

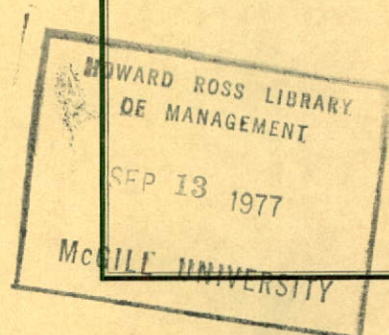
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BANK OF GREECE

REPORT  
OF  
GOVERNOR X. ZOLOTAS  
FOR THE YEAR 1976



ATHENS 1977













Printed in Athens, Greece  
at the Bank of Greece Printing Works



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# REPORT

to the

Forty - fourth Annual Meeting  
of Shareholders  
held on 28<sup>th</sup> April, 1977





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## I. PROBLEMS AND PROSPECTS OF THE GREEK ECONOMY

### 1. REVIEW OF ECONOMIC DEVELOPMENTS: 1975 and 1976

Economic growth and development in the last two years in Greece were, by and large, quite satisfactory. The economy began to turn around from the 1974 recession early in 1975. Real growth increased more rapidly in 1976 and, according to all indications, a high rate of growth can be expected for this year. Significantly, these achievements were accomplished despite the prevailing unfavourable international economic conditions and the serious domestic economic problems that were left behind by the dictatorship in July 1974.

Improvements have also been made in the battle against inflation, the level of employment and in the country's balance of payments. The rate of inflation gradually fell, the level of employment increased, the unemployment rate declined and the balance of payments showed a relative improvement, despite the increase in the oil import bill and the substantial increase in defence expenditures.

By way of comparison, the recovery of the Greek economy in 1975-1976 was considerably stronger than economic growth in the OECD countries. Greece's real gross national product advanced by 5.8 per cent annually while that of the European member countries of OECD increased by only 1 per cent annually. Similarly, the annual increase of industrial production in Greece was 6.5 per cent compared with a flat growth in the European countries of OECD. The higher economic growth realized in Greece led to higher levels of employment in industry (increase: 0.8 per cent in 1975 and 6 per cent approximately during the first ten months of 1976). In contrast, during the last two years, many European countries continued to face rising industrial unemployment. Considering, therefore, that Greece had to deal with a high rate of inflation while also maintaining external balance equilibrium, her achievements can fairly be described as quite satisfactory.

The relatively rapid, but steady, growth that has been realized can, to a large extent, be attributed to the expansionary policy measures that were implemented since the fall of 1974. Indeed, the expansionary path of public expenditures has played a decisive role in bringing about the economic recovery. The fiscal measures were accompanied by an expansive monetary and credit policy, which was designed to accommodate the recovery within the general guidelines of reducing inflation and maintaining external balance. Of course, the adopted incomes policy was a fundamental contributing factor to the success of the overall policy. Through these measures, efforts were made to expand consumer purchasing power in general, and that of lower income groups in particular.

As a result of the rapid rise of nominal wages and other money incomes over and above the increase of the consumer price index (CPI) in 1975-1976, workers' real purchasing power was restored to pre-inflation levels. Indeed, the real wage increases that have since then been realized raised workers' real income to substantially higher levels. On the basis of official estimates, Greece's real private disposable income advanced by 10.5 per cent in the last two years (1976 : 4.5 per cent; 1975 : 5.8 per cent), while it had declined by 7.2 per cent in 1974. It should, of course, be noted that the increase in private



disposable income in Greece was substantially higher than the corresponding increase realized by the European member countries of OECD.

Significantly, the rise in real income was accompanied by a substantial slowdown in the rate of inflation. The rate of increase of the consumer price index declined from 15.7 per cent in 1975 to 11.7 per cent in 1976. While most of the improvement occurred during the second half of 1976, the deceleration of the inflation rate continued during the first quarter of 1977. The rate of inflation of the second half of 1976, on an annual basis, was less than 10 per cent. More specifically, the rise of the CPI in the first quarter of 1977 was 2.4 per cent, compared with increases of 3.3 per cent and 5.3 per cent in 1976 and 1975 respectively. Put in another way, on a twelve-month basis (March 1976 to March 1977), the CPI increased by 10.8 per cent versus 13.4 per cent and 14 per cent for the comparable twelve-month periods of the previous two years.

The established price trends suggest that the government's target rate of inflation, namely the average price increase of the EEC countries, can be realized provided that: a) fiscal, monetary and credit policies remain reasonably restrained, and b) a spirit of cooperation prevails between the government and the various competing social groups, in order to help avoid unreasonable wage and income demands. Conversely, the satisfaction of excessive wage and income demands beyond the economy's productivity gains will increase product unit costs that will be passed on to consumers. Again it should be emphasized that high inflation is still a problem of crucial importance in Greece even though the slowdown in the inflation rate has been significant. Indeed, the resurgence of inflation is a threat not unique to Greece, but is a world phenomenon.

Favourable developments occurred in external transactions as well. The autonomous large inflow of private capital and the improvement in its composition significantly reduced the country's foreign borrowing requirements in 1976 and confirmed the confidence in the country's economic prospects. Another encouraging development of the last two years is the strong expansion of Greek exports, especially industrial exports. This expansion was accomplished despite the adverse economic conditions that have prevailed in Greece's export markets.

The improvement in the balance of payments was, to a large extent, aided by the exchange rate policy that was adopted and implemented as of the fall of 1974. This policy strengthened the competitiveness of Greek products both abroad and at home. Greece's foreign trade sector, however, continued to face some difficulties that ought to be resolved with the design of a sound economic strategy.

Despite the favourable developments thus far described, the Greek economy still faces serious and difficult problems. Coping successfully with these problems is, of course, a prerequisite for the steady continuation of further economic advance. Once again, the threat that inflationary pressures may re-emerge and thus disrupt economic progress must be clearly recognized. In order, therefore, to help reduce inflation further, moderation must continue to be exercised by Greece in her short-term economic policies. In addition, the various social pressure groups must exhibit a sense of responsibility and self-control. Finally, a rationally coordinated development policy must be implemented to take advantage of the new opportunities that will result from Greece's full membership in the EEC.



## 2. ANTI-INFLATIONARY POLICY

The relatively high rate of inflation continued through the first half of 1976, but began to decelerate during the second half of the year. Greece's inflation since 1975 was increasingly due to domestic factors. Chief among them was the excessive rise of money incomes, especially the incomes of middlemen and the self-employed. The rise of money wages and salaries also ran at rates substantially higher than the increase in the CPI.

The magnitude of the increase in incomes can be seen from the wage and salary developments in industry and trade. Data provided by Greece's National Statistical Service indicate that in the third quarter of 1976 the average industrial hourly wage was 28.7 per cent higher than in the comparable quarter of 1975. This rise came on top of a 26.1 per cent increase in hourly wages that was granted during the corresponding quarter of 1975 over 1974. Furthermore, the corresponding average monthly salary increase in trade was 26.8 per cent in 1976 and 21.3 per cent in 1975. Thus, the substantial increase in wages and salaries coupled with limited productivity gains have brought about considerable increases in labour costs. It has been estimated that the average unit labour cost in the non-agricultural sector of the economy rose by 17 per cent in 1975 and by 18 per cent in 1976.

At the same time, the oligopolistic structure of many markets induces autonomous price increases and, concomitantly, higher profits. In particular, middlemen reap wind-fall profits, while the self-employed rapidly adjust their remuneration upwards. It follows then that a price environment pregnant with inflationary expectations induces an over-expansion in the number of middlemen and of people earning high incomes in parasitic-type professions. As a result, the resources of the economy are used irrationally. In view, therefore, of the apparent threat of inflation, it is rather evident why the government's economic policies have aimed at its control.

Furthermore, when a small country, such as Greece, depends heavily on international trade, the movement of relative prices becomes decisive for her competitiveness. If, for example, domestic prices rise faster than foreign prices, the competitiveness of Greece's exportables unavoidably declines. In such a situation, competitiveness can be restored through currency devaluation. Such a course of action is, however, unsatisfactory for three reasons. One is the higher price that the country must pay for her imports. Another is the acceleration of domestic inflation. Yet another is the fact that currency devaluation leads to a fall in real incomes, hitting particularly hard the lower income groups.

Finally, it should be made clear that high rates of inflation cannot be sustained for very long, unless monetary and credit policy is also accommodating. That is, the growth rates of money supply and credit expansion must accelerate in order to accommodate the financing of rising unit costs. To reduce inflation, therefore, it is imperative to control effectively both the growth of monetary aggregates and the expansion and availability of credit.

The implementation, however, of an effective monetary policy becomes difficult, if not problematical, when the budgetary deficits of the public sector induce an expansion of the monetary base (high power money), reducing thereby the effectiveness of monetary and credit policies. Additionally, the structural weakness of Greece's financial system —



as evidenced by the unequal distribution of deposits among the various sectors of the banking system — also reduces the effectiveness of monetary policy.

Broadly speaking, the usefulness of monetary policy for controlling inflation has been generally recognized. For this reason, an increasing number of countries have set target growth rates for their monetary aggregates. These target rates have been set at levels significantly below the rate of increase of the money supply realized in Greece during the last two years. Indeed, in order for monetary policy to be more effective a number of countries have adopted appropriate fiscal measures so that the growth of monetary aggregates does not exceed the predetermined target growth rate. In this context, the EEC, in an effort to harmonize monetary policy among the member countries, is presently looking into the possibility of setting target rates for the expansion of the money supply. These targets will vary in accordance with the unique conditions prevailing in each country. They will, however, be binding on the other EEC member countries.

Hence, it follows that in order to control inflation it is necessary to contain the growth rate of money wages, profit margins and other categories of income. This can be attained through the implementation of a general incomes policy. The goal of such a policy in Greece is to hold the average wage and salary increases in 1977 at a rate below 15 per cent. In fact, such an increase not only corresponds to the annual increase of minimum wages and salaries stipulated in the National Labour Union Contract, but it will also have a favourable impact on the overall effort to further slow down the rate of inflation in 1977. Within the context of the anti-inflation package, the government, early in 1977, introduced new anti-monopoly legislation and adopted a series of other measures that attempt to reduce excessive profit margins and check the rising prices of a large group of products. These measures are considered complementary to the government's incomes policy. They aim at securing the proper functioning of the market mechanism and at reducing abnormal profits which may result either from the presence of monopoly market conditions or from the introduction of restrictive practices.

The success of the government's anti-inflationary incomes policy will, of course, depend on the implementation of a prudent monetary and credit policy. Perhaps even more important is the need for cooperation and self-restraint by the various social groups as they shape their wage, price and income demands. Indeed, it must be clearly understood by everyone that the continuation of inflation inevitably increases social inequalities, undermines the social fabric and leads to wasteful use of economic resources. In the final analysis, prolonged inflation not only reduces the country's possibilities for economic development, but also prevents the people from realizing any material improvement in their living standards.

### 3. MONETARY AND CREDIT POLICY PROBLEMS

The basic problems facing Greece's monetary authorities are the continuing rapid growth rate of liquid assets in general, and the money supply in particular. Moreover, the inadequate structure of credit markets makes the solution of these problems particularly difficult. In fact, the rapidly rising and highly liquid nature of private savings in the



banking system is by itself a potential source of inflation. Another problem is the distribution of savings in the banking system, which is connected with the asymmetrical development of the financial sectors and the existing wide differences in the ability of various parts of the credit system to attract private savings. Thus, the high concentration of most private savings in the country's commercial banks provides the source for the overexpansion of short-term credit to commercial and industrial sectors. These sectors, in turn, use these credits to finance undesirable luxury-good imports and other speculative activities.

Conversely, the financing of other more productive sectors of the economy is hindered and, to a large extent, made dependent on the Bank of Greece. Not only both the public and the agricultural sectors of the economy have necessarily access to the Central Bank, but also a substantial part of other private investment is financed by the Central Bank. This inevitably leads to an increase of liquidity in general, and the money supply in particular.

The inadequate development of a capital market in Greece is, to a large extent, responsible for the flow of a substantial proportion of private savings into bank deposits. The almost complete lack of new security and equity issues in recent years induces the public to hold its savings in a highly liquid form, namely bank deposits. Under these conditions, the commercial banks have developed strong ties of interdependence with the country's large firms. This inhibits the realization of the desired structural changes in the credit markets. At the same time, this interdependence affects adversely the quality and structure of both the companies' and the banks' balance sheets. That is, a certain asymmetry is created between the degree of liquidity of bank assets and liabilities. On the other hand, the capital structure of many industrial firms has been worsening in recent years. Firstly, because the industrial firms are used as vehicles to finance commerce. And secondly, because the combination of recession and inflation have led to a decline of profitability in many manufacturing firms. Consequently, in certain cases this type of funding induces the financial support of firms that are either unable or have no interest to modernize their operations in order to become competitive in world markets.

The supply of money and the economy's liquidity are affected to a very high degree by the deficits of the public sector. Since its financial requirements exceed the savings surplus of the private sector, the deficits are covered by borrowing from the banking system. The result is an expansion of the monetary base, increased liquidity in the economy and a further increase of private deposits which, in turn, leads to larger credit expansion.

Thus, the existing structure of the country's credit markets and the public sector's deficits hamper the implementation of effective monetary and credit policies consistent with the government's objective to bring inflation under control. To make monetary policy more effective, the public sector must reduce its budgetary deficits. In addition, the government must fund a substantial part of the deficit through direct borrowing from the capital market. Finally, a more rational distribution of private savings among the various sectors of the credit system must be secured in order to reduce the dependence of the financing of the basic sectors of the economy on the Bank of Greece. Towards this end, the monetary authorities have, in the last two years, introduced a series of measures that have already begun to yield results. These efforts, however, must continue



until the borrowing needs of the public sector are gradually reduced.

The policy measures which were adopted by the monetary authorities have attempted to reduce the effects of the inadequate structure of the credit markets on the growth of money supply and liquidity and on the distribution of private savings as they are channelled through the credit system. These measures aimed at three different directions. First, the redistribution of funds among the various sectors of the credit system. The effort was made to encourage the channelling of available funds towards special credit institutions. Second, the creation of an appropriate environment that could bring about the reactivation of the capital market. Third, the control of commercial bank liquidity in order to prevent credit overexpansion, while fully meeting the reasonable credit requirements of the commercial and industrial sectors. At the same time, these policy measures attempted to reduce the availability and/or use of credit for financing luxury-good imports. These measures aimed at diverting commercial banks' reserves towards the financing of the deficit of other sectors of the economy in general, and the government's investment budget in particular.

Reallocation of private savings among the various credit institutions was initially sought through the issue of short-term bank bonds. This successful float provided sufficient funds to the investment banks and helped reduce their dependence on the Central Bank. The monetary authorities also encouraged the Agricultural Bank to initiate a campaign for attracting private deposits. Beginning with the second half of 1976, the share of savings flowing into the Agricultural Bank as a percent of the total increase of private savings began to improve materially. As a result, the Agricultural Bank's borrowing from the Central Bank was, *pari passu*, reduced. It is thus expected that half as much of the Agricultural Bank's requirements for additional funds in 1977 will be met out of private deposits. Evidently, these efforts should be continued so that the Agricultural Bank becomes self-sufficient in funds. This is a prerequisite for providing sufficient credit to agriculture without causing monetary disturbances. It should, however, be mentioned that neither the Agricultural Bank nor the investment banks could have been encouraged to attract private savings without the appropriate legislation. This legislation enables the government to subsidize the cost of capital through the budget. For the cost of capital is too high, compared with the prevailing interest rates on agricultural loans and, to a lesser degree, on long-term productive investment loans.

The issue of bank bonds helps familiarize the public with forms of investment other than deposits, while it also creates the appropriate climate for reactivating the bond market. Furthermore, the widening interest rate differentials between commercial bank deposits and advances, instituted by the Currency Committee, has helped create favourable conditions for floating bond issues by both private and public enterprises. Meanwhile, the reduction of interest rates on the various forms of deposits coupled with the deceleration of the inflation rate provide the incentive to float new bond issues on terms that reflect current market conditions. Indeed, the Currency Committee has already approved a new bond issue to be floated by the Public Power Corporation (PPC) in 1977. This bond will provide PPC with a substantial part of the funds required for financing its investment programme. It would, of course, be advisable for the government to resort to the capital market for financing next year's public investment programme. The development of the capital market provides the most effective tool that can be used to correct the structural weak-



nesses of the credit system. It is, furthermore, a necessary requirement to bring under strict control the rate of expansion of the money supply, the economy's liquidity and a more rational allocation of savings. Moreover, the increased supply of securities will most likely bring about a rise in the private savings ratio.

