-1,295.6	-45.9	-26.9
Capital movement (net)	3,146.5	2,095.9	1,802.6	-33.4	-14.0
Private sector	910.7	944.6	1,641.9	3.7	73.8
Public sector	3,101.8	2,215.0	2,274.8	-28.6	2.7
Amortisation payments	-863.9	-1,063.7	-2,114.1	23.1	98.7
Allocation of SDRs	-2.1	—	—		
Errors and Omissions	-39.6	-80.9	309.2		
Revaluation of gold and foreign exchange holdings	767.2	350.0	558.9		
Overall Balance	598.4	592.9	1,375.1		
IMF	—	—	—		
Change in official reserves	631.0	625.8	1,378.2		
Change in clearing accounts	-32.6	-32.9	- 3.1		
Official reserves (end of period)	1,734.1	2,359.9	3,738.1		

* Gold reserves have been revalued at 65 per cent of the average buying market price per ounce of gold in U.S. dollars during December 1985, December 1986 and December 1987 respectively.

receipts correspond to less than 50 per cent of the import bill, exports should grow at least twice as fast as imports to keep the trade deficit from increas-



ing. Data on changes in the prices of imported and exported goods, on the basis of customs statistics, are available only for the January-September period¹. The special wholesale price indices calculated on the basis of cif and fob prices for imports and exports respectively, but using a different method for each index, provide some evidence that in 1987 dollar prices of non-oil imports increased by about 15 per cent and those of non-oil exports by about 11 per cent. These data, together with corresponding exchange record statistics, point to a faster growth of export volume compared with that of imports, and to a further deterioration in the terms of trade in 1987. It should be noted, however, that in the last months of the year, especially in December, the growth of export receipts accelerated, in anticipation of the abolition of export subsidies as from 1 January 1988. This implies that the increased export volume is overestimated.

As there are doubts about the reliability of the data available on prices of commodity exports and imports and in consequence of corresponding volume trends as well, no accurate conclusions can be drawn with respect to developments in the components of the trade balance. It should be noted, however, that the increase in the non-oil trade deficit seems to have stemmed from some transitory difficulties relating to the supply of certain agricultural products. An indication which supports this view is provided by the particularly large (48.9 per cent) widening of the deficit in the broad category of "food, beverages and tobacco", despite evidence of an improvement in the terms of trade for agricultural products.

As regards the basic determinants of the trade balance, foreign demand rose faster than domestic demand, while the competitiveness of Greek products is estimated to have recorded no significant change, despite the substantial decrease during 1987 in export subsidies (granted under Currency Committee Decision No 1574/1970 and Act No. 212/1983 of the Governor of the Bank of Greece) and in levies on imports (reduction in the regulatory tax, and abolition of advance import deposits). The adverse effects of these changes on the competitiveness of Greek products seem to have been largely, if not wholly, offset by developments in the real effective exchange rate index of the drachma. According to provisional data, this index, which is calculated

¹ These data show that in the January-September 1987 period dollar prices of non-oil merchandise imports and exports rose by 11 per cent and 13.4 per cent respectively. The volume of exports decreased by 6.7 per cent, while that of imports grew by 1.8 per cent.

on the basis of unit labour costs in the manufacturing sector and the wholesale price index, improved by about 3 per cent in 1987. This means that only if the reduction in the interest refund to exporters and in the levies on imports was passed entirely onto final prices, did the competitiveness of Greek products worsen slightly.

b. Exports

Commodity export receipts increased at a high rate (24.4 per cent) in 1987. In particular, earnings from exports of petroleum products grew by 6.4 per cent and non-oil commodity export earnings by 26.7 per cent. It should be pointed out again, however, that in December commodity export receipts recorded a very significant increase, which to a large extent can be attributed to a rush to beat the deadline set for the abolition of export subsidies (1 January 1988).

On the basis of the latest OECD data and estimates, foreign demand (volume of imports) in the principal markets for Greek products increased by 1 per cent in 1987, against 2 per cent in 1986. The slowdown of the growth rate occurred in all principal markets. Specifically, demand from EC member-countries for Greek products grew by 5.2 per cent (1986: 6.2 per cent) and from the USA by 4.2 per cent (1986: 10.4 per cent). On the other hand, demand from Eastern European and OPEC countries decreased at rates (3 per cent and 22 per cent respectively) quite close to those recorded in 1986. Different developments in foreign demand from individual markets affected the geographical distribution of Greek exports. EC countries absorb a continuously growing share of Greek exports, while the share of Greek exports to OPEC countries and Eastern Europe is declining.

Exchange record statistics show that the increase in earnings from non-oil commodity exports originated in all categories of exported goods. About three-fifths of this increase stemmed from the faster rise in exports of manufactured goods. Last December's rush in foreign exchange inflows may have affected developments in individual categories of products differently. With the exception of raw materials and semi-finished products, in all other categories of products the growth rate of export earnings rose faster in December than the average rate for the January-November period. This acceleration, however, and its concomitant effect on the respective annual growth rate, varied considerably between the various categories of exported goods. Of the basic categories of exported goods, the annual growth rate of earnings from

exports of manufactures was least affected (twelve months: 27.9 per cent; eleven months: 24 per cent), while the effect was most pronounced on mineral and ore exports (twelve months: 20.2 per cent; eleven months: 10.4 per cent). It is not possible to estimate, even approximately, what part of last December's acceleration in growth rates was due to a rush in foreign exchange inflows. For this reason, developments in earnings from individual export categories, and therefore in aggregate export earnings, should not be directly related to corresponding developments in the growth rate of exports on the basis of customs statistics.

Earnings from exports of food and beverages grew at a satisfactory rate (16.8 per cent). This rise was the result of dissimilar developments in earnings from individual products in this category. Earnings from exports of several of the main products in this category (currants, olives, olive oil, fresh fruit) remained unchanged or declined. In particular, exports of olive oil, which, owing to large volume, significantly affect developments in this category, decreased but nevertheless remained close to the high levels of the past few years. The imposition of negative monetary compensatory amounts as from November 1987 seems to have affected very little foreign exchange receipts in 1987, owing also to time lags between the shipment of goods and the actual inflow of the corresponding amount of foreign exchange. An increase was recorded in earnings from exports of cereals and preserved fruit. The apparently very large increase in cereal export receipts mostly reflects the fact that the corresponding figure for 1986 was very low because of problems in durum wheat sales.

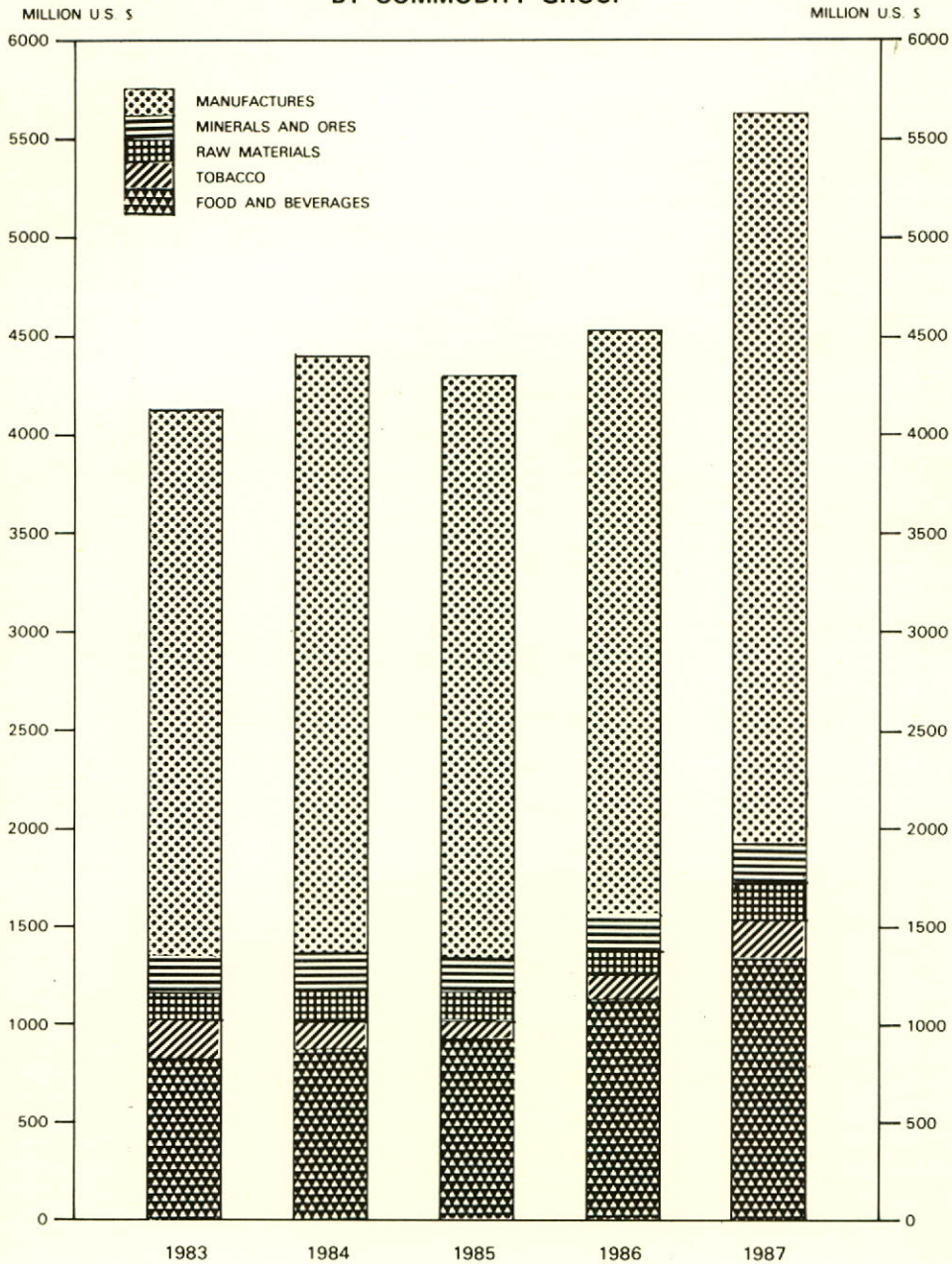
Of all categories of exported goods, the largest increase was recorded in earnings from tobacco exports, which more than doubled. This increase reflects a rise in both volume and prices. On the basis of National Tobacco Organisation data on shipments, however, in 1987 the volume of exports declined, while the average price rose substantially for the second consecutive year. The difference between the figures given for 1987 by the two sources of statistical data is due to the time lag between the shipment of goods and the actual inflow of the corresponding amount of foreign exchange. To a large extent, last year's increase in tobacco export proceeds reflects an increase in the volume of tobacco exports in 1986.

Earnings from exports of raw materials and semi-finished products grew at a very high rate (56.7 per cent), mainly owing to exports of cotton and hides and skins. The substantially larger cotton crop of 1986 made it possible both to meet domestic demand and to increase exports considerably.

TABLE VI.2
EXPORTS (fob)

Category	Million U.S. dollars			% change	
	1985	1986	1987	1986	1987
<u>I. FOOD AND BEVERAGES</u>	<u>918.3</u>	<u>1,149.3</u>	<u>1,341.9</u>	<u>25.2</u>	<u>16.8</u>
Currants	24.8	17.4	21.0	-29.8	20.7
Sultanas	50.0	56.7	38.3	13.4	-32.5
Olives	60.6	80.7	81.4	33.2	1.0
Olive oil	45.3	189.0	166.5	317.2	-12.0
Wines and spirits	56.5	63.9	75.5	13.1	18.2
Citrus fruit	64.3	88.8	62.8	38.1	-29.3
Other fresh fruit	81.2	124.9	123.9	53.8	- 1.0
Fruit and vegetables preserved	185.6	196.5	267.6	5.9	36.2
Cereals	121.5	55.5	167.1	-54.3	201.1
Other	228.5	275.9	337.8	20.7	22.4
<u>II. TOBACCO</u>	<u>103.7</u>	<u>110.8</u>	<u>228.1</u>	<u>6.8</u>	<u>105.9</u>
<u>III. RAW MATERIALS AND SEMI-FINISHED PRODUCTS</u>	<u>140.9</u>	<u>122.7</u>	<u>192.3</u>	<u>-12.9</u>	<u>56.7</u>
Cotton	60.7	34.8	90.1	-42.7	158.9
Hides and skins	45.8	35.1	55.9	-23.4	59.3
Other	34.4	52.8	46.3	53.5	-12.3
<u>IV. MINERALS AND ORES</u>	<u>214.1</u>	<u>173.5</u>	<u>208.5</u>	<u>-19.0</u>	<u>20.2</u>
Bauxite	47.2	36.7	24.1	-22.2	-34.3
Dead-burnt magnesite	22.0	21.4	15.3	- 2.7	-28.5
Other	144.9	115.4	169.1	-20.4	46.5
<u>V. PETROLEUM PRODUCTS</u>	<u>833.8</u>	<u>511.7</u>	<u>544.4</u>	<u>-38.6</u>	<u>6.4</u>
<u>VI. MANUFACTURES</u>	<u>1,919.2</u>	<u>2,250.8</u>	<u>2,879.0</u>	<u>17.3</u>	<u>27.9</u>
Textiles	731.3	984.6	1,278.5	34.6	29.8
Cement	150.9	139.1	143.2	- 7.8	2.9
Chemicals, pharmaceuticals	144.6	143.2	151.8	- 1.0	6.0
Aluminium and alumina	141.4	98.6	168.5	-30.3	70.9
Iron sheet	57.4	78.3	127.3	36.4	62.6
Metals and metal articles	185.0	209.6	268.6	13.3	28.1
Machinery and means of transport	43.3	40.5	52.4	- 6.5	29.4
Footwear, leather articles	54.4	61.6	72.3	13.2	17.4
Furs	77.5	123.4	172.9	59.2	40.1
Other	333.4	371.9	443.5	11.5	19.3
<u>VII. UNALLOCATED</u>	<u>163.1</u>	<u>193.7</u>	<u>219.3</u>	<u>18.8</u>	<u>13.2</u>
Total	4,293.1	4,512.5	5,613.5	5.1	24.4

DIAGRAM VI.3

COMPOSITION OF EXPORTS
BY COMMODITY GROUP

Export earnings from minerals and ores recorded a large increase (20.2 per cent). Developments, however, in individual products in this category varied considerably. Proceeds from exports of bauxite and dead-burnt magnesite decreased, while substantial growth was registered in those from marble and caustic magnesia, which have exhibited a steadily upward trend over the past few years.

Earnings from exports of manufactured goods expanded by 27.9 per cent. In particular, those from exports of textiles, which account for over 40 per cent of total proceeds from manufactures, grew at a high rate (29.8 per cent), due to an increase in both volume and prices. Increased exports contributed to a rise in the output of the textile industry, while manufacturing production as a whole fell in 1987. An even faster growth rate (40.1 per cent) was recorded in export receipts from furs, which seems to have been mainly due to higher prices. Large increases were recorded in export earnings from metal products, particularly aluminium, steel plate and other metals and metal articles. Cement export proceeds recorded a very small increase (2.9 per cent), which, however, took place in December. This suggests that it was due to a rush in the inflow of foreign exchange and not to a reversal of the downward trend observed in previous years, which reflected both a drop in demand from OPEC countries and keen international competition. Finally, export earnings from footwear and leather articles grew by 17.4 per cent. This increase seems to have been due to a rush in the inflow of foreign exchange and to higher prices.

c. Imports

Foreign exchange expenditure for non-oil commodity imports increased by 21.2 per cent in 1987. According to available indications, the prices of imported commodities rose at a lower rate. Hence, a substantial part of the increase in the commodity import bill was due to an increase in volume.

Exchange record statistics show that the increase in the non-oil import bill was due to all categories of products. The highest growth rate (31.5 per cent) was recorded, for the second consecutive year, in food imports. These large increases reflect, besides the permanent deficit in livestock products, the negative impact of exceptional factors, such as the Chernobyl nuclear accident and adverse weather conditions. Imports of dairy products increased again in 1987, though at a rate lower than the depreciation of the U.S. dollar against the ECU. Since the ECU prices of dairy products remained unchanged, these

developments denote a decrease in import volume. Import payments for cereals and flour grew at high rates, due to the persisting decline, below the level of domestic demand, of the soft wheat crop and to shortages created by very large maize exports. It is also worth noting that in 1987, as in 1985, a substantial amount (\$33 million) was allocated for sugar imports, since home production did not suffice to satisfy increased domestic demand.

A limited increase (7.8 per cent) was recorded in payments for imports of raw materials, as a result of the very small increase in payments for consumption materials (3.9 per cent) and of the 13.7 per cent increase in those for construction materials. As regards consumption materials, payments for cotton and fibres as well as wool fell, despite increased activity in the textile industry. Nevertheless, expenditure for cotton yarn and fabrics, included in the category "manufactured consumer goods", increased at a very high rate. Import payments for hides and skins fell, owing to reduced activity in the relevant home industry, while those for pulp and chemicals increased. Regarding construction material imports, there was a large increase in payments for timber, iron and steel, which was exclusively due to imports of crude iron and steel and was directly connected with higher exports of metallurgical products, since domestic construction activity showed a slight decline.

Expenditure for imports of capital goods increased by 14.8 per cent. Almost the entire increase stemmed from machinery imports, whereas imports of vehicles and electrical equipment registered only a slight increase. Machinery import expenditure rose by 17.5 per cent. This increase was exclusively due to higher imports of other than agricultural machinery and, according to some indications, was faster than that in prices. It should be noted that demand for capital goods is for the most part satisfied by imports, owing to insufficient home production.