The supply of equity shares must also increase not only because it will help many firms improve their capital structure, but also because it is the most effective means to achieve an efficient allocation of savings. The activation of the equity section of the capital market requires the solution of some problems created by a series of faulty moves and questionable policy measures adopted during the period of dictatorship. The existing difficulties, however, can be overcome. Indeed, the prevailing awkward climate has gradually begun to improve. The new environment will allow young and developing firms to bring new equity offerings to the market. For this purpose the banks should adjust their portfolio policies in order to encourage and/or direct large firms to raise part of their investment requirements in the capital market. In this respect, the monetary authorities intend to adopt strict criteria for approvals of bank loans, which exceed one-fifth of the banks' own share capital to firms which clearly have the capability of raising funds in the capital market.

Finally, the most effective means of curtailing excessive credit expansion is to control commercial bank liquidity. The need of tighter control of liquidity became pressing after the large increase in the inflow of foreign exchange deposits that began during the last months of 1975 and is still continuing. Of course, foreign exchange deposits have always been an autonomous source for bank credit expansion. To the extent, however, that the increase of these deposits remained limited, their impact on the overall expansion of credit was not significant. However, the steep rise of foreign exchange deposits flowing into the commercial banks in 1976 lessened the monetary authorities' ability to control credit expansion. This development largely explains why the Currency Committee's credit expansion target was exceeded by a substantial margin. For this reason, the Currency Committee early in 1977 decided to extend to foreign exchange deposits the reserve requirements applicable to drachma deposits.

Thus, the Currency Committee tightened further the restrictions applicable to all commercial bank deposits. These measures include: (a) a uniform 7 per cent reserve requirement to be held at the Bank of Greece, (b) a uniform 30 per cent required investment in short-term treasury bills and government bonds, and (c) an additional withholding of 15 per cent of the increase in current deposits until the balance of the commercial bank deposits at the end of 1976 meets the newly established reserve requirements and the appropriate portion invested in treasury bills and government bonds. In this context, the monetary authorities have estimated that in 1977 commercial banks' funds will be sufficient to finance a 20 per cent increase in their loans. This is considered adequate for meeting credit requirements of trade and industry, including working capital and part of their long-term capital investment needs. Of course, the estimate of the monetary authorities implicitly assumes that the banks will take the necessary steps to ensure that credit is not diverted into unproductive or socially undesirable activities.

The monetary authorities are, in fact, determined to oversee the lending policies of the commercial banks in order not only to ensure the necessary credit availability for the financing of productive investments, exports and manufacturing output, but also to



prevent the diversion of credit to non-productive uses. Towards this end, the Currency Committee, the Central Bank and the commercial banks have since 1975 instituted unofficial but close consultations among themselves. The purpose of these consultations is to assess the prevailing credit market conditions, to analyze the problems that may arise in the process of implementing credit policy, to evaluate bank lending policies, and to provide and clarify guidelines to banks in formulating their lending policies, ensuring thereby the effectiveness of monetary and credit policies.

#### 4. PUBLIC SECTOR DEFICIT AND MONETARY EQUILIBRIUM

The public sector borrowing requirements in 1976 remained high, even though they actually fell as a proportion of Gross Domestic Product (GDP). The financing of the public deficit, however, brought about an increase in the money supply during 1976 and is expected to do the same in 1977. The total public deficit has been estimated at Dr. 30.6 billion or 3.8 per cent of GDP in 1976, compared with Dr. 40.7 billion or 6 per cent of GDP in 1975. For the current year, this deficit is expected to rise to Dr. 57 billion. As a percent of GDP it will remain at 6 percentage points.

During recessionary periods, increased public deficits are both inevitable and desirable, not only because rising budgetary deficits during the downside of the cycle help cushion the economic decline, but also because during the upside of the cycle an increase in the public deficit provides part of the stimulus necessary to sustain economic recovery. In this context, the government's fiscal policies during the past three years were both stimulative and expansive. The financing of the public-sector deficits did not cause any serious monetary disturbances during the recession. A substantial part of the public deficits was funded out of savings which were transferred from the private to the public sector, particularly through compulsory treasury bill sales to banks. This accommodation was possible since the demand for financing private investment, particularly housing, had declined, while the supply of funds originating in the private sector exceeded the bank credit requirements of the business sector. To the extent then that the public sector's borrowing requirements were not met, financing of the budgetary deficit was covered through an increase in the money supply by the Central Bank and through borrowing from abroad.

With economic recovery under way, it has become gradually more difficult to cover the public sector deficits from the "surplus" units of the private sector. It therefore follows that the financing of this deficit through the expansion of the money supply by the Central Bank became unavoidable.

Hence, the maintenance of the public sector's deficit at its current high level will tend to have an expansionary effect on the money supply. To finance, therefore, a substantial part of the public deficit through savings of the private sector, while also keeping in line with the target growth rate of monetary aggregates, it will be necessary to curtail the expansion of credit to the private sector. The outcome of such developments, however, will be to slow down the pace of recovery of the private sector and to inhibit the growth of productive investment.



To bring inflation under control, it is necessary not only to reduce the public sector's borrowing requirements, but also to resort to methods of financing which minimize the expansionary effects on the monetary base. This entails a gradual reduction of the dependence of the financing of the public sector's deficits on the banking system. Both government and public enterprises should resort to the capital market to raise a substantial part of their borrowing requirements.

Raising funds through the capital market on terms that reflect market conditions becomes imperative for two basic reasons : (a) it will reduce the present high rate of increase of liquidity which could lead to monetary disturbances, and (b) it will probably induce a rise in the private savings ratio or a greater utilization of savings for productive investment and will help prevent the diversion of savings to parasitic-type activities yielding windfall profits. Indeed, Greece is among those very few countries where, following the adverse effects of inflation on the capital markets, the public sector and public enterprises did not draw any funds therefrom in the last two or three years for the financing of either the budgetary deficits or the investment needs of public enterprises.

Despite the relatively quick economic recovery in the last two years and the substantial increase in tax rates yielding approximately Dr. 40 billion, the public deficit to GDP ratio continues to be high (6 per cent). This is basically due to the rapid increase in public expenditures. The rise in these expenditures is explained partly by Greece's need to strengthen her defence capabilities, partly by restoring the purchasing power of civil service wages and salaries that had been eroded during the 1973-1974 high-inflation period, and partly by expanding and improving educational, public health, and other services. Furthermore, production and consumption subsidies have undoubtedly contributed to the widening of the public sector's deficits. These deficits get larger as a result of the rapidly rising unit costs of public enterprises and the delay of passing on to the consumer the higher production and service costs. This pricing restricts the public enterprises' capability to self-finance their investment programmes, which in turn leads to greater dependence on borrowed funds. It is thus evident that the public-sector deficit is largely structural. Hence, the reduction of budgetary deficits to levels that are consistent with the maintenance of monetary equilibrium requires containment of public expenditures, increased productivity in the civil service, improvement in organizational and managerial methods and more efficient operation of public enterprises. Taken together these improvements aim at containing the rising trend of operating costs. At the same time public enterprises must review their pricing policies in order to secure a rational allocation of economic resources.

The rational formulation of government investment programmes is also required to secure priority ranking of investment projects based on cost-benefit analysis. Finally, it is desired to gradually limit state subsidies and income support schemes and to pass on to the consumer the rising production costs. The Ministries of Coordination, Finance and other government agencies have taken measures geared towards these ends. However, the inherent difficulty of these problems should not be overlooked. Their solution requires in depth study and careful preparation. In this context, the Ministry of Finance has undertaken an overall study of the tax system, aiming at harmonizing gradually the Greek tax system with EEC regulations. The study also aims at strengthening the progressive nature of the tax system, attaining a more equitable distribution of the tax



burden and helping the country accomplish her development goals. The introduction of effective methods that could capture a larger part of taxable incomes is to be part of the proposed rationalization of the tax system. It is, of course, understood that the implementation of effective measures to combat tax evasion is a necessary prerequisite for increasing the efficiency of development incentives and for securing a rational allocation of economic resources.

## 5. PROBLEMS OF BALANCE OF PAYMENTS

During 1976 the current account deficit remained at almost the same level as in 1975. Thus, for a fourth consecutive year, the current account deficit exceeded \$1 billion. While the merchandise trade deficit increased further, it was partly offset by an improvement in the invisible trade surplus.

Indeed, no difficulties concerning the financing of the balance-of-payments deficit were encountered in 1976. This was due to the large inflow of private capital, mainly foreign exchange deposits of Greek emigrants. The rate of growth of imports accelerated beginning with the third quarter of 1976. This was partly due to the higher rate of growth of Gross National Product. An especially large increase in consumer goods imports was realized owing to the high income elasticity of demand for goods of this category.

Furthermore, payments for fuel imports have shown a big increase resulting from a restocking policy in anticipation of crude oil price increases in early 1977. However, the country's needs for fuel imports have been rising at a high rate. Accordingly, pressures on the balance of payments will continue to exist for some years to come. In contrast, the value of capital equipment and industrial raw material imports has remained at the 1975 level despite the large increase in industrial production and construction activity during the last two years. The sluggish growth of raw material imports could partly be attributed to inventory liquidation of imported raw materials which had been accumulated for speculative purposes during the 1973-1974 high-inflation period. According to current estimates, the process of inventory liquidation was completed in 1976. As of the second half of that year imports of raw materials exhibited a more direct relation to output and economic activity.

Developments in foreign exchange earnings indicate that exports of industrial goods, particularly textiles, continued to increase at a rapid pace. On the other hand, lower agricultural prices in foreign markets affected adversely the rate of growth of total export receipts. Finally, the pick-up in economic activity and trade in industrial countries had a favourable effect on Greece's foreign exchange earnings from tourism and shipping. Conversely, the high unemployment rate in Western European countries and, particularly, the contraction in Germany's labour market account for the stagnation in emigrants' remittances.

The 1976 balance-of-payments deficit was, to a great extent, financed by the increase of autonomous private capital inflows, chiefly foreign exchange deposits of Greek workers in West Germany. The existing interest rate differentials between Greece and other countries provide an important incentive for the rising inflow of these deposits.



Another contributing factor is the repatriation of Greek workers from Germany. This source of capital has significant advantages since a large part of these deposits is converted and spent in local currency and therefore does not entail any service obligation in foreign exchange. As a result of the large autonomous inflow of private capital, the stock of the country's foreign debt has decreased as amortization exceeded new commitments. Developments in net foreign exchange deposits in the first months of 1977 have been quite satisfactory. Although this source of capital is exhaustible, it can still provide the breathing space necessary for the promotion of the required structural changes in the economy without at the same time seriously upsetting its external balance.

The absence of serious difficulties in financing this year's current account deficit points to the fact that the maintenance of external balance in the near term will depend on the possibility of containing the growth of the trade deficit. This target relies heavily on furthering the export orientation of Greece's economy, and of its industry in particular. This, however, requires substantial changes in the structure of the economy as well as a much higher degree of specialization in industry. It should also be stressed that balance in the country's external accounts will be more difficult to sustain in the future through increases in the export of services, at least to the extent that it was done in the 1960's and 1970's. It is expected that, in the course of time, the possibilities of developing tourism further are not unlimited, especially when the social costs involved are taken into account. On the other hand, improvement of Greek economic conditions and policy changes concerning foreign workers in most European countries, especially W. Germany, have already turned emigration around.

In addition, the competitiveness of Greek products in world markets and the promotion of exports in the future can only be accomplished by improvements in productivity. At the same time, increased rewards to factors of production should be compatible with productivity gains. The conditions that prevailed in the Greek economy in recent years, especially the need to restore real wages and salaries to pre-inflation levels, have weakened the competitiveness of Greek products.

As was noted in last year's Report, the exchange rate policy pursued during the early period of democratic rule (July 1974-end 1975) was the only way available to strengthen the competitiveness of Greek products in world markets. Of course, resorting to foreign exchange policy cannot be used permanently as a means of improving the economy's competitiveness. For it increases the cost of imports and becomes a source of inflation in an open economy such as Greece's.

For a new successful export promotion campaign that will help maintain Greece's external balance, especially after full EEC membership, it is required to take measures that will bring about a change in the structure of national expenditures. Hence, it is imperative to contain the growth of imports within the economy's export earning capabilities without jeopardizing the country's economic growth rate. Otherwise, the maintenance of external balance will require a restrictive economic policy which, coupled with the anti-inflationary effects created by the substantial expansion of imports, will inevitably reduce economic growth to levels lower than those socially desired. To avoid the risk of slower growth while taking advantage of the opportunities provided by Greece's entry into the EEC and to strengthen the competitiveness of the export-oriented sector of the economy, it is necessary to:



a) Place under control the increase of profit margins and other incomes, mainly derived from intermediary professions, services and other profiteering parasitic-type activities. In addition, effective measures must be adopted to bring these incomes under taxation. Significantly, incomes from these categories are numerous, comparatively high and are rapidly rising. These incomes are, therefore, a significant source of over-consumption and strong demand for luxury-good imports. At the same time, the consumption patterns of these social groups influence the consumer behaviour of the population at large.

b) Adopt appropriate measures aiming at restricting the country's dependence on fuel and other energy imports. Significant progress has been made towards this end through a policy of promoting the development of domestic energy resources, particularly those concerning electric energy production. The efforts for research and development of domestic energy resources must, however, be intensified. Aside from traditional energy sources (petroleum, lignite) Greece seems to have also some possibilities of developing geothermic energy sources. In the absence of rapid utilization of these resources the country's growing dependence on fuel imports becomes inevitable. Furthermore, the subsidization policy of goods and/or of factors of production (in this case energy), which are capital-intensive and have a high foreign exchange content, is not appropriate and must be reconsidered as soon as possible. Towards this goal the National Energy Council has already worked out a general framework for a rational fuel policy which is being put into effect. A similar energy policy is, of course, followed by most industrial countries.

c) Concentrate on modernization and development of the agricultural sector in order to raise productivity and induce the cultivation of crops that will increase exports and/or substitute imports. Attention must also be paid to the development of the cattle and dairy industry which should be based on domestic production of animal feed. Indeed, the Ministry of Agriculture has, for the first time in the postwar period, made a systematic effort to develop and implement a rational agricultural policy. When fully implemented, this policy will contribute to more rapid agricultural development and will bring about the necessary structural changes in view of the country's entry into the EEC.

## 6. PROMOTING INDUSTRIAL INVESTMENT

The upswing of economic activity that has taken place during the last two years and is still continuing at a relatively increased pace has, to a great extent, been accomplished through rising capacity utilization. According to available indications, capital utilization in some sectors of industry approaches or tends to exceed all previous peaks attained during the last fifteen years. This means that rising demand, which began to accelerate in the fall of 1976, will, at some point, probably encounter inelastic supply in certain basic industries.

The rapid rise in capacity utilization, which is apparently taking place in many industries, has occurred partly as a result of the relatively small decline in industrial



production during the recession. Thus, industrial production at the end of 1976 exceeded by 13.2 per cent the pre-recession peak. Nevertheless, the substantial reduction in idle capacity reflects declining industrial investment for two consecutive years. This trend seems to have been reversed during the last months of 1976. Significant changes in the structure of investment have also occurred. The bulk of these investments is concentrated in certain traditional branches of Greek industry that have a relatively short pay-back period. Many entrepreneurs undertake small size cost-reducing investments aiming at expanding and/or further improving existing capacity. However, the size of these investments is insufficient in terms of total investment requirements. Activity in new industrial projects is inadequate, particularly when the pay-back period of investment is invariably lengthened.

Uncertainties with respect to costs and the size of demand in the future underlie slack investment activity internationally. Lack of clear-cut trends in the world economy coupled with a rather slow recovery of domestic demand for certain industrial goods inhibit risky investment undertakings. Added to that are the adverse effects of inflation on new industrial investment. Moreover, inflation affects adversely the allocation of savings in favour of less productive and/or parasitic-type activities yielding windfall profits.

Delays in the government's development policy concerning investment incentives and the spatial distribution of industrial plants apparently act as a deterrent for undertaking major business ventures. In addition, the complex and time-consuming bureaucratic processes and regulations that are required for the approval and realization of new investment create an unfavourable climate which discourages foreign investment in Greece. These difficulties are not only related to inflexible red tape but are also the result of a complex system of incentives and state regulations.