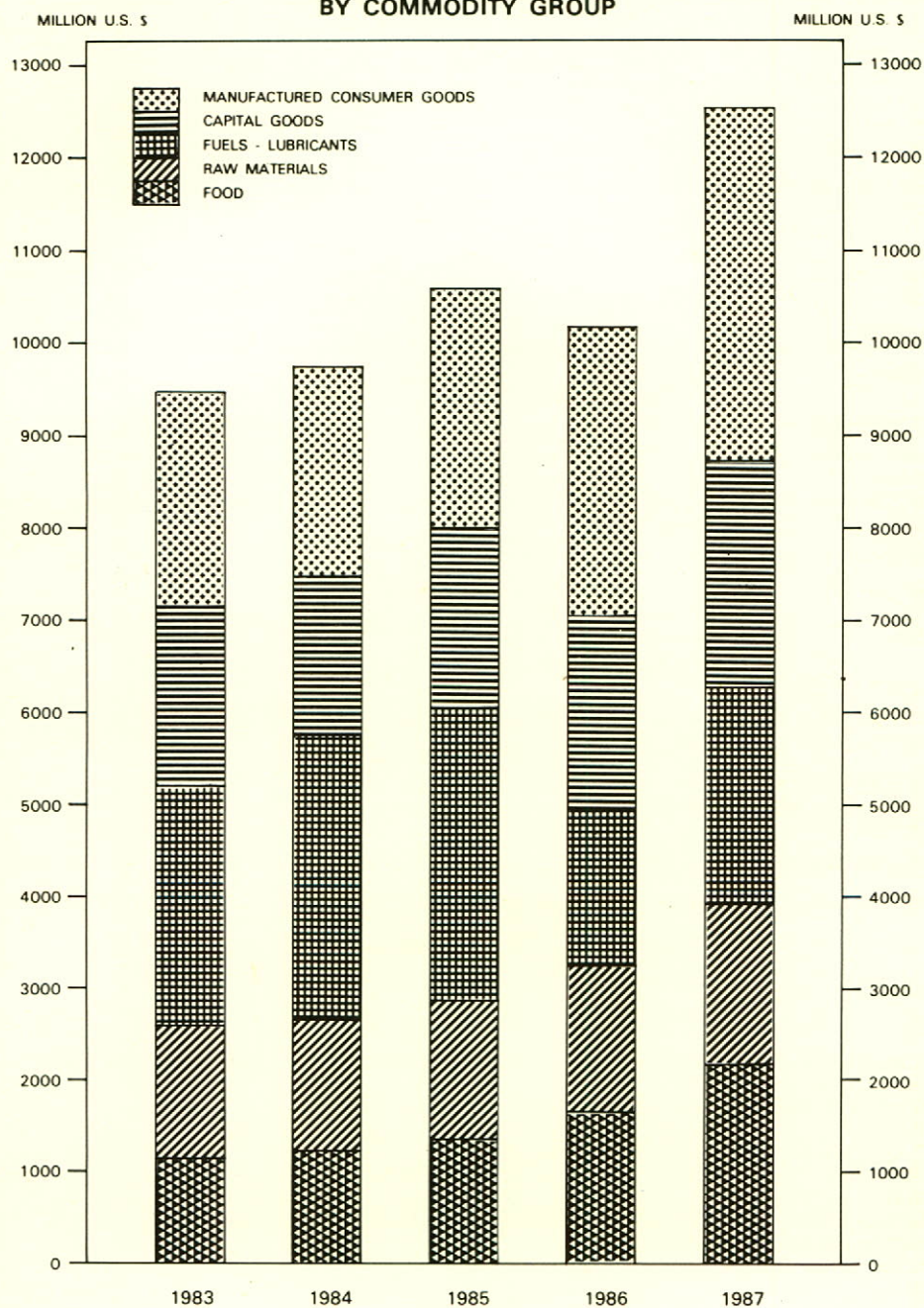
Expenditure for imports of manufactured consumer goods increased by 27.6 per cent. The rates of increase recorded in the three groups of products coming under this general category differ considerably. The largest increase occurred in the case of intermediate (semi-finished) products, which are imported for further processing by domestic industry, and the smallest in that of non-basic products. Though reliable information on price developments is not available, it seems that all three groups showed a considerable increase in import volume in 1987.

Payments for imports of intermediate manufactures rose by 34.5 per cent. Several intermediate goods imported for further processing by domestic industry are also included in the other two groups of manufactured consumer

TABLE VI.3
IMPORTS (cif)
(Payments and suppliers' credit)

Category	Million U.S. dollars			% change	
	1985	1986	1987	1986	1987
I. FOOD	1,305.5	1,655.2	2,176.0	22.6	31.5
1. Basic	1,133.0	1,381.3	1,775.7	21.9	28.6
Meat and live animals	503.0	611.7	739.8	21.6	20.9
Dairy products	230.6	299.6	338.5	29.9	13.0
Cereals and animal feed	81.7	124.4	260.9	52.3	109.7
Coffee	42.4	71.2	53.5	67.9	-24.9
Vegetable oils and seeds	74.8	78.0	107.4	4.3	37.7
Other	200.5	196.4	275.6	- 2.0	40.3
2. Non-basic	217.5	273.9	400.3	25.9	46.1
II. RAW MATERIALS	1,518.7	1,607.4	1,733.2	5.8	7.8
1. Consumption materials	906.7	958.6	995.6	5.7	3.9
Cotton and fibres	143.0	126.4	121.4	-11.6	- 3.9
Other chemicals	398.3	455.6	519.0	14.4	13.9
Raw minerals	64.9	54.8	32.4	-15.6	-40.9
Other	300.5	321.8	322.8	7.1	0.3
2. Construction materials	612.0	648.8	737.6	6.0	13.7
Iron and steel	405.6	435.5	494.0	7.4	13.4
Timber	103.3	118.8	138.9	15.0	16.9
Other	103.1	94.5	104.7	- 8.3	10.8
III. FUELS - LUBRICANTS	3,188.1	1,687.5	2,360.2	-47.1	39.9
1. Crude oil	1,988.7	1,032.9	1,660.5	-48.1	60.8
2. Other	1,199.4	654.6	699.7	-45.4	6.9
IV. CAPITAL GOODS	1,932.5	2,091.1	2,400.9	8.2	14.8
1. Machinery	1,434.1	1,589.0	1,867.2	10.8	17.5
2. Transport equipment	342.5	319.1	346.2	- 6.8	8.5
3. Electrical equipment	155.9	183.0	187.5	17.4	2.5
V. MANUFACTURED CONSUMER GOODS	2,530.3	3,014.8	3,846.8	19.1	27.6
1. Intermediate	312.9	367.3	493.9	17.4	34.5
2. Basic	832.2	973.7	1,241.5	17.0	27.5
Automobile parts and accessories	202.8	231.1	309.7	13.9	34.0
Paper and paper articles	127.7	148.9	173.1	16.6	16.3
Medical and pharmaceutical products	120.6	134.2	163.8	11.3	22.1
Other	381.1	459.5	594.9	20.6	29.5
3. Non-basic	1,385.2	1,673.8	2,111.4	20.8	26.1
Textiles	241.6	299.7	416.0	24.0	38.8
Electrical appliances	131.4	180.7	196.1	37.5	8.5
Passenger vehicles (other than buses)	209.8	191.0	249.7	- 9.0	30.7
Precious stones, metals, etc.	39.3	45.8	40.0	16.5	-12.7
Other	763.1	956.6	1,209.6	25.4	26.4
VI. FREIGHT (unallocated)	41.0	43.3	39.0	5.6	- 9.9
Total	10,561.1	10,099.3	12,556.1	- 4.4	-24.3

DIAGRAM VI.4
COMPOSITION OF IMPORTS
BY COMMODITY GROUP



goods. The rise in expenditure for intermediate goods resulted from all three groups of products in this category, which recorded similar growth rates. However, the largest increase (39.6 per cent) took place in yarn, chiefly cotton yarn, the import bill for which nearly doubled.

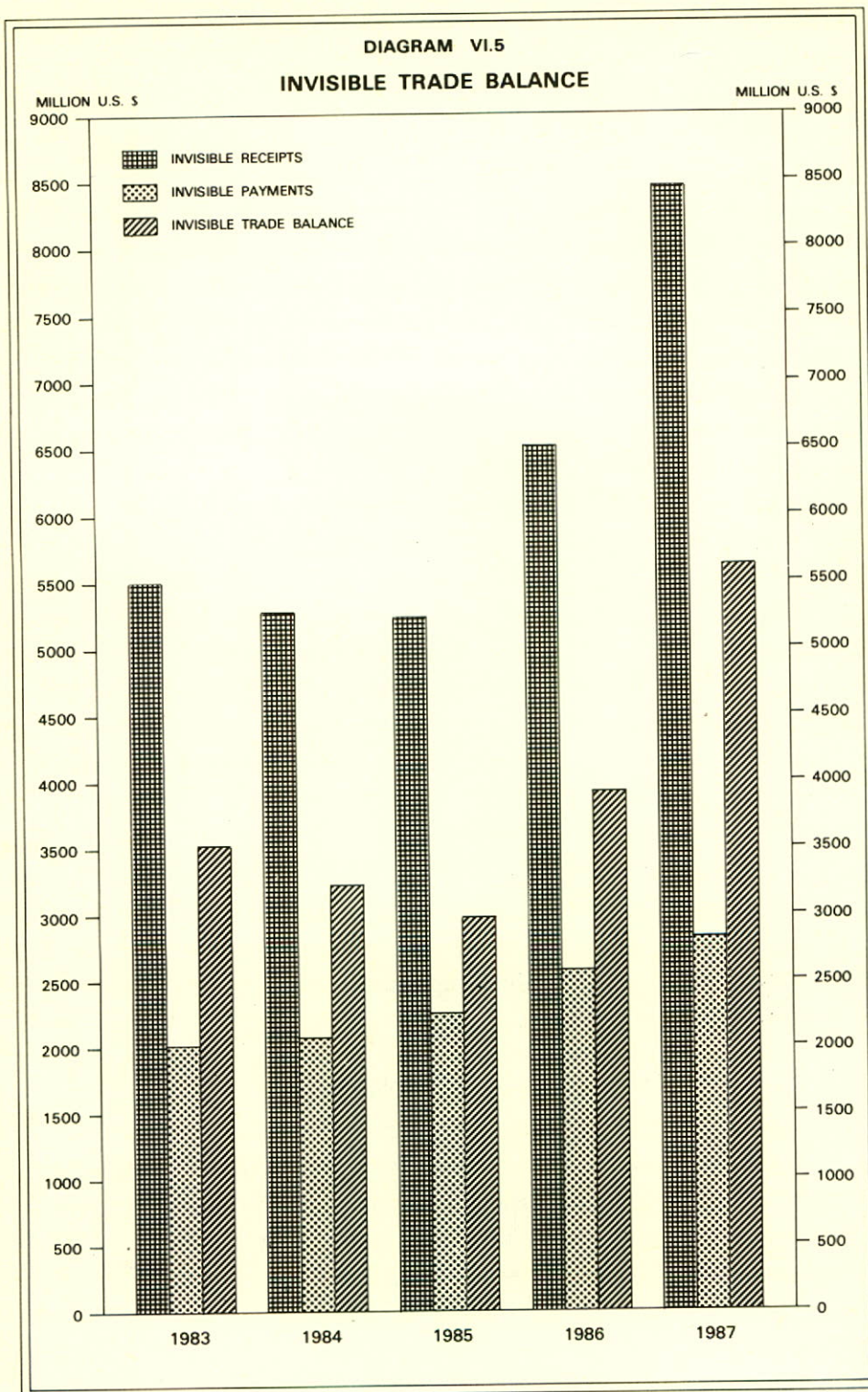
Payments for imports of basic consumer manufactures increased by 27.5 per cent. Among the main products in this group, high rates of growth were recorded in automobile parts and tyres, pharmaceuticals, and medical instruments and apparatus. Imports of automobile parts consist mainly of components for the local assembly of motor-cars.