Slack investment activity, primarily in manufacturing, is not a phenomenon unique to Greece; it is attributed to uncertainties created by the deepest and most prolonged postwar recession and the accompanying world-wide inflation. The recovery of industrial investments combined with changes in their structure and composition is the major and most pressing problem of the Greek economy. Lack of substantial new profitable industrial projects engenders risks of rising inflationary pressures that will adversely affect exports as the economy approaches full capacity utilization. At this stage new investment projects in manufacturing are indispensable, in order to bring about the necessary changes in the country's industrial structure, modernize Greek manufacturing and increase its competitiveness. All these are prerequisites in order to benefit from the redistribution of industrial activity within the EEC.

The country's industrialization can essentially be based on domestic entrepreneurship. New technology requirements, however, call for the attraction of foreign direct investment. Hence, the necessary industrial environment conducive to new undertakings must be created so that this goal may be attained. The country's expected entry into the EEC demands an attractive industrial environment that will induce foreign firms to locate in Greece. Development incentives, proprietary rights, fixed tax rates and other methods used in the past to motivate local businessmen and to attract foreign investment have not only been ineffective, but are also in contravention of EEC rules and regulations. Consequently, these incentives cannot remain in effect after the



country's entry into the EEC. To create a favourable industrial environment, therefore, the following steps must necessarily be taken:

a) Formulation and implementation of an efficient policy of development incentives. This policy should be simple and almost automatic in its implementation. The simplicity of the system will reduce and/or eliminate doubtful disputes and will discourage red tape. It is, therefore, necessary to reform the entire system of incentives. An effort towards this end has already been made by the Ministries of Coordination and Finance. Problems related to incentives policy, regional development and state subsidies, have also been submitted to the Community for further deliberation.

b) Adoption of a fixed-rate tax system which will be more favourable than the one in effect in industrial countries in general, and the EEC member countries in particular. This system should be designed to promote the country's development goals. Furthermore, the implementation of a non-discriminatory tax system is a necessary precondition to reduce red tape, state control and intervention, as in the case of development incentives policy. The introduction of a more favourable tax system than the one in force in other developed countries of the West is well-founded on the grounds of the less developed nature of the Greek economy. Such a tax system may also enable Greece to become a more attractive place for industrial investment. In any case, however, public revenues and expenditures should benefit substantially from the taxation of corporate profits.

c) Clarification of policies concerning foreign investment. The guidelines and criteria governing foreign-investment policy must be simple, clear, generally applicable and readily implemented. The prevailing confusion concerning the role of foreign investment and the public's distrust towards it originate from certain disadvantageous contracts negotiated during the period of the dictatorship. The formulation and implementation of a sound and clear-cut policy regarding foreign investment will ensure and serve the country's best interests. This policy will also help make public opinion more favourable, which is a prerequisite for attracting foreign investment.

The basic criteria for accepting foreign investment capital must be its contribution to (i) productivity gains, (ii) improving the country's technology and managerial know-how, (iii) increased specialization of labour, (iv) increasing competitiveness in domestic markets, (v) strengthening the export orientation of the Greek economy and, (vi) encouraging joint ventures between local and foreign firms. Finally, the preferential treatment that has at times been extended to foreign capital should not be repeated, for it has in the past hurt Greek firms in the same or related industries. In general, unfair competition leads to high concentration, abuse of monopoly power and occasionally to business inertia. Of course, the country's accession to the EEC will limit the interest in low-value-added investments that are generally concentrated in the final stages of production. This kind of investment basically constitutes an expansion of the multinationals' commercial network aiming at the domestic market.

d) Establishment of more competitive conditions both in the production and the distribution sectors. Market pressures along with the aforementioned measures constitute the most effective method to bring about rapid technological and financial changes in the structure of Greek companies. Thus, the most dynamic firms will be forced to develop and innovate rapidly, whereas firms that have no development potential or are



not interested in modernizing and adjusting themselves to new market conditions will be left behind. To enhance competition the following items must be taken into account: (i) Reconsideration of all outdated government regulations and market interventions that have, in the past, been adopted but are now out of date. These policies act as disincentives and impede the orderly functioning of the market mechanism. Regulations that are thought to be harmful or even superfluous should be abolished, while others should be simplified and improved. Reducing the protection of the less efficient firms and strengthening the relative position of the more dynamic ones, which are able to develop within a competitive EEC environment, is a fundamental objective; (ii) Introduction of antimonopoly legislation in the belief that its application will act as a counter-vailing force to monopolistic and/or oligopolistic tendencies that may exist in many industrial and trade sectors. Creating the appropriate agencies manned with trained and highly specialized personnel is of decisive importance for the success of such a policy.

Government policies concerning these issues are expected to be clarified by the new medium-term plan. The timely formulation and implementation of all proposed measures is, of course, of primary importance in furthering industrialization. The pending entry of Greece into the EEC makes their implementation imperative and exceptionally urgent. To implement this policy, however, prior lengthy consultations with the EEC authorities are required in many cases. A significant reduction of the current inflation rate is the prerequisite for the new measures to be effective since inflation leads to misallocation of resources and discourages new investment that can help bring about structural changes in industry. To this end, all interested parties should cooperate so that the government's incomes policy proves successful. Taxation of excess profits from intermediary or parasitic-type activities along with increases in real wages and salaries compatible with productivity gains are complements to such a policy.

To the extent that the private sector is reluctant to undertake investments in key branches of industry, the appropriate policy is believed to be that development agencies such as the Hellenic Industrial Development Bank and the Hellenic Industrial and Mining Investment Company become more involved. These agencies should be in a position to undertake such investment initiatives, preferably in close cooperation with private firms. While considerable progress has been made thus far, it cannot be said that these agencies could undertake the largest share of the required investment. Nor is it feasible or even desirable for them to act as a substitute for private initiative. Consequently, the largest part of the required industrial investment is bound to be undertaken by the private sector. Hence, it is of the utmost importance that proper measures, as suggested above, be taken to create the necessary competitive environment. Activating all development agencies and advancing profitable industrial projects will not only fill the investment gap, but will also create a business climate conducive to undertaking large private investment projects.

Also important is the role of banks in supplying the necessary funds for the realization of technically and financially sound investment projects. The monetary authorities should pursue a policy which ensures an ample supply of long-term capital for investment financing. Banks, however, have limited means at their disposal to influence the demand for long-term capital, for investment depends both on domestic and international development prospects and on the improvement of the business environment.



## II. ECONOMIC ACTIVITY, EMPLOYMENT, WAGES AND PRICES

### 1. NATIONAL INCOME AND OUTPUT

According to provisional national account estimates, real gross national income at factor cost rose by 5.6 per cent in 1976, compared with an increase of 4.1 per cent in 1975 and a decrease of 2.1 per cent in 1974. Rates of growth of GNP at constant market prices were higher, namely 6.0 and 5.7 per cent for 1976 and 1975 respectively, following a 3.8 per cent decline in 1974. The large increase of indirect taxation in 1975 accounts for the divergence observed between the growth rates of the two concepts of income.

In terms of GNP growth rates, the Greek economy performed better than the EEC and the European OECD countries where real GNP rose by 4.2 per cent and 3.7 per cent respectively. Moreover, in 1975, GNP in Greece increased by 5.7 per cent in contrast to a decline of 2.2 per cent and 1.9 per cent for the EEC and the European OECD countries respectively. Thus, Greece's average annual growth rate in 1975 and 1976 was much higher (5.8 per cent) than that of the EEC and the European OECD countries, where the corresponding growth did not exceed 1 per cent.

The acceleration of the rate of increase of real GNP at factor cost in 1976 reflects higher growth of real incomes originating both in the service sector — which accounts for half of national income — and in secondary production. Income from primary production dropped below the 1975 level, following a good record in the previous two years.

A more detailed account of the performance of the various sectors shows the following changes in income and output:

Real income from primary production is estimated to have decreased by 1.5 per cent in 1976. Growth rates for 1975 and 1974 were 4.6 and 5.1 per cent respectively. This decline stems from both agriculture and livestock. The fall of output in agriculture reflects smaller tree crops. Increased production of citrus fruit compensated only partially for the reduced output of olive oil products in 1976, while the output of annual crops remained unchanged. Finally, a lower level of meat production accounts for the smaller output of livestock and dairy products.

In contrast, agricultural income at current prices increased by 16 per cent in 1976 (1975: 10.7 per cent; 1974: 15.2 per cent). The changes in current and constant prices suggest that the implicit deflator of agricultural incomes showed a more rapid increase in 1976 (1976: 17.8 per cent; 1975: 5.8 per cent; 1974: 9.6 per cent). The increase reflects an improvement of producer's prices for almost all agricultural products and a smaller rate of increase in prices of basic agricultural inputs.

According to official estimates, real income originating in secondary production went up by 8.8 per cent. Growth in 1975 was 5.4 per cent, compared with an 11.0 per cent fall in 1974. A pronounced recovery in the manufacturing sector was the major factor behind the acceleration of the growth rate in 1976. Increased activity in mining and quarrying also contributed significantly to last year's growth. Real income from this sector rose by 6.0 per cent, almost twice as much as the 3.3 per cent rise recorded in 1975. Mining and quarry output was favourably affected by the substantial increase in the con-



struction of private dwellings. Similarly, the substitution of lignite for other electric power inputs boosted domestic demand for lignite. This offset the impact of reduced foreign demand for bauxite and limestone products, whose output fell below the 1975 level.

Real income from manufacturing increased by 9.8 per cent compared with a 5.2 per cent growth rate in 1975 and a 2.8 per cent fall in 1974. The rise of real disposable income revived domestic demand for manufacturing products, mainly final industrial goods and construction materials. Foreign demand contributed, to a lesser extent, to the acceleration of growth in 1976.

Income originating in the construction sector increased by 5.5 and 4.3 per cent in 1976 and 1975 respectively, as a result of high building activity in the private sector during both years. Real income from public utilities increased as well (1976: 11.3 per cent; 1975: 11.4 per cent) reflecting mainly larger electric power output.

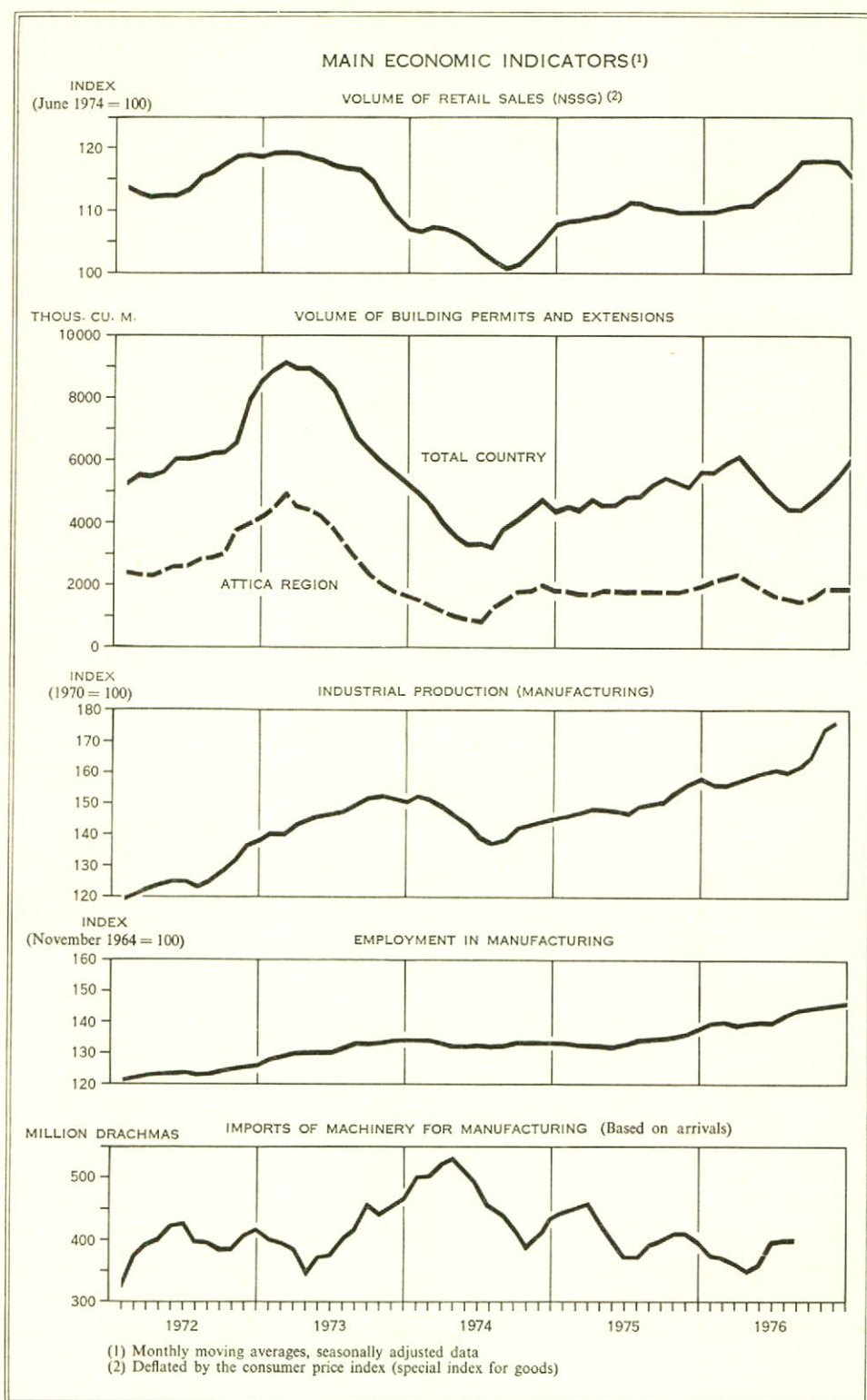
Growth in the service sector accelerated substantially. Owing to the improved performance in trade and tourism and a higher level of public-sector employment, real income from services increased by 5.5 per cent in 1976 compared with 4.0 per cent in 1975 and 2.4 per cent in 1974. In particular, income from transport and communications is estimated to have increased by 7.5 per cent (1975 : 5.0 per cent), trade and banks by 5.0 per cent (1975 : 3.0 per cent), rents by 4.5 per cent (1975 : 4.1 per cent), Public Administration services by 4.0 per cent (1975 : 2.7 per cent), and income from "other services", mainly tourism, by 8.1 per cent (1975 : 7.8 per cent).

## 2. THE EXPENDITURE OF THE ECONOMY

According to the latest available provisional estimates, the gross expenditure of the economy in real terms increased by 4.7 per cent in 1976. The recorded growth for 1975 was 6.0 per cent, following a drop of 6.3 per cent in 1974. Since the rate at which expenditure expanded was lower than GNP growth (6.0 per cent), net transfers from abroad on current and capital account were reduced by 21.6 per cent in 1976 in contrast to an 11.1 per cent increase in the previous year.

In view of the satisfactory GNP growth rates achieved for two consecutive years following the 1974 recession, Greece seems to have weathered the prevailing adverse international economic climate. A closer examination of the structure of the recovery will, however, reveal certain weaknesses that may hamper the economy's future prospects. First, both the pattern and allocation of total expenditure between consumption and investment do not provide a favourable setting for the sustenance of a high economic growth rate in the future, nor can they help bring about the necessary structural changes in the Greek economy. A sizable amount of consumer expenditure is diverted to conspicuous consumption of luxury goods and services.

Second, investments have not as yet reached pre-recession levels, and continue for the third year to absorb a relatively small share of available resources. The bulk of private investment is channelled to private dwellings, mostly luxury apartments and villas. Moreover, investment in manufacturing has been particularly sluggish. Should this trend continue, the basic transformation of Greece's economy could be placed in jeopardy.





The volume of total consumption increased by 4.8 per cent in 1976 (1975 : 5.9 per cent; 1974 : 2.5 per cent). This amounts to two thirds of GNP growth, with private consumption contributing the larger part. Rates of increase in private consumption were 5.1 and 4.7 per cent for 1976 and 1975 respectively, against 0.8 per cent in 1974.

The increase in real consumer expenditures in the last two years has been stimulated by the growth of personal disposable income, following large increases in wages and salaries and in incomes of the self-employed, particularly those engaged in intermediate trades and other services. In short, the continuing growth of consumer demand is a potential source of serious difficulties, for it tends to reduce the flow of savings available for the financing of investments. This is particularly evident when we consider that a large part of private consumption is channelled to luxuries or semi-luxuries, which are mostly imported. Strong pressures are thus exerted on the balance of payments. In general, the composition of private consumption leads to a misallocation of resources.

In contrast to rising consumer expenditures, the rate of growth of public consumption slowed down in 1976, owing to efforts made by the Ministry of Finance to curtail some flexible expenditure items included in the ordinary budget.