Payments for non-basic consumer manufactures increased by 26.1 per cent. This increase spread over all individual products, though at different rates. Of the main products in this group, high rates of increase were recorded in household articles, textiles, plastic articles and private vehicles. Conversely, a limited increase, which did not cover price rises, was recorded in electrical appliances, glass articles and ceramics. The large increase (38.8 per cent) in expenditure for textile products stemmed from both fabrics and ready-made clothing. In particular, imports of ready-made clothing, following the fall in 1985, resumed their upward trend at a very fast pace in 1987. Lastly, the increase in payments for passenger vehicles at a rate substantially higher than the rate of increase in prices contrasts with the steep decline of sales in the home market.

d. Invisible Trade Balance

In 1987, the invisible trade surplus increased by \$1,733 million or 44.3 per cent (1986: \$922 million or 30.8 per cent), having totalled \$5,647 million against \$3,914 million in 1986. Thus the surplus on invisibles continued to rise for the second year running at an accelerating pace, reversing the downward trend observed since the early 1980s. It should be noted that the contribution of net transfers under the EC budget to the increase in the surplus was limited (16 per cent against 57 per cent in 1986). As a result, the increase in the invisible trade surplus, excluding transfers under the EC budget, was much larger.

The very large increase (44.3 per cent) in the surplus on invisibles was the result of the fast growth of receipts (30.4 per cent) and the limited growth of payments (9.4 per cent). The increase in invisible receipts and in the surplus on invisibles would have been larger, had it not been for the deferment of disbursements of agricultural subsidies by the EEC, owing to the liquidity problems faced by the Community. This situation led to the delay of pay-



ments by the EEC of the November and December subsidies, estimated at over \$300 million.

The faster increase in invisible receipts than in invisible payments led to a large expansion of the surplus on invisibles, since invisible receipts are more than double the amount of payments. Favourable developments in the invisible trade balance were substantially enhanced by the restoration of a climate of confidence regarding the stabilisation of the economy, as well as by the establishment of positive real interest rates. As a result, foreign exchange "leakages", prominent in invisible transactions, were extensively curtailed. This can be seen in the rapid increase in invisible receipts, excluding transfers under the EC budget, as well as in the standstill in invisible payments (excluding interest payments), which do not seem to be justified by developments in the basic determinants of these flows.

As regards developments in individual categories of invisible receipts, the following should be noted:

The increase by 19.6 per cent in transfers under the EC budget was almost entirely due to the depreciation of the dollar. In ECU terms, the increase is limited to 2.9 per cent. Yet not even this small increase represents actual growth, because in 1987 an amount of about 130 million ECUs, representing payments made by Greece in 1986 following the devaluation of the drachma in October 1985, was refunded. If this transaction is taken into consideration, net transfers in ECUs in 1987 show a significant decrease which, however, was due to the two-month deferment of disbursements of agricultural subsidies.

The steep increase in invisible receipts, excluding transfers under the EC budget, is only partly explained by developments in economic activity abroad, the rebound in world shipping and the competitiveness of Greek services. As previously mentioned, a significant part of this increase should be attributed to the monetary and foreign exchange policies pursued, particularly in the second half of 1987.

"Withdrawals out of convertible drachma deposits" and "other invisible receipts" registered very large increases of 90.3 and 30.7 per cent respectively. The first category includes remittances made on behalf of foreign firms for the payment of exports of goods and services invoiced in drachmas. The second category includes many items of invisible receipts whose precise nature is not clear. This means that the large increases in these two categories, particularly in withdrawals out of convertible drachma deposits, substantially increase the usual lack of precision associated with the analysis of developments in the

basic items of invisible receipts. This lack of precision seems to be greater in the case of foreign exchange earnings from tourism and shipping, since contracts between Greek hoteliers and foreign tour operators, as well as the collective labour agreements of Greek seamen, are drawn up in drachmas. It should be noted here that the increase in foreign exchange earnings from shipping, as shown by official data, grossly underestimates the contribution of shipping to the balance of payments and its direct contribution to national income. The indirect contribution of shipping to national income is considerably greater, in view of the fact that the balance of payments is the main

TABLE VI.4
INVISIBLE TRADE

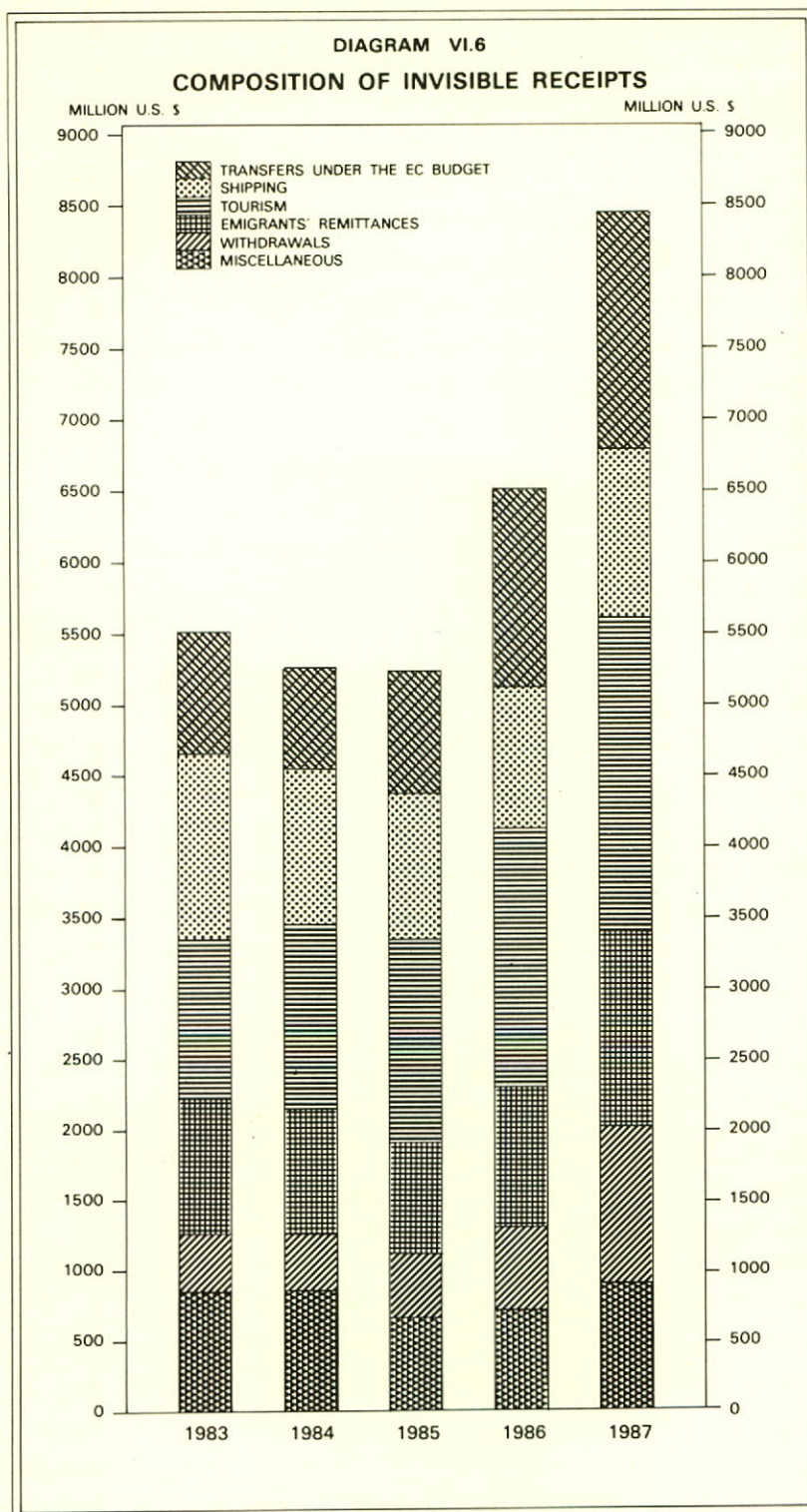
	Million U.S. dollars			% change	
	1985	1986	1987	1986	1987
INVISIBLE RECEIPTS					
1. Travel	1,428.0	1,834.2	2,191.7	28.4	19.5
2. Transportation	1,038.5	1,000.9	1,193.1	- 3.6	19.2
3. Emigrants' Remittances	800.7	983.2	1,378.8	22.8	40.2
4. Interest-Dividends-Profits	121.3	81.9	111.4	-32.5	36.0
5. Withdrawals out of convertible drachma deposits	451.0	596.5	1,135.4	32.3	90.3
6. Other	551.9	623.0	814.3	12.9	30.7
7. EEC Transfers	869.1	1,392.0	1,665.5	60.2	19.6
Total	5,260.5	6,511.7	8,490.2	23.8	30.4
INVISIBLE PAYMENTS					
1. Travel	367.5	494.2	507.5	34.5	2.7
2. Transportation	204.9	195.7	231.0	- 4.5	18.0
3. Interest-Dividends-Profits	1,237.1	1,353.6	1,536.9	9.4	13.5
4. Official Services	119.9	141.5	152.1	18.0	7.5
5. Other	338.9	413.0	415.8	21.9	0.7
Total	2,268.3	2,598.0	2,843.3	14.5	9.4
INVISIBLE TRADE BALANCE	2,992.2	3,913.7	5,646.9	30.8	44.3

constraint on the conduct of economic policy. For a proper assessment of the contribution of shipping to the balance of payments and national income, it should be taken into account that shipping is essentially an offshore economic activity. Consequently, the supply of shipping services in the international market does not require imports of goods and services. Lastly, it should be stressed that a significant part of private capital inflow, which cannot be estimated, however, seems to originate in the shipping sector.

Foreign exchange earnings from tourism increased by 19.5 per cent in 1987. This increase underestimates actual developments, since a part of earnings from tourist services is recorded under withdrawals out of convertible drachma deposits. According to estimates of the National Tourist Organisation of Greece, tourist arrivals increased by 7.6 per cent while consumer prices as well as the prices agreed upon between Greek hoteliers and foreign tour operators showed increases, in dollar terms, of 20.5 per cent and over 35 per cent respectively. These data, combined with the overall reduction of foreign exchange leakages, show that in 1987 there probably occurred a decrease in per capita expenditure, at constant prices, even after taking into account a substantial part of the increase in withdrawals out of convertible drachma deposits. This could be attributed to the worsening, in terms of income level, of the composition of tourist arrivals, a fact which is supported by the considerably lower occupancy rates in superior class hotels in certain areas during the peak season.

For the first time since 1981, foreign exchange earnings from shipping increased (19.2 per cent). This increase reflects chiefly the recovery of all basic sectors of the freight market, particularly that of dry cargo, where the greater part of the Greek-owned fleet trades. This is illustrated by the estimated 43 per cent rise in the Baltic Freight Index on average for 1987. Favourable developments in international freight markets were the combined result of a reduction in the world merchant fleet, owing to a decrease in new shipbuildings, and of increased demand from several sources, such as transport of cereals for the USSR and of iron ores and oil.

The recovery of the freight market was accompanied by a considerable increase in the active Greek-owned fleet, which stemmed exclusively from ships under flags of convenience, whereas the active fleet under the Greek flag decreased. The growth of the active Greek-owned fleet had no significant impact on the number of Greek seamen in employment, which seems to have remained at the level of 1986. Conversely, on the basis of the pay increases of seamen employed on ocean-going vessels and the adjustment of contributions to the Greek Seamen's Pension Fund (NAT), it is estimated that total pay and contributions to NAT by Greek seamen (in dollars) increased by 25 to 30 per cent. The increase in the Greek-owned merchant fleet must have favourably influenced all shipping service activities in Greece, such as ship stores and ship repairs as well as employment in the offices of shipping firms. Furthermore, a large increase (40 per cent) was recorded in cruise passenger arrivals, which shows that there was a significant recovery in this sector too.



The particularly large increase (40.2 per cent) in emigrants' remittances was almost equally due to increased remittances from abroad and to withdrawals in drachmas out of foreign exchange deposits. A part of the increase was due to the depreciation of the US dollar against European currencies, particularly the Deutschemark. The larger part of the increase is only partly explained by developments in the relevant economic indicators (employment and disposable income) in the host countries of Greek emigrants. A substantial part of the increase in these remittances should be attributed to the restoration of a climate of confidence and to the establishment of positive real interest rates in Greece, which limited capital flight and were instrumental in starting the repatriation of capital. Furthermore, the establishment of competitive rates of return on drachma investments had a favourable impact on the inflow of savings from abroad.

The rise by 9.4 per cent in invisible payments was chiefly due to the increase (13.5 per cent) in payments of interest, dividends and profits. Other items in invisible payments recorded a limited increase (5 per cent). The increase in payments of interest, dividends and profits was almost exclusively due to higher (13.9 per cent) interest payments by the public sector (1985: \$1,385 million; 1986: \$1,216 million). The depreciation of the dollar against the other currencies in which a part of Greece's foreign borrowing is denominated explains nearly the entire increase, since the external debt, in constant dollars, increased only slightly, while interest rates in international money markets in 1987 showed only marginal changes compared with 1986. On the other hand, interest payments by the private sector remained unchanged (1987: \$112 million; 1986: \$113 million).

Of the other categories of invisible payments, a considerable increase (18 per cent) was recorded in payments for transportation, as a result of the recovery of the international freight market. Lastly, payments for travel remained almost unchanged (an increase of only 2.7 per cent), despite the rise in the tourist currency allowance and the liberalisation of the greater part of payments for travel abroad.

2. CAPITAL MOVEMENT

The gross inflow of private capital increased by 73.8 per cent to \$1,642 million against \$945 million in 1986. Most of the increase resulted from the rise in non-debt creating capital inflow.

Specifically, the gross inflow of non-debt creating private capital (entrepreneurial capital, capital intended for real estate investment, deposits

TABLE VI.5
FINANCING OF THE CURRENT ACCOUNT DEFICIT

	Million U.S. dollars		
	1985	1986	1987
BALANCE ON CURRENT ACCOUNT	-3,275.7	-1,772.1	-1,295.6
Private capital	808.7	838.6	1,524.6
Venture capital	289.7	300.6	391.5
Real estate investment	430.9	462.7	674.9
Commercial banks	186.3	-47.4	-63.2
Deposits with credit institutions	76.8	286.4	440.0
(Deposits by Greeks living abroad)	(85.2)	(301.9)	(377.0)
Suppliers' credit (net) ¹	-40.8	-33.8	221.3
Other	-32.2	-23.9	-22.6
Amortisation	-102.0	-106.0	-117.3
Errors and omissions	-39.6	-80.9	309.2
BALANCE OF PAYMENTS BEFORE CENTRAL BANK AND PUBLIC SECTOR BORROWING	-2,506.6	-1,014.4	538.2
Revaluation of gold and foreign exchange holdings	767.2	350.0	558.9
Central Bank and Public Sector Borrowing	2,339.9	1,257.3	278.0
Central Bank	1,970.1	749.2	868.4
Government	167.9	910.4	1,017.0
Public entities	916.4	557.8	404.4
(of which: PPC)	(442.7)	(310.0)	(232.6)
Suppliers' credit (net) ¹	47.4	-2.4	-15.0
Amortisation	-761.9	-957.7	-1,996.8
Allocation of SDRs	-2.1	—	—
OVERALL BALANCE	598.4	592.9	1,375.1
IMF	-	-	-
Change in foreign exchange reserves*	631.0	625.8	1,378.2
Change in clearing accounts	-32.6	-32.9	-3.1

¹ Suppliers' credit (to the public and private sector):

a. Short-term	48.4	50.1	282.8 ²
b. Long-term	-41.8	-86.3	-76.5 ²

² Provisional data.

* Gold reserves have been revalued at 65 per cent of the average buying market price per ounce of gold in U.S. dollars during December 1985, December 1986 and December 1987 respectively.

in foreign exchange and "other" capital) totalled \$1,484 million in 1987, compared with \$1,026 million in 1986 (an increase of 44.6 per cent). On the

other hand, private sector foreign borrowing (i.e. foreign borrowing by commercial banks and suppliers' credit) showed a net inflow of \$158 million against a net outflow of \$81 million in 1986. The net inflow in 1987 was entirely due to increased suppliers' credit, whereas foreign borrowing by commercial banks showed a net outflow of \$63 million compared with \$47 million in 1986. After the deduction of amortisation payments of the private sector (\$117 million), the resulting net inflow of private capital in 1987 totalled \$1,525 million, fully covering the current account deficit (in 1986 it had covered only 47 per cent of this deficit).