The volume of gross fixed investment in 1976 increased by 6.5 per cent, remained unchanged in 1975 and dropped by 25.6 per cent in 1974. This implies that fixed investment has not yet reached pre-recession levels. Fluctuations in the rate of growth of investment reflect changes in the volume of investment in private dwellings, which in 1974 dropped by 48 per cent, but rebounded by 29.0 and 8.0 per cent in 1975 and 1976 respectively. Conversely, real fixed investment in manufacturing over the same two years declined by 2.5 per cent in 1976 and 11.5 per cent in 1975.

Considering investment developments, Greece did better than most of the European countries of OECD. However, the importance of this performance is reduced by the fact that investment realized mostly represents investment in private dwellings. Moreover, manufacturing investment accounts for a small share of total investment. Actually, investment in housing represents a very high proportion of the total, i.e., about 30 per cent of total fixed investment or about 40 per cent of private fixed investment. These figures are substantially lower in most industrial countries, or even in countries in the same stage of development as that of Greece.

### 3. AGRICULTURAL OUTPUT

Provisional Ministry of Agriculture estimates suggest that the gross value of real agricultural production decreased by 1.4 per cent in 1976 compared with a rise of 4.4 per cent in 1975 and 9.3 per cent in 1974. The lower level of output in 1976 can be explained, first, by inadequate foreign demand for certain exportables (tomato paste, rice) which led to a curtailment of these cultivations; second, by adverse weather conditions which caused a fall in the cotton crop; third, by reduced olive oil and meat production. The latter resulted from a drop in livestock population in 1975 which followed the substantial increase in animal feed prices relative to meat prices recorded during previous years. However,



larger wheat, tobacco, sugar beet and potato crops offset, to a significant extent, the above-mentioned losses of output.

Experience gained in the last few years shows that policy measures decisively influence short-run developments in agriculture — a point that should be strongly emphasized. For Greek farmers respond rationally to market signals and policy changes, providing thereby the opportunity for the alignment of farmers' decisions with agricultural policy guidelines. Hence, the implementation of a sound agricultural policy assumes greater importance.

Certain developments, particularly those of last year, can be better evaluated in the light of this assessment. The larger wheat crop, for example, was the result of a policy aimed at expanding hard wheat varieties. The increased production of tobacco and potatoes aimed at raising the level of output of agricultural exportables. The increase in sugar beet production aimed at the attainment of complete substitution of domestic for imported sugar. Another planned development was to hold down the output of rice and tomatoes used in making tomato paste. Since in the previous two agricultural years their output had increased to levels well above domestic consumption and export capabilities, these crops had to be restricted in the 1975/1976 crop year, within limits dictated by market conditions.

The effort to develop and expand the output of animal feed and livestock products must be continued. Fodder output recorded a small increase, whereas meat production decreased by 2.5 per cent in 1976. The import bill for meat and animal feed increased from \$240 million in 1975 to \$360 million in 1976. This shows that the problem of developing livestock production in Greece reached a critical point for reasons related to erroneous policy measures taken during the dictatorship.

A break-through can, of course, be made by increasing low-cost fodder output and by implementing a correct pricing policy concerning animal feed and livestock products, especially various types of meat. To a great extent, the development of this sector depends on the magnitude of the differential between breeding costs and product prices. It is well understood that a policy aiming at ensuring a reasonable profit margin for the producers should not rely on a policy that subsidizes costs or prices. Such a policy is equivalent to subsidizing the consumer, which in turn leads to over-consumption of products in short domestic supply, as is the case with veal.

It is hoped that certain policy measures, taken recently, will bring about a reversal of these adverse trends. For example, in order to widen producers' profit margins, prices of milk and certain meats have been increased. At the same time, government subsidies that distort market prices for animal feed are in the process of being reduced. Nevertheless, in order to have an integrated economic policy regarding this sector and to solve, on a longer term basis, the problem of meat production, it is necessary to design well coordinated policy measures that affect the entire process, i.e., make effective use of the possibilities of producing low-cost animal feed, operate farms rationally, develop fully all products and by-products and organize efficiently their marketing and distribution. These goals must be related to appropriate interventions that affect both inventories and imports.

Apart from the short-run measures already introduced in the annual agricultural plans, which succeeded in clearing the markets, the government should also work out



and apply measures aiming at solving the long-run development problems of Greek agriculture. This is a factor of paramount importance pending Greece's full membership of the EEC.

Such a policy should especially deal with the optimization of production possibilities of farm land and with problems related to the reorganization of the production process. This should be accomplished according to production patterns prevailing in countries with advanced agricultural sectors, such as the EEC member countries. The framework of this policy has begun to take concrete form in the annual plans of the Ministry of Agriculture. The directives of government policy aim at improving productivity so as to raise the economic, social and cultural status of the rural population and help the entire sector prepare for an effective solution of the problem that will be encountered upon Greece's entry in the EEC.

#### 4. DEVELOPMENTS IN INDUSTRY

The 1975 upturn in industrial production (manufacturing, electric energy, mining and quarrying) accelerated in 1976. The rate of growth of output was 10.6 per cent, compared with 4.4 per cent in 1975. Manufacturing also grew by 10.6 per cent, in contrast to an average growth rate of 6.1 per cent for the European OECD countries and a 7.2 per cent growth rate for the EEC member countries. Output in mining and quarrying increased by 8.0 per cent while power generation rose by 11.6 per cent.

The acceleration in the rate of increase in manufacturing output was induced by buoyant domestic demand, stimulated by the rise of wage earners' real income; by the continuing upturn of private dwelling construction; by an increase in public investment; and by strong foreign demand for products of a limited number of industries.

The output of consumer goods industries — which constitutes the larger part of manufacturing production — increased by 12 per cent. Among these industries consumer durables exhibited the most rapid growth rate (13.1 per cent). It should be noted that the 1974 recession was particularly pronounced in these industries. Compared with the relative recovery of other branches of manufacturing, their turn-around was delayed. Finally, output in capital goods industries increased by 6.9 per cent.

A closer examination of developments in specific branches of manufacturing shows that output in textile industries increased by 15.4 per cent in 1976 and by 18.4 per cent in 1975. Growth was particularly pronounced in cotton industries, where the rate of increase in output jumped by 29.6 per cent — a figure which was three times higher than that of 1975. Knitting and silk industries recorded output rises of 19.0 and 16.6 per cent respectively. Trends in textile exports suggest that foreign demand contributed to this growth. In the January-October 1976 period, the average level of textile export receipts (measured on a customs basis), increased by 62.0 per cent over the same period in 1975. In the previous comparable ten-month period, textile export receipts dropped by 7.0 per cent.

Growth of export markets, coupled with the expansion of domestic demand, caused by the upturn in building activity, led to a higher output of basic metal industries (1976: 6.9 per cent; 1975: -2.6 per cent). Nickel output, for example, increased by 11.1 per cent



in 1976 against a drop of 1.6 per cent in 1975. Basic metal export receipts in the January-October 1976 period rose by 33 per cent compared with a fall of 7.0 per cent over the same period in 1975.

Output in chemical industries increased by 9.0 per cent in 1976, compared with 8.5 per cent in 1975. In general, all industries recorded substantial growth rates in output, with the exception of fertilizers, where production dropped by 1.7 per cent. Despite the increase in manufacturing output, however, the average level of the value of exports in the January-October 1976 period dropped by 16.4 per cent, compared with a 46 per cent increase in 1975.

The rise of output in non-metallic mineral industries which began in 1975 speeded up in 1976. Production increased by 15.1 per cent compared with 5.2 per cent in 1975. This increase originated in the cement and glass industries, the output of which expanded by 17.2 and 31.0 per cent respectively. The rise in cement production was stimulated mainly by domestic demand, which grew by 9.8 per cent in 1976, whereas cement exports increased by only 10.8 per cent compared with a 49.0 per cent jump in 1975.

Output in mining and quarrying responded positively to the upturn of domestic demand. Activity in these industries increased by 8.0 per cent. Lignite output increased by 24.5 per cent and that of iron and ferronickel ores by 11.7 per cent. Conversely, ore exports fell in 1976, with the exception of lead and zinc ores, marble and sulfur.

Power generation was the other sector where the 1976 rate of recovery picked up speed. According to National Statistical Service data, electric energy production increased by 11.7 per cent in 1976 and by 6.5 per cent in 1975. At the same time, total electric energy consumption increased by 10.8 per cent. Manufacturing accounted for 57.2 per cent of total electric energy consumption, reflecting a 10.3 per cent rise over 1975.

## 5. THE EMPLOYMENT SITUATION

Available evidence regarding the employment situation in the non-agricultural sector of the economy in 1976 suggests substantial employment gains in contrast to the previous two-year near stagnation. Data produced by the Organization for the Employment of the Labour Force show that in comparison with 1975 the number of persons placed in the 1976 January-October period increased by 7.8 per cent, while the number of those discharged from work decreased by 8.1 per cent. A special survey carried out by the National Statistical Service suggests that in 1976 the unemployment rate in urban and semi-urban centres was reduced.

Manufacturing employment in particular began to rise as of the third quarter of 1975. The established upward path continued at a more rapid pace throughout 1976. National Statistical Service data show that employment in large-scale manufacturing increased by 6.1 per cent in 1976, compared with 0.8 per cent and 1.1 per cent increases for 1975 and 1974 respectively. Conversely, hours worked per person employed decreased for a second consecutive year, presumably because the statutory average work week was reduced in certain industries. As a result, the rate of increase of total hours worked in manufacturing declined to 3.5 per cent over the 1976 January-September



period, while manufacturing employment rose by 5.9 per cent. Total hours worked in manufacturing dropped by 1.8 per cent in 1975. However, recent evidence suggests that the construction and public sectors realized significant employment gains in 1976.

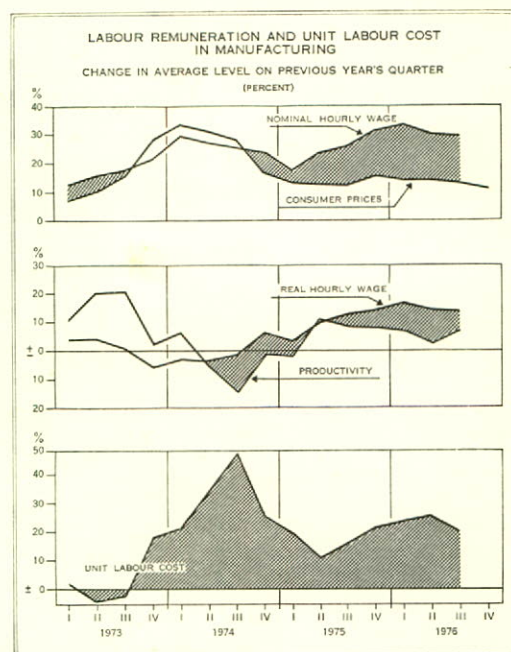
Net immigration was positive for a second year in succession. Net emigration began to fall in 1972 and by 1974 it was almost zero. In 1975 a reversal of trend occurred for the first time resulting in a net immigration of 14,000 persons. In 1976 the rate of repatriation continued as in 1975. For the first nine months of 1976 net immigration reached 11,000 persons. Though three quarters of these repatriates entered the labour force, their impact on the domestic labour market was relatively unimportant. Most of these repatriates either engaged themselves in rural activities or became self-employed. Hence, their influx has not, up to now, raised the unemployment rate.

## 6. WAGES AND SALARIES

Wages and salaries recorded sizable increases in 1976. The average level of minimum wages and salaries, including family allowances, rose by 22.0 per cent. In particular, civil servants' salaries increased by 21.0 per cent, while salary increases for employees in public enterprises, banks, local administration and social security ranged from 15.0 per cent to 18.0 per cent. Wages in wholesale and retail trade rose by 26.0 per cent, while wage increases of private firms ranged from 29.0 to 30.0 per cent. Accountants and bus transport employees were granted 34.0 and 18.0 per cent salary increases respectively. Generally, the 1976 wage and salary increases exceeded by a substantial margin the sum of the increase in the consumer price index and the increase in productivity.

In the January-September 1976 period, for example, nominal hourly wages in large scale industry rose by 30.4 per cent (14.5 per cent in real terms) over the comparable period of the previous year. Correspondingly, nominal weekly earnings rose by 28.0 per cent (12.3 per cent in real terms). Similarly, monthly salaries rose by 23.8 per cent in money and 9.3 per cent in real terms. In the same period, labour productivity in manufacturing increased by 6.0 per cent compared with a 6.3 per cent increase in 1975 and a 3.8 per cent decrease in 1974.

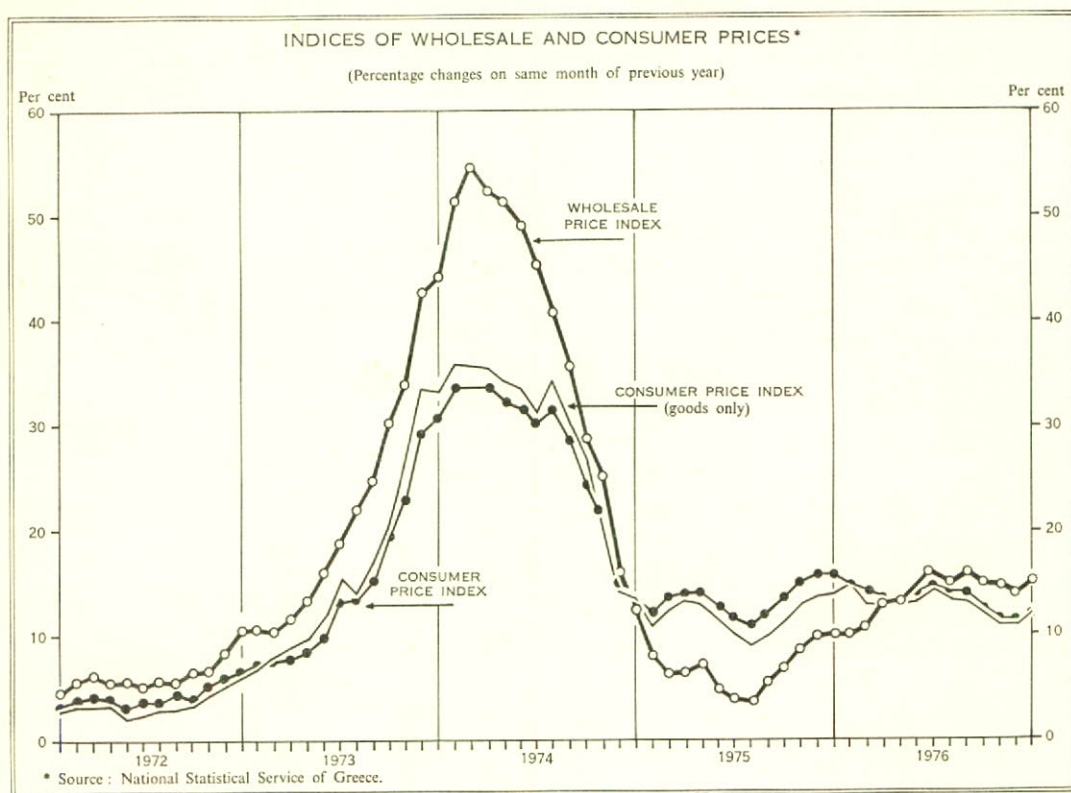
In spite of the relatively high labour productivity gains, the substantial increase in nominal hourly industrial wages led to a significant rise in unit labour cost. In the January-September 1976 period, unit labour cost increased by 23.0 per cent, compared with a



rise of 17.0 per cent in 1975 and 31.0 per cent in 1974. Significantly, labour cost developments in 1976 coincided with a rise in industrial raw material prices. According to the special wholesale price index compiled by the Bank of Greece, raw material prices declined substantially in 1975. Despite the unfavourable wage and price developments, prices of finished manufactures did not accelerate in 1976.

## 7. PRICE DEVELOPMENTS

The rate of inflation continued to decelerate throughout 1976. The slowdown of inflation was first observed in the consumer price index during the early months of 1976. By way of contrast, the rate of increase of the wholesale price index began to accelerate during the fourth quarter of 1975, continued into the second quarter of 1976 and began to decelerate



ate as of May 1976. However, the extent of the deceleration of price rises is not clearly discernible if we compare the average price levels of the last two years. This is explained by the fact that during the later months of 1975 price indices exhibited substantial increases. As a result, the average price level showed an increase despite the price slowdown which occurred particularly during the last months of 1976. The difference between the rate by which prices rose through the year and the average annual change in the price



level was more pronounced in the case of the wholesale price index. This is explained by the fact that the 1975 acceleration of wholesale prices continued through the first months of 1976.