The substantially increased private capital inflow should be attributed to the strengthening of expectations for a further improvement of the economic climate at home, in combination with the measures taken to liberalise capital movement. Furthermore, the establishment of positive interest rates at home, together with the foreign exchange policy pursued, have limited capital flight and started the repatriation of capital.

Developments in individual categories of private capital flows in 1987 were as follows:

Following the stagnation witnessed in the last quarter of 1986 and the decline in the first quarter of 1987, entrepreneurial capital inflow accelerated substantially, reaching \$392 million for the whole of 1987 against \$301 million in 1986, having thus risen by 30.2 per cent against 3.8 per cent in 1986. This significant increase should be attributed to the favourable impact of the measures taken to liberalise capital movement, the enhanced profitability of firms and, generally, the improved economic climate.

The substantial increase in new official approvals in 1987 for foreign direct investments is related to this increase in entrepreneurial capital inflow. Specifically, 142 applications were approved in 1987 (compared with 51 for 1986) totalling \$199 million, compared with \$109 million in 1986. Of the sums approved for 1987, 26 per cent related to capital for investing in oil refineries, 36 per cent in the non-oil manufacturing sector, 31 per cent in tourist enterprises and 7 per cent in commercial banks and other sectors of activity.

In 1987 the increase in the inflow of capital for real estate investment continued at an accelerated pace. This growth trend had originally appeared in mid-1986, following the announcement of the first measures liberalising capital movement. The rate of growth of this category of capital inflow rose from 15.8 per cent in the second half of 1986 to 36.3 per cent in the first half of 1987 and to 52.4 per cent in the second half of the same year. Thus, for the

whole of 1987 the inflow of capital for real estate investment grew by 45.9 per cent to \$675 million (1986: \$463 million), which is the peak figure recorded for this item. The increase in 1987 stemmed mainly from the direct inflow of foreign exchange (\$462 million against \$317 million in 1986) but also from withdrawals in drachmas out of foreign exchange deposits under the Housing Loan Deposit Scheme (1987: \$213 million; 1986: \$146 million).

The net inflow of deposits in foreign exchange (new deposits minus withdrawals in drachmas and foreign currency) continued to rise in 1987, reaching \$440 million against \$286 million in 1986 (an increase of 53.8 per cent). More than 90 per cent of the net inflow of foreign exchange deposits stemmed from private deposits and the residual from the transfer of deposits in convertible drachmas. Specifically, the net inflow of private foreign exchange deposits totalled \$377 million against \$302 million in 1986. It should be noted that the net inflow of foreign exchange (new deposits minus withdrawals in foreign currency) through private deposit accounts grew from \$989 million in 1986 to \$1,332 million in 1987. As in previous years, the largest part of the net inflow of foreign exchange in this category, specifically \$955 million, was converted into drachmas.

A notable characteristic of developments in foreign exchange deposits, especially during the last two years, was the considerable increase in the inflow of deposits made by residents of Greece under Decision 232/83 of the Bank of Greece. In fact, the net inflow of these deposits (new deposits minus withdrawals in drachmas and foreign currency) grew from \$45 million in 1985 to \$112 million in 1986 and \$195 million in 1987. Specifically, the net inflow of foreign exchange (new deposits minus withdrawals in foreign currency) totalled \$288 million in 1987 against \$156 million in 1986.

As regards the above increase in foreign exchange deposits, it should be noted that it was partly due to the depreciation of the dollar against other currencies. The breakdown by currency of private foreign exchange deposits shows that deposits in US dollars increased (1987: \$129 million; 1986: \$45 million), while the net change in DM deposits remained at the level of 1986 (1987: DM 237 million; 1986: DM 240 million). It is worth noting that this was due to an increase in DM deposits converted into drachmas and not to a drop in net inflows of foreign exchange, which increased in 1987 (1987: DM 803 million; 1986: DM 720 million). Deposits in currencies other than the US dollar and the Deutschmark developed similarly to DM deposits.

Suppliers' credit to the private sector showed a net increase (new acceptances minus repayments) of \$221 million in 1987, compared with a net

decrease of \$34 million in 1986. An analysis of credit by main category of imports shows that, with the exception of capital goods imports, all the other categories (food, raw materials, fuels and manufactured consumer goods) were financed with increased suppliers' credit. Specifically, credit for imports of manufactured consumer goods contributed nearly two-thirds of the total increase in suppliers' credit to the private sector.

TABLE VI.6
GREECE'S EXTERNAL DEBT¹
(Balance at year-end in million U.S. dollars)

	1985	1986	1987*
A. PUBLIC AND PUBLICLY GUARANTEED (1+2+3)	13,133.1	15,712.8	18,207.7
1. MEDIUM-AND-LONG-TERM	11,653.5	14,646.0	17,747.2
Central Government	927.1	1,991.0	3,453.4
Public enterprises	4,473.7	4,973.6	5,512.2
Bank of Greece	5,265.3	6,376.9	7,254.6
Other banks ²	881.8	1,217.5	1,463.6
Private enterprises ²	105.6	87.0	63.4
2. SHORT-TERM	1,249.1	838.7	247.5
Bank of Greece	914.4	497.2	106.5
Public enterprises	334.7	341.5	141.0
3. SUPPLIERS' CREDIT ³	230.5	228.1	213.0
B. PRIVATE FOREIGN DEBT (1+2)	2,396.4	2,318.9	2,499.0
1. Medium-and-long-term	1,044.4	1,000.7	959.5
2. Suppliers' credit ³	1,352.0	1,318.2	1,539.5
C. GRAND TOTAL (A+B)	15,529.5	18,031.7	20,706.7

¹ Refers to loans disbursed and not serviced in drachmas. Conversion of currencies to U.S. dollars has been effected at the parities valid at year-end. From the total increase of Greece's foreign debt (\$2,675 million in 1987), the largest part (89 per cent or \$2,383 million) was due to the change in foreign exchange parities.

² Refers to publicly guaranteed loans.

³ Short-term and long-term.

* Provisional estimates.

In 1987, owing to favourable developments in the balance of payments, foreign borrowing requirements decreased substantially. Net foreign borrowing by the public sector was limited to \$278 million (1986: \$1,257 million) and was used to strengthen foreign exchange reserves.

Gross foreign borrowing by the public sector increased from \$2,215 million in 1986 to \$2,275 million in 1987 (a rise of 2.7 per cent). Borrowing by the Bank of Greece on behalf of the State and direct borrowing by Central Government increased, whereas borrowing by public enterprises and organisations dropped from \$558 million in 1986 to \$404 million in 1987. Specifically, total borrowing by the Bank of Greece grew by 15.9 per cent (1987: \$868 million; 1986: \$749 million). Gross foreign borrowing by Central Government grew by 11.8 per cent (1987: \$1,017 million; 1986: \$910 million). This increase was due to the drawing down in 1987 of the second tranche (875 million ECUs) of the loan granted by the EEC to support the programme of economic stabilisation.

TABLE VI.7
INTEREST AND AMORTISATION PAYMENTS
(Million U.S. dollars)

	1985	1986	1987
INTEREST	1,221.9	1,329.2	1,496.5
Private sector	138.6	112.8	111.6
Public sector	1,083.3	1,216.4	1,384.9
AMORTISATION	863.9	1,063.7	2,114.1
Private sector	102.0	106.0	117.3
Public sector	761.9	957.7	1,996.8
TOTAL	2,085.8	2,392.9	3,610.6
Debt Service Ratio (DSR)			
D.S.R. I ¹	21.8	21.7	25.6
D.S.R. II ²	21.8	20.9	22.6

¹ Amortisation payments include advance payments.

² Not including amortisation advance payments.

Amortisation payments totalled \$2,114 million, against \$1,064 million in 1986. This increase stemmed almost exclusively from the public sector and was partly due to amortisation prepayments on loans maturing after 1987. Specifically, total amortisation payments on public sector loans grew by \$1,039 million (1987: \$1,997 million; 1986: \$958 million), which included \$430 million for amortisation prepayments. Total amortisation payments on the country's external debt reached \$3,611 million against \$2,393 million in

1986, corresponding to a debt-service ratio of 25.6 per cent, against 21.7 per cent in 1986. Net of amortisation prepayments, the debt-service ratios in 1987 and 1986 were 22.6 and 20.9 per cent respectively. Interest payments on foreign loans corresponded to 10.6 per cent of foreign exchange earnings from exports of goods and services in 1987, against 12.1 per cent in 1986.

Borrowing in 1987 had a limited expansionary effect on Greece's external debt. At constant US dollar parities, it would have remained on 31 December 1987 at nearly the same level as at the end of 1986 (around \$18 billion). However, owing to the depreciation of the dollar against the other currencies in which part of the external debt is denominated, the external debt of the public sector reached \$18.2 billion at the end of 1987, while the private sector's debt is estimated at \$2.5 billion. As a percentage of GDP, Greece's external debt (public and private) dropped from 45 per cent in 1986 to 41 per cent in 1987.

3. FOREIGN EXCHANGE DEVELOPMENTS

The main feature of foreign exchange developments in 1987 was the substantial slowdown in the rate of depreciation of the drachma. As shown in Table VI.8, the average level of the drachma's effective exchange rate index, as

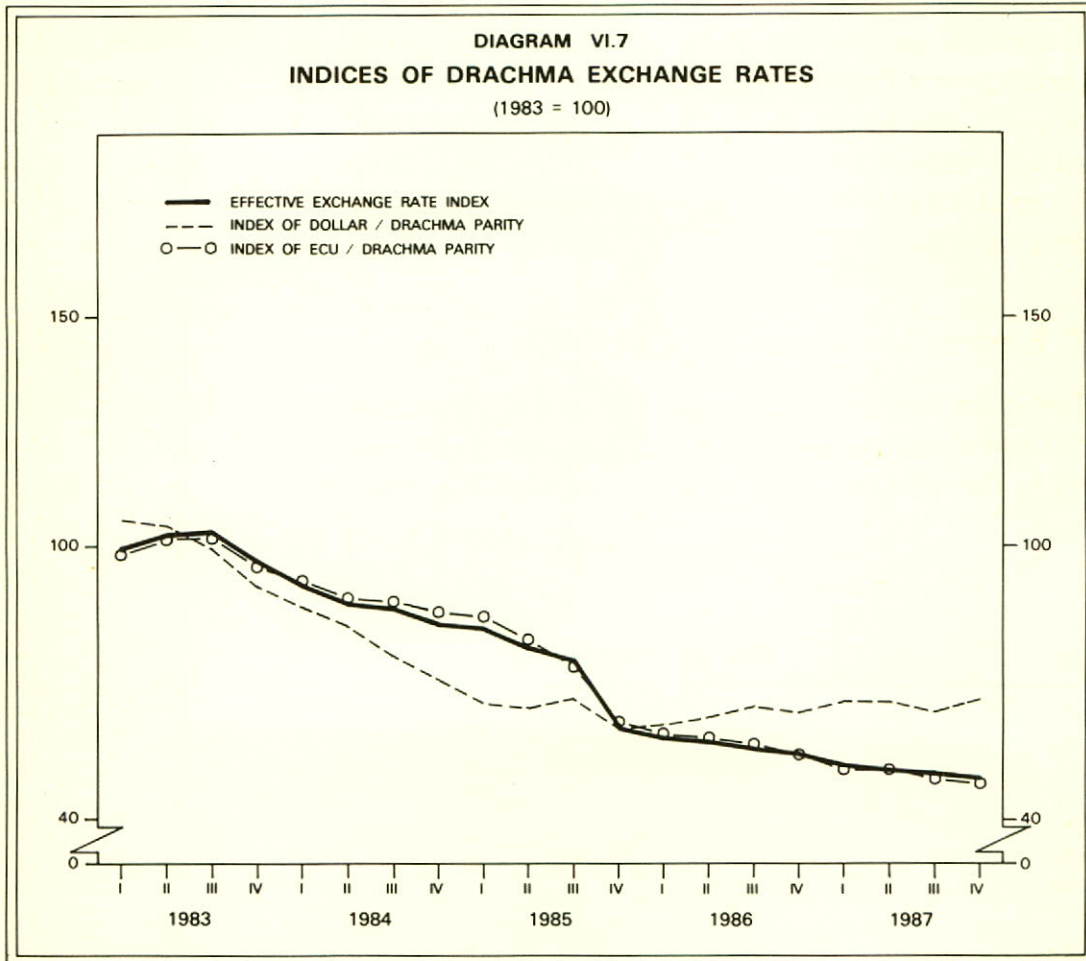
TABLE VI.8
FOREIGN EXCHANGE PARITY OF THE DRACHMA
(Per cent changes against previous period)

	Drachma against U.S. Dollar	Drachma against Deutschemark	Effective exchange rate ¹	Drachma against ECU
1983	-24.1	-20.5	-16.9	-16.4
1984	-21.9	-12.6	-11.5	-11.7
1985	-18.4	-16.6	-17.9	-16.3
1986	- 1.3	-26.5	-22.2	-23.1
1987	3.4	-14.3	-11.0	-12.0
1986 First quarter	2.9	- 6.3	- 3.9	- 4.1
Second quarter	2.5	- 1.9	- 1.5	- 1.3
Third quarter	3.7	- 3.8	- 2.3	- 2.1
Fourth quarter	- 1.5	- 5.3	- 3.6	- 3.9
1987 First quarter	2.8	- 5.7	- 4.0	- 5.0
Second quarter	0.1	- 1.7	- 2.1	- 2.1
Third quarter	- 3.7	- 2.0	- 2.0	- 2.0
Fourth quarter	4.5	- 3.1	- 2.2	- 2.7

¹ New revised index compiled by the Bank of Greece.

calculated by the Bank of Greece, fell by 11 per cent, which is the lowest rate in the last five years. Through the year, the drachma depreciated by 8.1 per cent, against 11.5 per cent in 1986.

Developments in the foreign exchange markets, particularly the large depreciation of the US dollar after October 1987, are reflected in the changes in the drachma's parity against individual currencies. Through the year, the



drachma depreciated by 9.9 per cent against the ECU and appreciated by 10.2 per cent against the US dollar. At average levels, the respective changes were 12 per cent and 3.4 per cent.

Table VI.8 shows the quarterly movements of the effective exchange rate of the drachma. According to this table, the index of the effective

exchange rate of the drachma fell by 4 per cent in the first quarter, but in the following quarters the drachma depreciated at nearly half the rate of the first quarter. The drachma-ECU parity moved in a similar way. The difference is that, during the first and the last quarters of the year, the drachma depreciated at a higher rate. Lastly, the drachma-dollar parity fluctuated sharply during 1987, largely reflecting a variation in the US dollar rate in international foreign exchange markets. Specifically, in the first quarter of 1987, the drachma appreciated by 2.8 per cent compared with the last quarter of 1986 and remained unchanged during the second quarter of 1987. In the third quarter, the drachma depreciated by 3.7 per cent, but appreciated at a high rate (4.5 per cent) in the last quarter of the year.

APPENDIX TO CHAPTER VI

MEASURES CONCERNING CAPITAL MOVEMENTS AND INVISIBLE TRADE

In 1987, the most important developments regarding the liberalisation of capital movements were: (i) The Bank of Greece permitted (Decision 1011/22 April 1987) borrowing in foreign currency by manufacturing, mining and hotel firms, without prior approval by the Bank of Greece. The funds must be borrowed for a period of at least six months and the proceeds of the loans can be used for financing investment and working capital needs; (ii) Presidential Decree 170/19 May 1986 was replaced by Presidential Decree 207/19 June 1987, which harmonised Greek law with EC directive 86/566. Also, Presidential Decree 207 regulates certain pending matters, such as the retroactive validity of provisions related to the liberalisation of capital movements between Greece and the EEC.

As with PD 170/19 May 1986, PD 207/19 June 1987 stipulates that liberalised transactions shall be verified for their legality and genuineness only, excluding *a priori* the verification of economic expediency. Responsibility for direct investment (establishment, export of profits, export of liquidation proceeds etc.) rests with the Ministry of National Economy. All other transactions are the responsibility of the Bank of Greece which, by means of directives/circulars, may authorise commercial banks to undertake the relevant foreign exchange operations.

In 1987 the Bank of Greece continued to issue decisions concerning the liberalisation of capital movements on the basis of PD 170/1986 and PD 207/1987.

These decisions are described in:

1. Circular 13/24 March 1987 concerning the acquisition by residents of Greece of securities denominated in foreign currencies, issued by the EC and the European Investment Bank.

2. Circular 37/19 November 1987 which specifies the procedure for the acquisition by EC and non-EC residents of securities dealt in on the Athens Stock Exchange, the repatriation of redemption or sale proceeds, and the export of income from such securities. This circular is a combination of Circular 30/11 September 1987 (acquisition by EC residents of securities dealt in on the Athens Stock Exchange) and of Bank of Greece Decision 1178/12 November 1987 (repatriation of capital imported from non-EC countries for the purchase of securities dealt in on the Athens Stock Exchange).

3. Circular 34/16 October 1987 instructing commercial banks to supply the required foreign exchange to EC residents for transferring abroad income accrued from real property in Greece.

4. Directive/Circular 1/23 November 1987 which specifies the details concerning the liberalisation of capital from inheritances belonging to EC residents. This directive/circular abolishes Bank of Greece Circular 19/6 May 1986 to the extent the latter concerns inheritances.

Besides the above decisions, the Bank of Greece issued in 1987 a series of other decisions related to capital movements in general. These are as follows:

1. Decision 1153/25 September 1987, (complementing Decision 1011/22 April 1987), which permits the use of loans in foreign exchange, contracted in accordance with the terms and conditions of Decision 1011, for (i) the settlement of previous obligations in foreign exchange; (ii) the purchase abroad of raw materials and mechanical equipment, and (iii) the payment of royalties on imported know-how.

2. Decision 1155/5 October 1987 which specifies, among other things, the procedure for the sale to residents and non-residents of government bonds in drachmas from the conversion of foreign exchange which does not have to be surrendered to the Bank of Greece. Bondholders are permitted to transfer abroad or deposit in a foreign exchange account in Greece the proceeds from the redemption or sale of these bonds.

Apart from the above decisions concerning capital movements, other decisions were also taken in 1987 related to invisible payments, the most important of which are:

1. Decision 1149/22 September 1987 by which the annual tourist currency allowance for travel to non-EC countries was increased to \$600. On 1 January 1987 the annual tourist currency allowance for travel to EC countries was raised from 760 ECUs to 800 ECUs and on 1 January 1988 to 840 ECUs.