The consumer price index increased by 11.7 per cent in 1976 and 15.7 per cent in 1975. Thus, the 1976 inflation rate was close to the 10 per cent target rate set by the government at the beginning of the year. Considering that the average price increases in the European OECD countries and the EEC were 11.2 and 10.7 per cent respectively, it becomes evident that the Greek authorities were successful in their overall effort to contain inflation within tolerable limits. It is also noteworthy that Greece's inflation rate in 1976 (see diagram on p. 34) was much lower than the inflation rate in other Southern European countries, or for that matter in some of the more advanced OECD countries. Greece's achievement in bringing down the inflation rate assumes added importance if we take into account that it was accompanied by a substantial increase in real national income and by a fundamental structural change in the factors determining price formation. Price increases of imported goods, for example, weighed more heavily in determining the 1975 inflation than they did last year. Indeed, factors of domestic origin were dominant in the 1976 price rises.

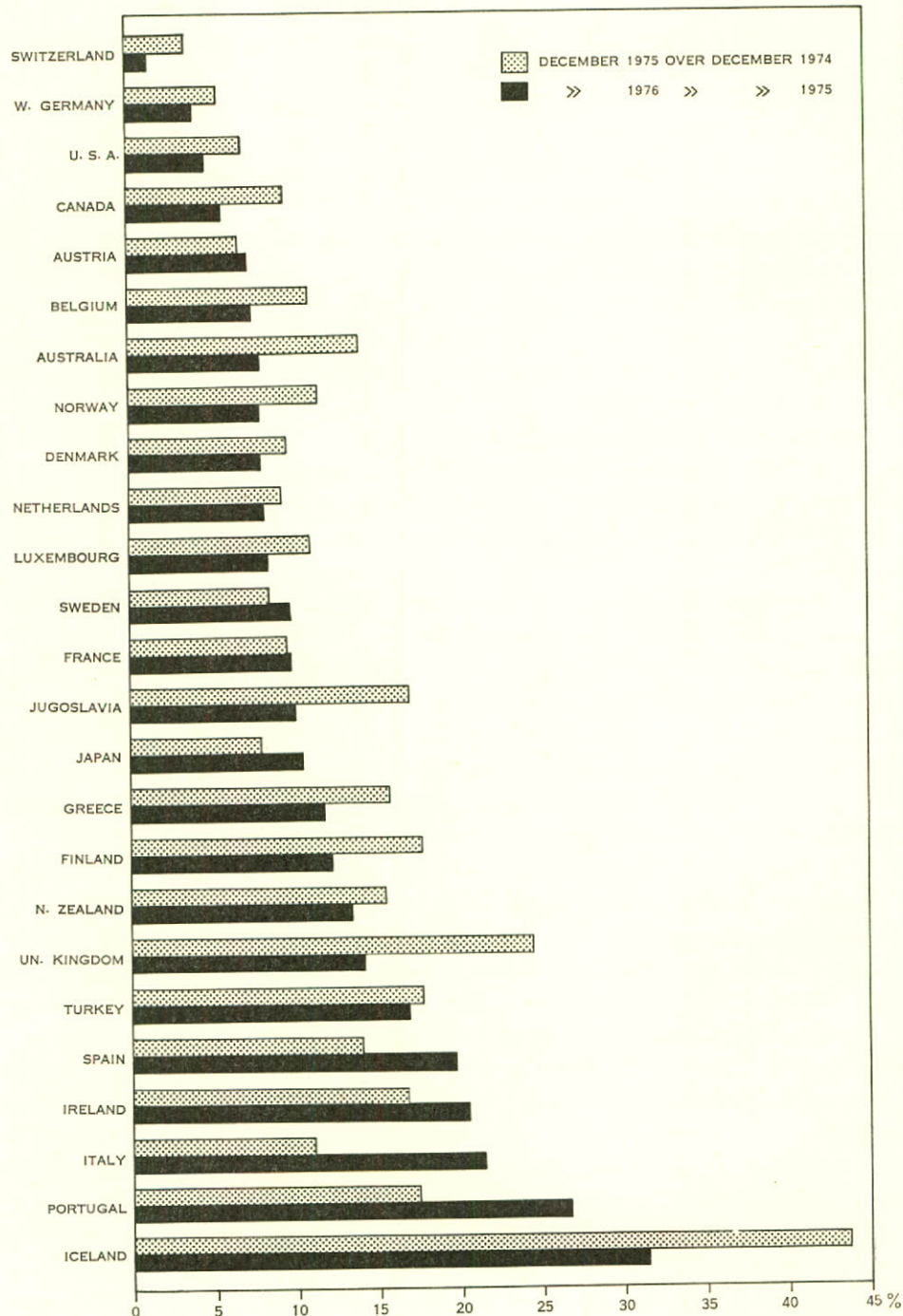
Increased unit labour cost was the main cause of the increase in prices in 1976, followed by higher prices of agricultural commodities, which increased faster than in 1975. Prices of imported goods, expressed in foreign exchange, increased less rapidly than in 1975, while the effect of the change in the drachma parity on the price level was weaker than in 1975.

The difference between the rate by which consumer prices increased in 1976 and 1975 is attributed mainly to the price increase in services (1976: 12.7 per cent; 1975: 21.1 per cent) and foodstuffs (1976: 11.5 per cent; 1975: 15 per cent). The rate of price increase of all other commodities decelerated in 1976 with the exception of footwear, clothing and final durable consumer goods. Compared with 1975, the latter recorded higher price rises in 1976. It should be mentioned that goods and services, whose prices advanced at a slower pace last year, represent approximately four fifths of the family budget in Greece and include items that are under government price regulations. Conversely, prices of footwear, clothing and final durable consumer goods were set by the market and, in most cases, they increased more rapidly. It can therefore be argued that the deceleration of inflation was, in large part, due to the government's price control policy. Higher indirect taxes and necessary price adjustments of certain items under government price control in 1975 led to an acceleration in the rate of inflation over a certain period of time.

As previously stated, wholesale prices rose sharply during the last quarter of 1975 and the first months of 1976. These prices increased by 7.0 per cent in the second half of 1975 and by 8.3 per cent in the first four months of 1976. The upward price trend was, however, checked in the following months. Thus, in the May-December 1976 period price rises slowed down to 6.4 per cent or to a monthly average of 0.8 per cent. The increase of the wholesale price index was greater in 1976 (15.2 per cent) than in 1975 (10.1 per cent). Developments in the last months of 1976 and in the beginning of 1977 suggest that a price slowdown is clearly under way.

It is worth noting that the upward trend of wholesale prices did not greatly affect consumer prices. A correlation of short-term changes in the two indices (after eliminat-

PERCENTAGE CHANGES IN THE CONSUMER PRICE  
INDICES OF OECD COUNTRIES





ing changes in the prices of services from the consumer price index) supports this view. Actually, the fact that changes in wholesale prices were not passed on to the consumer price index is largely explained by differences in the composition of the two indices. More specifically, the increase in wholesale prices originated in agricultural products, particularly certain foodstuffs, which have smaller weights in the general consumer price index.

The wholesale price index increased by 15.2 per cent in 1976 compared with 10.1 per cent in 1975. This acceleration was chiefly caused by price increases of agricultural and livestock products, especially exportables, amounting to 3.7 percentage points out of the recorded 5.1 percentage points incremental difference. Prices of "products of domestic primary production for home consumption" increased by 15.7 and 14.6 per cent in 1976 and 1975 respectively. Prices of "domestic industrial products for home consumption" increased by 10.2 and 8.6 per cent. In contrast, prices of "exportable primary and industrial products" increased much faster in 1976 (42.0 per cent) compared with 1975 (3.8 per cent). The same upward trend was observed in the case of prices of "products of foreign origin" (1976: 13.9 and 1975: 7.9 per cent). The acceleration of the rate of increase in the prices of the last two groups explains more than 80 per cent of the difference of the wholesale price index increase between 1976 and 1975. In addition to agricultural and livestock exportables and imports, these two groups include metals, textiles (whose high prices were determined by world markets), transportation equipment, petroleum products, machinery and electrical equipment, wood products, etc.

### III. MONETARY DEVELOPMENTS

#### 1. CHANGES IN THE LIQUIDITY OF THE ECONOMY

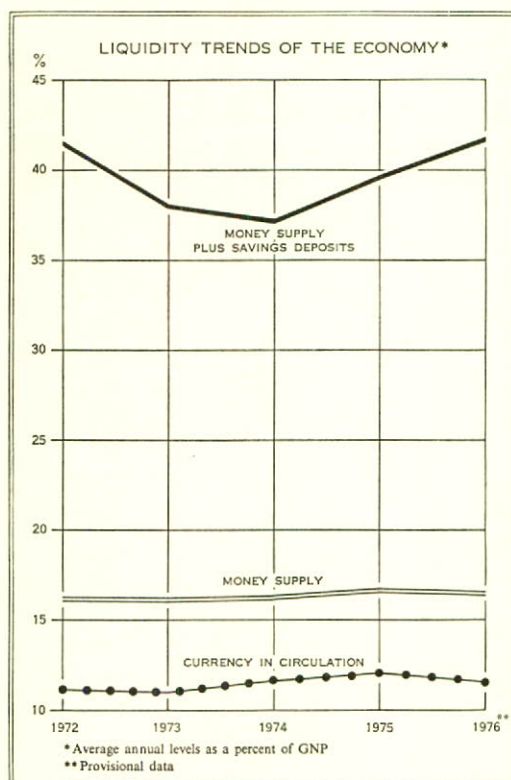
##### a. Money Supply

Money supply, which includes currency in circulation and sight deposits, increased by 24.3 per cent in 1976, compared with a growth of 15.6 per cent in 1975. Specifically, currency in circulation increased by 22.1 per cent in 1976 and sight deposits by 29.5 per cent. In this context, it should be stressed that the variations in the annual rates of change of currency in circulation in recent years were affected, to a large extent, by

frequent conversions of private deposits into cash and vice versa, caused by non-economic factors. Generally, the rate of increase of liquid assets, which basically corresponds to the sum of these two magnitudes, is particularly high.

As regards sight deposits, the acceleration in their rate of growth in 1976 was entirely due to an increase in deposits of public enterprises and entities. The increase in deposits of public enterprises occurred in the last months of 1976, was of a temporary nature, and was chiefly caused by the Public Power Corporation's placement of foreign loans proceeds in current accounts. The increase in public entities' sight deposits represents surpluses of current revenues over expenditures, which are eventually transferred into deposits of longer maturity.

Private sight deposits increased in 1976 as well at a relatively high rate, which was only slightly lower than that of 1975. At the same time, private firms continued to economize cash as can be seen from the private sight deposits' velocity of circulation, which



increased in 1976 as well. This policy was facilitated by the capability of chiefly small and medium size firms, to place their liquid reserves provisionally in savings deposits. These deposits cannot only be withdrawn on demand (without any advance notice or other restrictions), but can also be transferred almost automatically into sight deposits. In practice, this means that there is a high degree of substitutability between money and savings deposits. It should be noted that the ratio of withdrawals to total outstanding savings deposits balances with commercial banks (which hold the largest share of bank



## CHANGES IN MONEY SUPPLY

	Balances outstanding on 31 Dec. 1976 (million drachmas)	Annual changes					
		Million drachmas			Percentage		
		1974	1975	1976	1974	1975	1976
Currency in circulation	111,921	15,353	11,435	20,274	23.7	14.3	22.1
Sight deposits	48,237	2,983	5,978	10,998	10.6	19.1	29.5
Private	(28,438)	(972)	(4,022)	(4,424)	(5.1)	(20.1)	(18.4)
Public entities	(15,339)	(853)	(2,207)	(4,297)	(10.7)	(25.0)	(38.9)
Public enterprises	(4,460)	(1,158)	(-251)	(2,277)	(90.7)	(-10.3)	(104.3)
Money supply	160,158	18,336	17,413	31,272	19.7	15.6	24.3

deposits of private firms) has been increasing in recent years. This ratio is already three times as high as the equivalent ratio for the Postal Savings Bank. Day-to-day movements of bank deposits also provide concrete evidence of large-scale transfers between sight and savings deposits.

*b. Short-run Developments in Monetary Variables*

As in 1975, the pattern of short-term developments in monetary variables was also of interest in 1976. Specifically, the rates of change of seasonally adjusted quarterly data for currency in circulation and private bank deposits exhibited large fluctuations in the course of the year. However, the fluctuations in total liquid assets—which are the sum of these two magnitudes—were not of the same size. These large fluctuations are attributed to conversions of savings deposits into currency.

Developments in the first two months of 1976 were marked by an inflow of liquid assets into the banking system, which in 1975 had been kept in cash. As a result of the increase in the liquidity of commercial banks, their accounts with the Bank of Greece improved and currency in circulation fell during the first months of 1976. In the course of the next few months, the increased liquidity of commercial banks financed their credit expansion, which, in combination with the ensuing retardation in the rate of growth of deposits, led to a higher pace of expansion of currency in circulation. The largest increase in currency in circulation occurred in July and August, chiefly as a result of the Aegean crisis which led to withdrawals of deposits and made banks dependent on the Bank of Greece. Following that crisis, as of September 1976 the high cash balances started flowing into banks. During this period, the monetary authorities took measures to curtail commercial bank liquidity, aiming at restricting the rate of increase in the extension of commercial bank credit. As a result of these measures, the rate of increase of currency in circulation slowed down during the last months of 1976.

*c. Income Velocity of Currency Circulation*

Developments in the income velocity of currency in circulation and money supply for the period 1970-1976 are presented in the following table:

INCOME VELOCITY OF : <sup>(1)</sup>

Years	Currency circulation	Money supply
1970	8.79	6.32
1971	8.88	6.25
1972	8.97	6.21
1973	9.06	6.20
1974	8.64	6.17
1975	8.34	6.01
1976	8.73	6.16

<sup>(1)</sup> Ratio of gross national product at current market prices to the average annual level of currency circulation or money supply.

Variations in the annual change of income velocity, in recent years, cannot be explained solely in terms of shifts in the demand for money caused by economic factors. They should mostly be attributed to frequent changes in the form of holding liquid assets for non-economic reasons. Despite these influences, which, to a large extent, persisted in 1976 as well, the figures in the table clearly show a downward trend in the income velocity, both of currency in circulation and of money supply, which follows the slowdown of inflation. This development shows that the demand for money is significantly affected by the inflationary expectations prevailing in the economy.

#### *d. Total Liquidity of the Economy*

Under present conditions, changes in the economy's liquid assets are perhaps a better indicator (compared with other monetary variables) of developments in the monetary sector. This is based mainly on the fact that there is a high degree of substitutability between the different categories of liquid assets. Savings deposits, which constitute the greater part of private bank deposits, have a high degree of liquidity as they can be withdrawn without advance notice or other restrictions. It must also be added that their liquidity, in recent years, has increased owing to the apparently widespread banking practice of transferring, almost automatically, savings into sight deposits. This is the reason why monetary authorities focus their attention, more than in the past, on developments in liquid assets and are basically trying to promote the channelling of private savings into investment via the capital market.

In 1976 total liquid assets, i.e., currency in circulation and total private drachma deposits, excluding deposits in blocked accounts, increased substantially. The high rate of increase in time and savings deposits, for the second year in succession, can be largely attributed to the slowdown of inflation. The increase in deposits is also due to some other factors which are examined in the relevant section of this Report. As a result of these developments in 1976, there was an increase in the economy's total liquidity, i.e., a rise of the liquid assets to GNP ratio.

Liquidity had been continuously increasing in the postwar period and reached its peak in 1972 (45.8 per cent). During the high inflation period (1973-1974), liquidity was reduced substantially (42 per cent). Since 1975, liquidity has been rising again. In 1976 liquidity increased at a slower pace and it reached the level of 46.7 per cent, which is higher than that of 1972.



LIQUIDITY OF THE ECONOMY :  
RATIOS OF LIQUID ASSETS IN THE PRIVATE SECTOR TO GROSS NATIONAL PRODUCT

	1971	1972	1973	1974	1975	1976
1.(a) Money supply ( $M_1$ ) as a percentage of GNP	0.141	0.142	0.143	0.145	0.148	0.143
(b) Percentage change compared with previous year	—	+0.7%	+0.7%	+1.4%	+2.1%	-3.4%
2.(a) Money supply plus private time and savings deposits in drachmas ( $M_3$ ) as a percentage of GNP	0.425	0.458	0.421	0.419	0.456	0.467
(b) Percentage change compared with previous year	+9.0%	+7.8%	-8.1%	-0.5%	+8.8%	+2.4%

Note : In assessing liquidity ratios, monetary aggregates are taken at average annual levels. Furthermore, money supply is here taken to include private sight deposits only.

Empirical evidence of recent years, especially in 1973, suggests that during periods of inflationary expectations high liquidity constitutes an autonomous inflationary factor. The rapid price increase, observed in 1973, adversely affected the demand for liquid assets, especially bank deposits. The existence of a large amount of liquid assets in the public's hands is a potential source of inflation, for it can exert pressure on aggregate demand, thereby strengthening the inflationary process. The experience of recent years shows that savings deposits are particularly sensitive to sudden changes in the growth rate of prices.

## 2. FACTORS AFFECTING MONEY SUPPLY

The increase in money supply in 1976 was primarily caused by the public sector and, to a lesser extent, by the private sector. Conversely, the foreign sector had a contractionary effect on the money supply.

The extensive borrowing requirements of the public sector were the main influence behind the increase in money supply in recent years. The resulting public sector deficits during the recession and/or the beginning of the upturn in the economy were largely cyclical in nature. However, following the recession, the policy to revive economic activity was primarily based on fiscal measures and, especially, on the expansion of public investment programmes. Efforts were also made by the government to improve agricultural incomes through increased subsidies, which led in turn to substantially larger deficits. Finally, the demand for bank financing of public enterprises has increased in recent years, as their own funds could only finance a small part of their total investment budget. This was due to the fact that price increases of goods and services which public enterprises provide did not keep up with rising operating costs.

Taking into account that credit requirements of the private sector absorb the largest share of private savings channelled into the credit system, the financing of the public sector deficit leads in general to an expansion of the monetary base and of the economy's liquidity. This reduces the effectiveness of monetary and credit policy. It must be stressed that the state of affairs appears to have worsened in 1976, owing to the fact that the private sector also exercised an expansionary effect on the money supply.

**FACTORS AFFECTING MONEY SUPPLY**  
(+) Money supply increase (—) Money supply decrease  
(Million drachmas)

Sectors	1975	1976 <sup>4</sup>
<b>A. PUBLIC SECTOR</b> .....	<b>+38,216</b>	<b>+39,226</b>
<i>I. Central Government (excluding foreign borrowing) (a)</i> .....	<i>+36,123</i>	<i>+40,332</i>
1. Loans and advances .....	+ 8,400	+ 17,389
2. Treasury bills .....	+ 12,244	+ 32,254
3. Bonds .....	— 142	— 118
4. Deposits .....	— 1,222	— 5,629
5. Other accounts <sup>1</sup> .....	— 4,393	— 7,329
6. Foreign borrowing .....	+ 21,236	+ 3,765
<i>II. Public entities</i> <sup>2</sup> .....	<i>— 3,785</i>	<i>— 7,967</i>
1. Local authorities .....	— 712	+ 894
2. Social security .....	— 2,329	— 6,235
3. Other .....	— 744	— 2,626
<i>III. Public enterprises</i> .....	<i>+ 5,878</i>	<i>+ 6,861</i>
1. Loans and advances .....	+ 5,616	+ 6,887
2. Bonds .....	+ 262	— 26
<b>B. PRIVATE SECTOR</b> .....	<b>— 3,659</b>	<b>+11,369</b>
<i>I. Loans and advances</i> .....	<i>+59,594</i>	<i>+75,183</i>
1. Agriculture .....	+ 12,151	+ 13,483
2. Manufacturing .....	+ 30,852	+ 32,048
3. Other .....	+ 16,591	+ 29,652
<i>II. Securities</i> .....	<i>+ 2,271</i>	<i>+ 3,922</i>
<i>III. Deposits</i> .....	<i>—65,524</i>	<i>—67,736</i>
1. Savings .....	— 47,466	— 51,111
2. Time <sup>3</sup> .....	— 12,618	— 20,230
3. Restricted .....	— 5,440	+ 3,605
<b>C. FOREIGN SECTOR</b> .....	<b>—26,604</b>	<b>—25,956</b>
1. Change in foreign exchange reserves .....	+ 7,639	+ 5,294
2. » » clearing accounts .....	+ 1,024	— 1,920
3. » » foreign exchange sight liabilities .....	— 5,486	— 10,230
4. Change in long-term foreign exchange liabilities .....	— 21,236	— 3,765
5. Change in foreign exchange deposits by Greek workers and seamen .....	— 8,545	— 15,335
<b>D. OTHER ITEMS</b> .....	<b>+ 9,458</b>	<b>+ 6,633</b>
<b>CHANGE IN MONEY SUPPLY</b> .....	<b>+17,411</b>	<b>+31,272</b>
1. <i>Currency in circulation</i> .....	<i>+11,435</i>	<i>+20,274</i>
a) Bank notes .....	+ 11,118	+ 19,844
b) Coin .....	+ 317	+ 430
2. <i>Sight deposits</i> .....	<i>+ 5,976</i>	<i>+10,998</i>
a) Private .....	+ 4,022	+ 4,424
b) Public entities .....	+ 2,207	+ 4,297
c) Public enterprises .....	— 253	+ 2,277
 (a) Analysis of Central Government		
1. Current expenditures .....	+ 3,920	— 8,785
2. Investment expenditures .....	+ 29,938	+ 36,561
3. Consumer goods account .....	+ 6,595	+ 16,480
4. National Tobacco Org.-Autonomous Currants Org.-Cooperative Sultana Associations.....	+ 1,300	+ 2,448
5. Other .....	— 5,630	— 6,372

(<sup>1</sup>) Coin in circulation and other government credit accounts.

(<sup>2</sup>) Not including investment in treasury bills totalling Dr. 3,982 million for 1975 and Dr. 1,246 million for 1976, shown as a receipt item under Central Government - Other. Also not including investment in bank shares totalling Dr. 4,070 million for 1976, shown as a contractionary effect under Other Items.

(<sup>3</sup>) Including short-term bank bonds issued by special credit institutions (1975 : Dr. 246 million; 1976 : Dr. 2,742 million.

(<sup>4</sup>) Provisional data.



In 1976, the various sectors of the economy had the following impact on money supply:

The public sector, broadly defined<sup>1</sup>, had an expansionary effect of Dr. 39,226 million in 1976 compared with Dr. 38,216 million in 1975. This change was basically caused by the Central Government and public enterprises. Public entities in 1976 recorded a higher surplus.

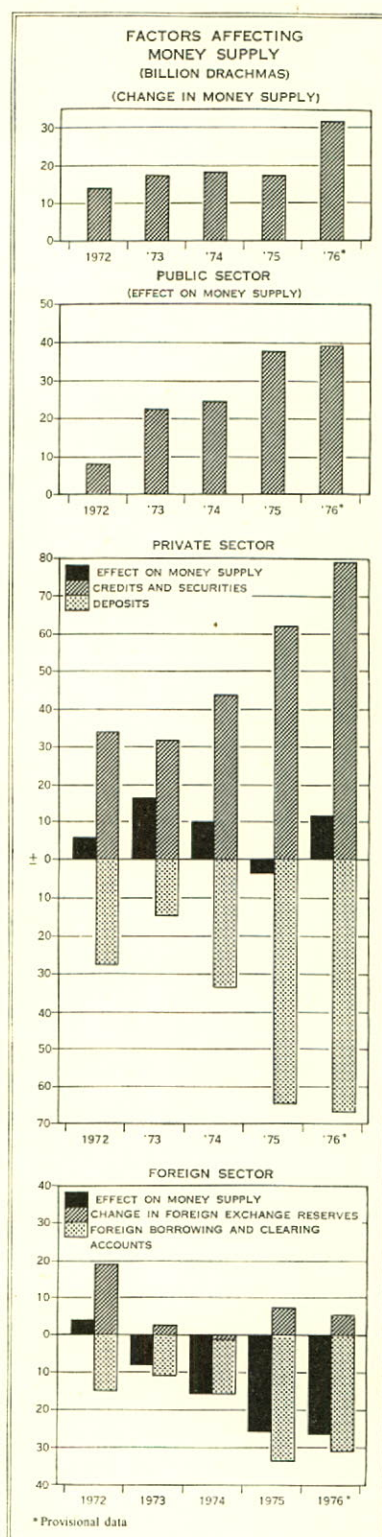
Central Government accounts (the ordinary budget, the public investment budget, the consumer goods account and the various other accounts for government purchases of agricultural products) led to an increase in money supply of Dr. 40,332 million (1975: Dr. 36,123 million). This was due to larger disbursements for public investment and agricultural income support schemes.

Specifically, the Central Government's accounts with the Bank of Greece show a surplus in the ordinary budget for 1976 that had a contractionary effect of Dr. 8,785 million on the money supply in contrast to an expansionary effect of Dr. 3,920 million in 1975. The public investment budget deficit amounted to Dr. 36,561 million in 1976 (1975: Dr. 29,938 million) and exerted an equivalent expansionary effect on the money supply.

The expansionary effect of the consumer goods account on the money supply in 1976 was substantially higher (1976: Dr. 16,480 million; 1975: Dr. 6,595 million), owing to both increased payments and reduced receipts.

Similarly, the financing of the National Tobacco Organization, the Autonomous Currants Organization and the Cooperative Sultana Associations also contributed to the expansion of the money supply (1976: Dr. 2,448 million; 1975: Dr. 1,300 million). Public entities, that is, social security agencies, local authorities, etc. had, however, a contractionary effect on the money supply in both years (1976: Dr. -7,967 million; 1975: -3,785 million). Moreover, in the last two years, public entities invested part of their surplus funds in treasury bills. In 1976 they purchased Dr. 4,070 million of Commercial Bank of Greece shares. If these investments are taken into account (Dr. 5,316 million in 1976 and Dr. 3,980 million in 1975), then the

(<sup>1</sup>) Including Central Government, public enterprises and public entities.



surplus of public entities can be said to have increased substantially in 1976.

Public enterprises had an expansionary effect of Dr. 6,861 million on the money supply in 1976, compared with Dr. 5,878 million in 1975. The increase recorded in 1976 was due to investment outlays, while the level of self-financing remained unchanged.

The private sector of the economy exerted an expansionary effect of Dr. 11,369 million on the money supply in 1976, compared with a contractionary effect of Dr. 3,659 million in 1975. Considering further that the difference in these two years was substantial (amounting to Dr. 15,028 million), the higher pace by which money supply grew in 1976 could be partly attributed to the private sector. This sector's effect on the money supply differed in 1976, as compared with 1975, in the sense that credit expansion, chiefly by commercial banks, continued at a high rate while the rate of inflow of private deposits into the banking system decelerated. As analyzed in the following chapter, the rate of credit expansion to the private sector in 1976 was as high as in 1975 (approximately 25 per cent). Thus, if domestic private savings channelled into the banking system (Dr. 67,736 million) are subtracted from the total credit increase that went to the private sector (Dr. 75,138 million), it can be shown that part of the bank financing of this sector ultimately exerted a pressure on the money supply. Credit expansion to the private sector was facilitated by high commercial bank liquidity caused by the increase in foreign exchange deposits. Moreover, the uneven distribution of private savings among the various types of credit institutions undoubtedly led to the financing of certain activities of the private sector by the Bank of Greece.

The foreign sector of the economy — excluding the proceeds of public sector borrowing from abroad and the change in the outstanding balance of foreign exchange deposits — had a contractionary effect on money supply (1976: Dr. -25,956 million; 1975: Dr. -26,604 million<sup>1</sup>).

The foreign sector's effect on the money supply remained basically unchanged during the last two years, reflecting the fact that the current account deficit remained at approximately the same level.

(<sup>1</sup>) Note that the effect exerted by the foreign sector on the money supply, as presented in the above analysis, differs from the one resulting from changes in the Bank of Greece official reserves. While public sector borrowing abroad and foreign exchange deposits are converted into drachmas, they are also added to the official reserves. However, these loans and deposits are not counted as an effect on the money supply caused by the foreign sector, but are included in the effect of Central Government and the private sector of the economy respectively. Moreover, the analysis of the factors affecting the money supply takes into account the changes in foreign exchange reserves held by commercial banks.



## IV. CREDIT DEVELOPMENTS

### 1. MONETARY AND CREDIT POLICY MEASURES

The aim of monetary and fiscal policy in 1976 was to boost the economy's upturn, which began early in 1975, within limits consistent with the targets of restraining inflation and attaining equilibrium in the country's external transactions. The formulation of this policy was, to a significant extent, influenced by the fluctuations in private bank deposits, the lack of clear indications in the beginning of the year concerning the stability of the economic recovery and, finally, by the *ex post* magnitude of the public sector deficit compared with initial forecasts.

The monetary authorities' initial aim was to attain a sizable slowdown in credit expansion in 1976. In the first quarter of the year, during which demand for credit is seasonally low, a substantial part of the increase in commercial bank liquidity — created by new deposits — was placed as reserves with the Bank of Greece. The rise in reserves was substantial as a result of the sizable inflow of private deposits, which occurred in the first two months of 1976.

During the second quarter of the year, the seasonally high demand for bank credit occurred concurrently with a substantial slowdown in the rate of increase in deposits. In this quarter the increase in bank lending was financed by the banks' free reserves, which were accumulated in the Bank of Greece during the first two months of 1976. As a result of the Aegean crisis, the rate of increase in deposits slowed down further in July and August. During this period the Bank of Greece strengthened the commercial bank reserve position aiming at preventing the disruption of production and productive investment and at meeting the borrowing requirements for the marketing of various agricultural products. Following the easing of the Aegean crisis, the rate of increase of private deposits accelerated and bank liquidity was restored to a level permitting a substantial increase in bank lending. Concurrently, the monetary authorities in order to curtail the expansion of bank lending enforced seasonal reserve requirements on commercial bank deposits. As a result, the Bank of Greece absorbed funds amounting to Dr. 7,700 million. At any rate, large fluctuations in the rate of increase of bank deposits throughout the year significantly constrained the ability of the monetary authorities to control the expansion in commercial bank credit.

The lenience exhibited by the monetary authorities in the beginning of the year contributed to an increase in credit expansion beyond the originally designated limits. This lenience was determined by the prevailing uncertainty, in the spring of 1976, concerning the stability of economic recovery. The uncertainty was created by the sluggish performance of certain leading economic indicators. The hesitancy of the monetary authorities to take tighter credit measures was also due to expectations that the budget would be less expansionary than the original forecast at the time of its submission (end of 1975).

Finally, a basic factor which contributed to the substantial increase in bank lending in 1976 was the increase in foreign exchange deposits, which led to a sizable and largely



unforeseen increase in commercial bank liquidity. The increase in commercial bank funds from this source exceeded by approximately Dr. 8 billion the initial forecast of the monetary authorities. Thus, the only way to curtail credit expansion was to extend the minimum legal reserve requirements to foreign exchange deposits as well.

The principal monetary and credit policy measures, which were taken towards the end of 1976 and are expected to affect credit developments much more in 1977, are the following :

a) Seasonal reserve requirements were imposed on commercial banks in the last quarter of 1976. These compulsory reserves expressed as a per cent of private deposits increased from 1 per cent in October to 2.5 per cent in November and 3.5 per cent in December 1976. As a result, commercial bank liquidity was curtailed by Dr. 7,700 million.

b) Compulsory commercial bank reserves with the Bank of Greece and investments in treasury bills and government bonds were increased and extended to foreign exchange deposits as well. These measures were to take effect from the beginning of 1977. Specifically, commercial banks were obliged to : (i) deposit with the Bank of Greece 7 per cent of the increase in their drachma and foreign exchange deposits; (ii) invest in treasury bills or government bonds 30 per cent of the increase in their drachma and foreign exchange deposits; (iii) make an additional withholding of 15 per cent of the increase in current deposits until the balance of the commercial bank deposits at the end of 1976 meets the newly established reserve requirements and the appropriate portion invested in treasury bills and government bonds.