2. Decision 1150/22 September 1987 which fixed at 10,000 drachmas the amount of Greek currency allowed to residents when leaving or entering the country. For non-residents the respective sums are 10,000 drachmas on leaving and 25,000 drachmas on entering. Non-residents and Greeks residing abroad are permitted, within a year from entry into Greece, to re-export the equivalent of USD 1,000 in foreign banknotes, not declared by holders at the time of import. Furthermore, individuals in this category are permitted to carry, when entering or leaving the country, traveller's cheques in their name,

regardless of whether they were declared when the holder came into Greece, without any ceiling or time limit as to re-export.

3. Decision 1151/22 September 1987 which liberalised the foreign exchange allowances to persons travelling abroad for commercial or professional reasons. Besides raising or abolishing ceilings on the foreign exchange allowed, it permitted travellers to use international corporate credit cards parallel to and without affecting the use of personal credit cards. Corporate credit cards have no limit with respect to expenses for hotel accommodation and meals.

BANK OF GREECE

60TH YEAR

GENERAL BALANCE SHEET

31st December 1987

(In drachmae)

A S S E T S		1 9 8 7		1 9 8 6		L I A B I L I T I E S		1 9 8 7		1 9 8 6
GOLD AND FOREIGN EXCHANGE*						SHARE CAPITAL		3,876,964,365.—		3,876,964,365.—
I. Bank's holdings		370,537,547,676.—		255,972,372,272.—		RESERVES				
II. Foreign exchange position with IMF		12,513,120,958.—		11,878,662,196.—		I. Regular reserve		3,876,964,365.—		3,876,964,365.—
III. Special Drawing Rights on IMF		6,167,578.—		1,530,662.—		II. Special reserve from the sale of shares above par		486,428,000.—		486,428,000.—
IV. ECU holdings		89,928,865,299.—		59,713,598,058.—		III. Provision according to Art. 71 of the Statutes		2,328,982,000.—		2,269,170,000.—
V. Sundry claims in foreign exchange		6,430,219,551.—	479,415,921,062.—	4,629,420,463.—	332,195,583,651.—	IV. Provision for foreign exchange risks		304,600,000.—		304,600,000.—
BALANCES UNDER BILATERAL TRADE AGREEMENTS			3,415,191,167.—		4,255,809,210.—	V. Other provisions		897,121,324.—	7,894,095,689.—	814,558,527.65
DEPOSITS WITH BANKS UNDER CURRENCY COMMITTEE DECISIONS			373,329,208,621.—		389,168,234,854.30	BANKNOTES IN CIRCULATION		669,069,522,000.—		571,375,031,250.—
COIN			874,107,872.—		439,094,148.45	LIABILITIES IN DRACHMAE				
DOMESTIC BILLS DISCOUNTED			66,259,838.—		84,919,796.—	I. Government Current Accounts				
LOANS AND ADVANCES						1. Government Departments accounts		3,955,770,344.—		696,022,050.35
I. To the Government						2. Public Investment accounts		2,141,854,376.—		640,226,839.40
1. Current Receipts & Payments account ..		258,036,031,280.—		209,897,837,103.45		3. Special accounts		1,614,087,230.—	7,711,711,950.—	775,512,314.55
2. Consumer Goods and Agricultural Products		—		98,030,701.—		II. Deposits				
3. Oil products		69,205,388,000.—		63,161,768,775.—		1. Banks		522,605,345,839.—		372,226,727,629.95
4. Treasury bills and government bonds ...		64,566,647,000.—		10,893,954,588.—		2. Advance deposit requirements on imports		164,447,129.—		85,677,962,530.—
5. Loans under special agreements						3. International institutions and foreign banks		59,006,154,981.—		69,642,093,540.95
a. Loans for membership in international financial institutions		95,937,857,762.—		82,021,361,432.55		4. Public entities		215,112,897,039.—		213,289,747,273.15
b. Long-term loans in drachmae		497,729,752,191.—		465,795,287,684.—		5. Other deposits		10,568,099,889.—		9,120,431,953.85
c. Long-term loans in foreign exchange .		1,012,929,679,602.—	1,998,405,355,835.—	985,966,467,206.—	1,817,834,707,490.—	6. Dividends for 1987		960,136,350.—	808,417,081,227.—	816,128,793,177.—
II. To Banks and Others						SHORT TERM LIABILITIES IN FOREIGN EXCHANGE		39,806,531,717.—		89,796,823,505.—
1. Advances		162,338,466,499.—		179,217,675,151.85		REDEPOSITS IN FOREIGN EXCHANGE BY COMMERCIAL BANKS		1,179,842,460,192.—		1,036,986,557,331.—
2. Advances out of public entity funds deposited with the Bank of Greece		123,211,249,862.—	285,549,716,361.—	131,775,378,703.—	310,993,053,854.85	LONG-TERM LOANS IN FOREIGN EXCHANGE ON BEHALF OF THE GREEK GOVERNMENT		999,541,255,356.—		974,593,369,491.—
INVESTMENTS			300,690,300.—		284,176,507.—	OTHER LONG-TERM LIABILITIES IN FOREIGN EXCHANGE		89,396,013,812.—		70,067,723,977.—
PREMISES AND EQUIPMENT						ALLOCATION OF SPECIAL DRAWING RIGHTS (IMF)		18,476,411,785.—		17,539,593,277.—
1. Land		3,209,296,463.—		6,221,891,281.35		OTHER LIABILITIES		71,902,696,123.—		64,097,843,224.45
2. Buildings and equipment		7,146,067,855.—		5,260,779,198.85	961,112,082.50					
Less depreciation:					2,563,863,777.90					
Up to 1986		5,250,850,654.—			301,034,144.—					
In 1987		287,293,387.—	5,538,144,041.—	1,607,923,814.—	4,817,220,277.—					
VALUE OF BANKNOTE PRINTING MATERIALS		2,952,731,782.—								
Less depreciation		396,931,100.—	2,555,800,682.—		2,262,829,633.90					
FOREIGN EXCHANGE VALUATION DIFFERENCES, Law 1083/1980 (art. 8, para.1)			673,926,789,196.—		604,558,700,674.65					
OTHER ASSETS			73,278,483,005.—		122,801,855,442.65					
* The Bank's holdings in gold and foreign currency on 31st December 1987 have been calculated on the basis of the drachma/dollar parity effective on that date (Dr. 126.53 per \$1).			3,895,934,744,216.—		3,589,048,271,495.30			3,895,934,744,216.—		3,589,048,271,495.30
The value of gold holdings has been calculated on the basis of \$316.34 per ounce (65 per cent of average purchase price per ounce in \$, December 1987).										

PROFIT AND LOSS ACCOUNT

D E B I T		1 9 8 7		1 9 8 6		C R E D I T		1 9 8 7		1 9 8 6
Personnel Remuneration - Pensions:						Interest, commission and other earnings		17,659,074,127.—		17,134,266,867.25
Wages and salaries		6,863,182,136.—		6,487,960,311.—						
Principal and supplementary pensions		4,014,772,025.—	10,877,954,161.—	3,771,475,837.—	10,259,436,148.—					
Contributions to Personnel Insurance Funds:										
Pension Fund		1,686,124,978.—		1,441,466,811.—						
Supplementary Pension Fund		666,766,924.—		690,245,468.—						
Self-insurance Fund		250,635,894.—		222,741,073.—						
Health Insurance Fund		440,024,399.—	3,043,552,195.—	406,781,319.—	2,761,234,671.—					
Contributions to other Social Insurance Funds and Organisations			460,065,091.—		379,373,677.—					
Other Administrative Expenses			1,397,030,340.—		1,250,058,717.50					
Depreciation:										
Banknote printing materials		396,931,100.—		301,034,144.—						
Buildings and equipment (other than office equipment)		220,709,237.—		175,132,340.10						
Office equipment		66,584,150.—	684,224,487.—	59,372,097.—	535,538,581.10					
Provisions:										
Provision according to Art. 71 of the Statutes		59,812,000.—		93,531,000.—						
Sundry provisions		78,000,000.—	137,812,000.—	78,000,000.—	171,531,000.—					
Net Profit for 1987			16,600,638,274.—		15,357,172,794.60					
			1,058,435,853.—		1,777,094,072.65					
			17,659,074,127.—		17,134,266,867.25			17,659,074,127.—		17,134,266,867.25

DISTRIBUTION OF NET PROFIT OF DRACHMAE 1,058,435,853.—

(Article 71 of the Statutes and article 8 of Law 1083/1980)

	1 9 8 7	1 9 8 6
12% dividend on share capital, i.e. Dr. 702.60 per share, on 662,163 shares	465,235,724.—	465,235,723.80
Additional dividend of Dr. 747.40 per share, on 662,163 shares	494,900,626.—	428,684,326.20
To cover valuation differences in the foreign exchange portfolio and expenses in connection with foreign exchange transactions, according to article 8, para. 1, of Law 1083/1980 ..	98,299,503.—	883,174,022.65
	1,058,435,853.—	1,777,094,072.65

DEMETRIOS CHALIKIAS
GOVERNOR

Athens, 22nd March 1988

BASIL BOKOS
DEPUTY MANAGER, ACCOUNTANCY DEPARTMENT