These measures are expected to ensure effective control of commercial bank liquidity and to restrain credit expansion in 1977 within limits consistent with the general targets of economic policy. As a result of the above measures taken by the monetary authorities, only 48 per cent of the increase in commercial bank deposits will be available for financing credit expansion.

c) As of November 1976, interest rates on drachma deposits were reduced by half a percentage point. Specifically, the interest rate on savings deposits with commercial banks was set at 7 per cent, for deposits with the Agricultural Bank at 7.25 per cent and for deposits with the Postal Savings Bank at 7.5 per cent. Interest rates on time deposits were set at 8.5 to 9.5 per cent, depending on maturities.

d) Beginning with 1977 interest rates on credits were increased by half a percentage point. Certain classes of loans were specifically exempted from this increase: long-term loans for productive investment; housing loans for workers and low income people and civil servants, etc. At the same time, the rediscount rate was increased from 10 per cent to 11 per cent along with the interest charged on commercial bank overdrafts on their current account with the Bank of Greece. The latter varies from 12 per cent to 14.5 per cent depending on the duration of the overdraft.

e) As of 1977 the interest rate on savings deposits in foreign exchange was reduced by half a percentage point; and by 1 percentage point on foreign exchange time deposits of Greek emigrants and seamen. These interest rates had remained unchanged since 1974, even though equivalent interest rates in the countries of origin of these deposits had fallen substantially in the last two years.

f) Beginning with 1977, interest rates on treasury bills were reduced by 1.5 percentage points. The new rates were set at 7.75 to 8.25 per cent.



The above-mentioned measures are expected to have a positive effect on commercial bank profitability despite the increases in reserve requirements.

In order to encourage the acceptance of private deposits by the Agricultural Bank, it was decided to subsidize the interest rate cost by 3.5 percentage points since the beginning of 1976.

Apart from the above, the monetary authorities took additional and more specific measures in order to harmonize previous decisions with the newly created conditions and to tackle problems which had arisen in the course of the year. The most important of these measures are the following: Ceilings on ordinary private housing loans were increased from Dr. 300,000 to Dr. 500,000 and on housing loans to civil servants and employees of public enterprises from Dr. 700,000 to Dr. 900,000. This was deemed essential because of increased housing prices in the last two years.

Long-term bank loans were extended to firms to help them pay the "special tax levy" in accordance with the provisions of Law 257/1976. The ceiling on loans to firms in small-scale industry was increased from Dr. 500,000 to Dr. 1 million for the purchase of new premises.

Favourable conditions were established for the financing of firms located in border regions. Also housing loans per person extended by the Agricultural Bank in the same regions were increased from Dr. 55,000 to Dr. 150,000. Ceilings were also increased on personal credit card loans from Dr. 25,000 to Dr. 40,000. Quota ceilings allocated per bank for loans of this category were also increased.

## 2. BANK CREDIT

### *a. Credit by Major Sector*

Bank credit continued to expand at a high rate in 1976. The outstanding balance of bank credit to the private and public sectors increased by Dr. 86,174 million or 24.4 per cent

BANK CREDIT TO THE ECONOMY BY SECTOR

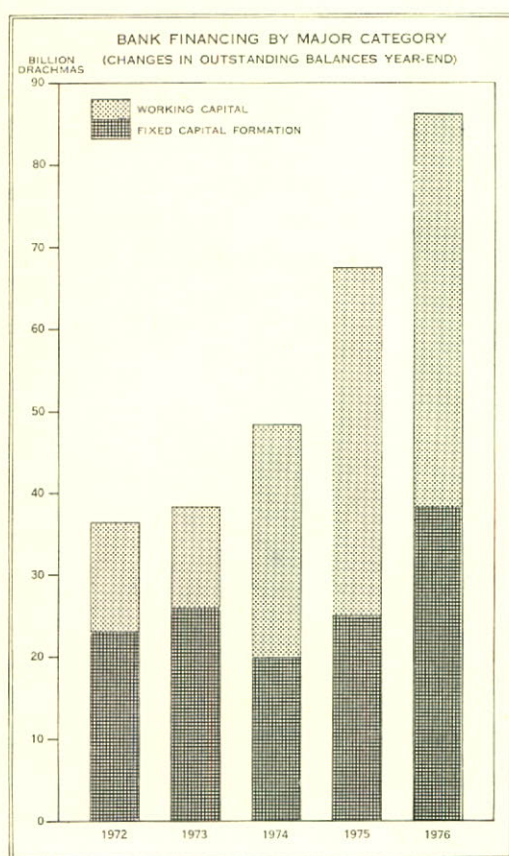
Sectors financed	Outstanding balances on 31 Dec. 1976 (million drachmas)	Changes in outstanding balances at year-end					
		Million drachmas			Percentage		
		1974	1975	1976	1974	1975	1976
PRIVATE SECTOR	378,006	+40,630	+59,593	+75,183	+20.1	+24.5	+24.8
Long-term credit	165,166	+14,449	+18,693	+29,782	+14.1	+16.0	+22.0
Short-term credit	212,840	+26,181	+40,900	+45,401	+26.1	+32.3	+27.1
PUBLIC SECTOR	61,961	+7,930	+7,915	+10,991	+22.6	+18.4	+21.6
Public enterprises	37,506	+5,649	+5,615	+6,888	+29.2	+22.5	+22.5
Public entities	14,363	— 99	+1,000	+1,655	— 0.8	+8.5	+13.0
Government agencies purchasing agricultural products	10,092	+2,380	+1,300	+2,448	+60.0	+20.5	+32.0
Total	439,967	+48,560	+67,508	+86,174	+20.4	+23.6	+24.4

compared with an increase of Dr. 67,508 million or 23.6 per cent in 1975. However, deducting from this sum total the loans granted to private firms in 1976 to facilitate the payment of the special tax levy, as stipulated by Law 257/1976, the rate of increase of bank credit drops to 22.1 per cent.

Bank credit to the private sector of the economy (including the "special tax levy" loans) increased in 1976 by approximately the same rate (24.8 per cent) as in 1975. Excluding the "special tax levy" loans, bank credit to the private sector increased by 22.2 per cent. Comparing developments in bank lending with those in GNP, prices and business investment, it can be concluded that credit requirements of the various sectors and branches of the economy financed by the banking system were amply covered. This conclusion still holds taking into account that

wages and raw material prices increased at a faster pace in 1976 compared with prices of industrial products. Part of the increase in bank credit has, however, been used for financing inventory accumulation and for expanding credit extended to traders by industrial firms, beyond the necessary requirements for the marketing of their products. This extension of credit along with the diversion of credit to less desirable activities contributed to an increase in demand in 1976, as had happened during the previous year. Moreover, in many cases the substantial increase in bank lending led to the substitution of loans in drachmas for foreign currency loans. Finally, credit expansion exceeded the capital requirements of the agricultural sector as well. In this sector, for many years, short-term credit has been increasing at a pace faster than the increase in the gross value of agricultural production.

As was stressed in last year's Report, beginning with the last quarter of 1974 credit expanded at a rate higher than the increase in production and prices and has contributed



to the increase in home demand. It should not, however, be overlooked that the use of credit policy to boost the upturn in the economy can have serious economic implications if it is excessive. In such a case it may lead to an undesirable increase in the economy's liquidity, which is a potential source of inflation. At the same time, it can have severe repercussions on the financial condition and the competitiveness of many firms and can lead to an irrational distribution of economic resources. These effects can occur because excessive credit expansion encourages consumption and imports, nurses inflationary expectations and strengthens speculative tendencies in the economy. For these reasons,



the recourse to credit policy as a means of boosting demand must be confined within certain limits and must primarily have a time constraint.

Bank credit to public enterprises, public organizations and government agencies purchasing and marketing agricultural products increased by Dr. 10,991 million in 1976 (21.6 per cent), compared with an increase of Dr. 7,915 million in 1975 (18.4 per cent). Of this total, bank credit to public enterprises increased by Dr. 6,888 million in 1976 compared with Dr. 5,615 million in 1975. These loans were used to finance the investment programmes of the Public Power Corporation and Greece's Telecommunications Organization. Moreover, bank credit to public entities increased substantially in 1976, chiefly for financing projects of local authorities (outstanding bank credit increased from Dr. 1,000 million in 1975 to Dr. 1,665 million in 1976).

The 1976 increase of bank credit to special agencies purchasing and marketing agricultural products was almost double that of 1975 (1976: Dr. 2,448 million; 1975: Dr. 1,300 million). The biggest share of this increase was due to the financing of larger tobacco purchases by the National Tobacco Organization (outstanding credit increased by Dr. 1,637 million in 1976, compared with a decrease of Dr. 562 million in 1975). As a result of a fall in the production of currants and increased loan repayments, following a substantial liquidation of stocks accumulated in 1975, outstanding credit to the Autonomous Currants Organization and the Cooperative Sultana Association increased at a much slower pace (1976: Dr. 811 million; 1975: Dr. 1,862 million).

#### *b. Credit by Institution*

The breakdown of credit by institution shows that the rate of increase of commercial bank lending in 1976 was reduced while lending by other financial institutions accelerated.

Commercial bank credit increased by 31.4 per cent in 1976 (or 28.1 per cent excluding the "special tax levy" loans), 33.5 per cent in 1975 and 20.6 per cent in 1974. Credit expansion to the private sector increased by 29.7 per cent in 1976 (or 26.3 per cent excluding the "special tax levy" loans), 30.9 per cent in 1975 and 21.4 per cent in 1974. With the exception of 1975, the rate of increase of bank credit extended to the private sector in 1976 was the highest recorded in the last decade. The substantial credit expansion of 1975 can, however, be justified, as the economy was in the initial stage of an upturn and it was essential to restore liquidity in the business community. Finally, commercial banks increased their holdings of treasury bills and government bonds in 1976 by Dr. 19,081 million (1975: Dr. 14,823 million).

The increase of commercial bank lending was not spread evenly over the course of 1976. On the basis of seasonally adjusted data, the largest increases were recorded in the second and third quarter of 1976 (8.2 per cent and 7.1 per cent respectively). Rates of increase in the first and fourth quarter amounted to 5.2 per cent and 6.7 per cent respectively. These fluctuations were to a significant extent due to the demand for funds by business firms since June 1976, for the payment of the "special tax levy". The fluctuations in commercial bank credit during 1976 were also influenced by developments in



bank deposits as well as by measures taken by the monetary authorities, in the last quarter of the year, to reduce commercial bank liquidity.

Commercial banks also increased their lending to public enterprises by Dr. 4,321 million in 1976 (1975: Dr. 3,886 million). It should be clarified that the financing of public enterprises by credit institutions is decided by the monetary authorities. The financing is within the general framework of the policy pursued to ensure a rational allocation of

## CREDIT TO THE ECONOMY BY INSTITUTION

Credit institution	Outstanding balances on 31 Dec. 1976 (million drachmas)	Changes in outstanding balances at year-end					
		Million drachmas			Percentage		
		1974	1975	1976	1974	1975	1976
<i>Bank of Greece</i>	13,660	+ 1,384	+ 1,901	+ 1,326	+ 15.3	+18.2	+ 10.8
<i>Commercial banks</i>	212,253	+20,626	+40,560	+50,698	+ 20.6	+33.5	+ 31.4
<i>Specialized credit institutions</i>	214,054	+26,550	+25,047	+34,150	+ 20.7	+16.2	+ 19.0
Agricultural Bank	93,996	+12,280	+14,062	+19,102	+ 25.3	+23.1	+ 25.5
National Mortgage Bank	33,333	+ 2,861	+ 4,691	+ 5,958	+ 14.4	+20.7	+ 21.8
Hellenic Industrial Development Bank	22,629	+ 2,172	+ 2,035	+ 1,738	+ 13.0	+10.8	+ 8.3
Postal Savings Bank	40,325	+ 7,044	+ 2,471	+ 4,015	+ 26.3	+ 7.3	+ 11.1
Consignations & Loans Fund	10,558	+ 32	+ 209	+ 566	+ 0.3	+ 2.1	+ 5.7
Private investment banks (National Investment Bank for Industrial Development and Investment Bank S.A.)	11,863	+ 1,915	+ 1,351	+ 2,423	+ 31.0	+16.7	+ 25.7
Mortgage Bank S.A.	1,350	+ 246	+ 228	+ 348	+ 46.6	+29.5	+ 34.7
<b>Total</b>	<b>439,967</b>	<b>+48,560</b>	<b>+67,508</b>	<b>+86,174</b>	<b>+ 20.4</b>	<b>+23.6</b>	<b>+ 24.4</b>

savings accumulated in the banking system to the various sectors of the economy. Certain commercial banks operated under abnormal circumstances in 1976 that led to a fall in their share of total commercial banking activity. As a result, the degree of concentration in the commercial bank sector increased. However, after the restoration of normal operating conditions, and following the increase in the share capital of the second largest commercial bank, appropriate conditions have been created for a reversal of the trend towards higher concentration, for such concentration would have affected the degree of competition in Greece's banking system.

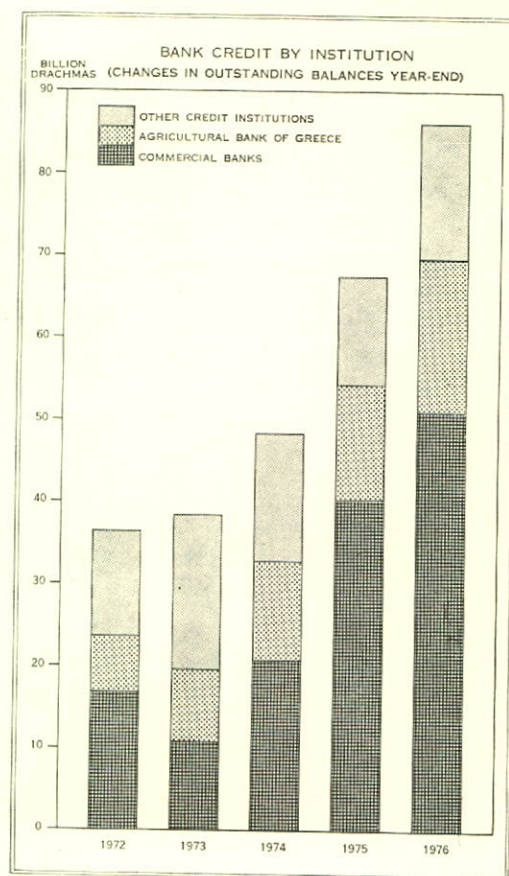
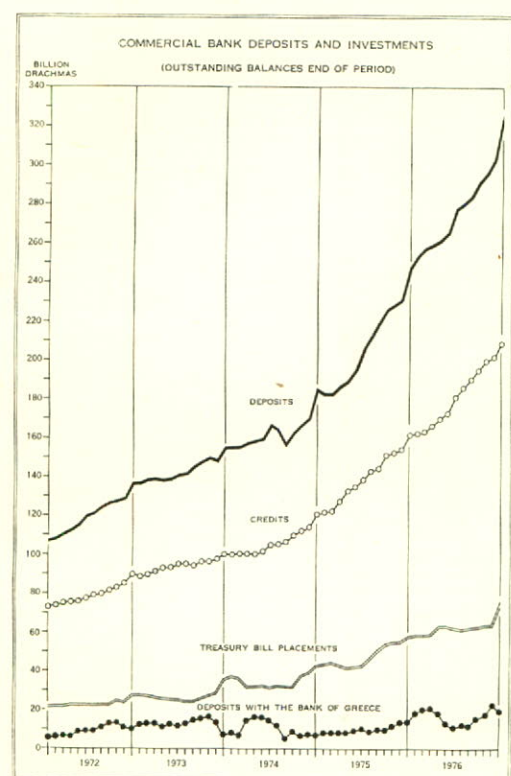
The increase in lending by the Agricultural Bank was substantially higher in 1976 than the previous year (1976: 25.5 per cent; 1975: 23.1 per cent), chiefly reflecting increases in housing loans to farmers and in financing the National Tobacco Organization. Conversely, the rate of increase of credit extended to agriculture declined in 1976, as stated in the relevant section of this Report.

Lending by other special credit institutions accelerated in 1976, with the exception of the Hellenic Industrial Development Bank (HIDB) loans (1976: 8.3 per cent; 1975: 10.8 per cent). Two thirds of the 1976 increase in HIDB loans were due to financing



firms for the payment of the "special tax levy". A substantial part (40 per cent approximately) of the increase in private investment bank lending is also attributed to this reason.

Finally, direct lending extended to the economy by the Bank of Greece increased



at a slower pace in 1976, chiefly as a result of a drop of Dr. 232 million in credit to the Autonomous Currants Organization (1975: Dr. 1,011 million).

### c. Sectoral Breakdown of Credit

Compared with 1975 credit extended in 1976 to trade, housing and tourism showed a high growth rate. Conversely, credit to other sectors of the economy slowed down.

Total credit to industry and mining (excluding the "special tax levy" loans) increased by 23.5 per cent in 1976 (1975: 29.5 per cent; 1974: 25.6 per cent). Even including these loans, the increase in 1976 was smaller than in 1975. A deceleration in the rate of increase of industrial credit was recorded for both working capital loans (1976: 25.9 per cent; 1975: 33.6 per cent) and long-term credit (1976: 19 per cent; 1975: 22.4 per cent).

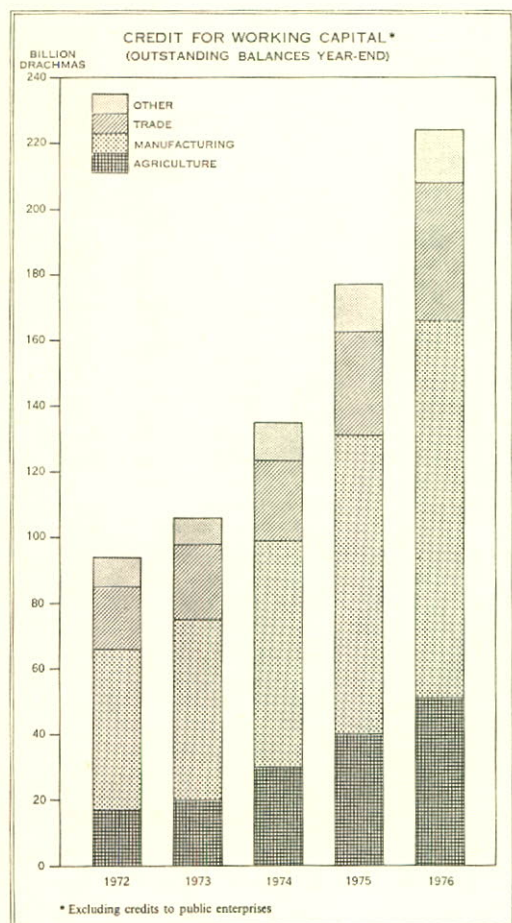
The increase of total long-term credit to industry in 1976 was even smaller, taking

into account the reduction in foreign suppliers' credit for capital equipment imports (1976: \$ 7 million; 1975: \$ 72 million). To assess developments in long-term finance, it should be mentioned that in 1975 this type of finance was specifically exempted from ceilings imposed on other types of credit. This exemption may partly explain the increase in long-term credit in that year. The monetary policy pursued since the autumn of 1974 ensures an ample supply of funds for financing productive investments. Thus, the observed sluggishness of long-term lending reflects the weak demand for funds to finance industrial investment, which persisted during the greater part of 1976.

Short-term credit extended to industry for working capital exhibited a larger deceleration in 1976. The outstanding balance of this type of credit increased by 25.9 per cent (1975: 33.6 per cent; 1974: 28.9 per cent). Average annual levels increased by 28.8 per

cent in 1976 (1975: 33.7 per cent; 1974: 21.3 per cent). It must be pointed out, however, that despite the deceleration in the rate of growth, the increase of short-term industrial credit was quite sizable and was amply sufficient to meet requirements for working capital. This conclusion is confirmed by the fact that credit expansion in 1976 exceeded the corresponding increase in the value of industrial output, estimated at 21.2 per cent.

Drawing upon funds earmarked for low-interest loans and from other bank funds, credit to small-scale industry (handicraft) increased substantially in 1976 (24.9 per cent). The outstanding balance of these low-interest loans increased in 1976 by Dr. 1,458 million or 36.7 per cent (1975: Dr. 1,368 million or 53.5 per cent). It should be noted, however, that despite the substantial increase in low-interest loans to small-scale industry in the last two years, a large part of the earmarked funds has not as yet been absorbed. To ease bank lending, it was decided as of March 1976 to increase the ceiling on business loans from Dr. 500,000 to Dr. 1 million for the acquisition of premises. Similarly, total government guarantees for small-scale industry loans increased from Dr. 2 billion to Dr. 3 billion.



The outstanding balance of credit to agriculture increased by 23.8 per cent in 1976 (1975: 27.3 per cent; 1974 : 32 per cent). The deceleration in the rate of growth reflects a book transfer entry of Dr. 2,280 million that increased the Agricultural Bank's claims on the Government due to price subsidies for agricultural supplies paid chiefly in 1974.



Not taking into account this book transfer, credit to agriculture in 1976 would have increased by 27.8 per cent.

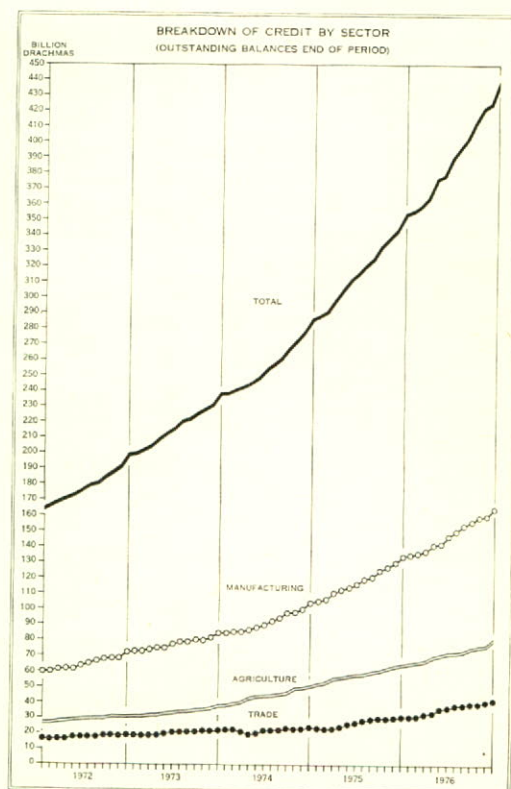
The rate of growth of new advances to agriculture slowed down in 1976 (1976: 22.8 per cent; 1975: 31.2 per cent). This was largely realized in new short-term loans to agricultural organizations and in those loans used for purchasing agricultural supplies. The observed decline in the rate of increase of new advances is, however, more apparent than real, because price increases for fertilizers already bought by the Agricultural Bank are still pending. Conversely, new long-term credit advances to agriculture increased significantly in 1976 (26.7 per cent compared with 5.3 per cent in 1975). This suggests that investment in agriculture is beginning to pick up, especially in livestock production.

For the second year in succession, credit to trade increased at a high rate. Specifically, credit to domestic trade increased by 37.9 per cent in 1976 (1975: 29.6 per cent; 1974: 15.3 per cent). This acceleration is almost entirely due to loans on collateral of goods and to discounts of bills originating from sales of durable consumer goods on an instalment basis.

The financing of both import (increase: Dr. 1,239 million or 78.6 per cent) and export trade (increase: Dr. 1,021 million or 33.4 per cent) also increased at a rapid pace in 1976. The increase of credit to import trade reflects mainly the financing of basic food imports, particularly meat. Contrary to what has happened in other branches of trade, the financing of tobacco trade increased at a much slower pace in 1976 (6.9 per cent compared with 51.0 per cent in 1975). This has occurred because of the lower market prices of exportable tobacco.

Long-term housing loans increased considerably in 1976 (17.3 per cent compared with 11.8 per cent in 1975), while the financing of the tourist sector increased at approximately the same rate as in 1975 (1976: 14.4 per cent; 1975: 13.6 per cent). Shipping finance fell, however, by 2 per cent, compared with an increase of 5.8 per cent in 1975.

The acceleration of the outstanding balance of housing loans, recorded in 1976, was the result of the resumption in 1975 of approvals of this category of loans, following a freeze imposed during part of 1973 and most of 1974. Increased ceilings on personal housing loans also contributed to the aforementioned acceleration. The monetary authorities approved in 1976 a programme of new housing loans, which was 90 per cent higher than that of the previous year. Disbursements for new housing loans in 1976



## CHANGES IN TOTAL BANK CREDIT BY SECTOR

	Outstanding balances on 31 Dec. 1976 (million drachmas)	Changes in outstanding balances at year-end					
		Million drachmas			Percentage		
		1974	1975	1976	1974	1975	1976
I. PRIVATE SECTOR	378,006	+40,630	+59,593	+75,183	+20.1	+24.5	+24.8
Long-term loans	165,166	+14,449	+18,693	+29,782	+14.1	+16.0	+22.0
Short-term loans	212,840	+26,181	+40,900	+45,401	+26.1	+32.3	+27.1
1. Agriculture	70,157	+10,806	+12,152	+13,482	+32.0	+27.3	+23.8
Long-term loans	28,579	+ 3,066	+ 3,747	+ 4,011	+17.3	+18.0	+16.3
Short-term loans	33,028	+ 5,511	+ 4,781	+ 7,866	+37.1	+23.5	+31.3
Agricultural supplies	8,550	+ 2,229	+ 3,624	+ 1,605	+204.1	+109.1	+23.1
2. Manufacturing and Mining	149,972	+19,142	+27,628	+ 28,565	+25.6	+29.5	+23.5
Long-term loans	49,985	+ 5,806	+ 7,676	+ 7,972	+20.3	+22.4	+19.0
Short-term loans	99,987	+13,336	+19,952	+ 20,593	+28.9	+33.6	+25.9
3. Handicraft <sup>1</sup>	17,448	+ 701	+ 3,223	+ 3,484	+ 7.0	+30.0	+24.9
4. Trade	41,908	+ 2,102	+ 6,663	+10,711	+ 9.4	+27.2	+34.3
Domestic	29,409	+ 2,179	+ 4,869	+ 8,087	+15.3	+29.6	+37.9
Import	2,815	— 558	— 307	+ 1,239	—22.9	—16.3	+78.6
Export	4,076	+ 193	+ 329	+ 1,021	+ 7.6	+12.1	+33.4
Tobacco	5,608	+ 288	+ 1,772	+ 364	+ 9.0	+51.0	+ 6.9
5. Other	98,521	+ 7,879	+ 9,927	+18,941	+12.8	+14.2	+23.8
Long-term loans	84,187	+ 5,349	+ 6,796	+17,089	+ 9.7	+11.3	+25.5
—Housing	(43,400)	(+ 1,281)	(+ 3,896)	(+ 6,392)	(+ 4.0)	(+11.8)	(+17.3)
—Tourism	(22,549)	(+ 2,928)	(+ 2,363)	(+ 2,835)	(+20.3)	(+13.6)	(+14.4)
—Shipping	(6,267)	(— 79)	(+ 350)	(— 126)	(— 1.3)	(+ 5.8)	(— 2.0)
—Other	(11,971)	(+ 1,219)	(+ 187)	(+ 7,988)	(+47.3)	(+ 4.9)	(+200.6)
Short-term loans	14,334	+ 2,530	+ 3,131	+ 1,852	+37.1	+33.5	+14.8
II. PUBLIC SECTOR	61,961	+ 7,930	+ 7,915	+10,991	+22.6	+18.4	+21.6
Public enterprises	37,506	+ 5,649	+ 5,615	+ 6,888	+29.2	+22.5	+22.5
Public entities	14,363	— 99	+ 1,000	+ 1,655	— 0.8	+ 8.5	+13.0
Government agencies purchasing agricultural products	10,092	+ 2,380	+ 1,300	+ 2,448	+60.0	+20.5	+32.0
T o t a l	439,967	+48,560	+67,508	+86,174	+20.4	+23.6	+24.4

(1) Small-scale industry.



increased at a slower pace than approvals, namely by 56 per cent. This differential growth rate was caused by the slow absorption of housing loans by certain categories of those entitled to receive them, such as civil servants and other employees.

### 3. DEPOSITS

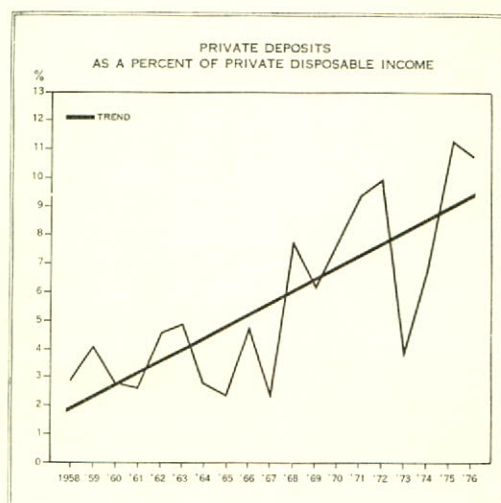
#### *a. Private Deposits*

For the second year in succession, private deposits increased in 1976 at a rapid pace (1976: 26.3 per cent; 1975: 31.8 per cent). According to provisional estimates, the increase in deposits reflects a high ratio to private disposable income (1976: 10.8 per cent; 1975: 11.3 per cent; 1973-1974: average 5.4 per cent; during the pre-inflation period 1966-1972 the average was 6.9 per cent). These developments indicate that, in the last two years, this ratio resumed its long-run upward trend, following its decline during the inflationary period.

The acceleration in the rate of growth of deposits recorded in the last two years has been influenced by the slowdown in the rate of inflation and by reduced inflationary expectations. Both these influences had adverse effects on bank deposits in 1973-1974. Under present conditions other factors may also induce a rise in deposits. For example, the steep increases in real estate prices during the high inflation period substantially lengthened, for many savers, the time needed to accumulate sufficient funds for the purchase of a house. This holds true even for people eligible to use bank loans to partially finance the purchase of a dwelling. For this reason, withdrawals of deposits for housing purchases have apparently slowed down, while the inflow of new deposits intended for the purchase of dwellings continues at the same or even a higher rate. Finally, the inadequate supply of new equity and bond issues, in recent years, has contributed to the increase in deposits.

Bank deposits, being very sensitive to changes in Greek-Turkish relations, fluctuated sharply in the course of 1976. In the first half of the year deposits grew at a faster rate, reflecting a re-inflow of deposits which had been converted into cash in 1975. Following the crisis in the Aegean, the rate of increase of deposits slowed down considerably in July-August and resumed its upward trend in September.

The growth of savings deposits slowed down (1976: 27 per cent; 1975: 33.5 per cent), while that of time deposits accelerated (1976: 34.3 per cent; 1975: 32 per cent). The



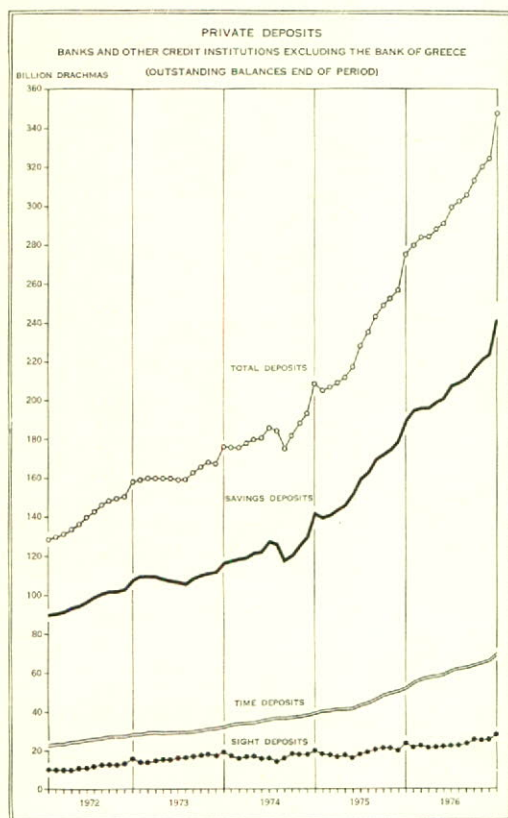
## PRIVATE DEPOSITS

Category	Outstanding balances on 31 Dec. 1976 (million drachmas)	Annual changes					
		Million drachmas			Percentage		
		1974	1975	1976	1974	1975	1976
Sight	27,767	+ 648	+ 4,108	+ 4,153	+ 3.4	+21.0	+17.6
Savings	240,095	+25,036	+47,466	+51,111	+21.5	+33.5	+27.0
Time	68,530	+ 7,061	+12,372	+17,488	+22.3	+32.0	+34.3
Restricted	10,860	— 97	+ 2,350	— 475	— 1.1	+26.1	— 4.2
<b>Total</b>	<b>347,252</b>	<b>+32,648</b>	<b>+66,296</b>	<b>+72,277</b>	<b>+18.5</b>	<b>+31.8</b>	<b>+26.3</b>

more rapid pace of increase of time deposits may also be attributable to the 0.5 percentage point increase in the interest rate differential between interest paid on time and savings deposits since October 1975. The sensitivity to interest rate differentials has be-

come more apparent after November 1976, when interest rates on deposits were reduced. This reduction, which raised to 1 percentage point the yield differential between bank bonds and time deposits, seems to have induced the public to invest in these bonds.

Sight deposits, which as of October 1975 pay no interest, increased at a slower pace in 1976 (17.6 per cent compared with 21 per cent in 1975). Deposits in restricted accounts decreased in 1976, chiefly as a result of substantial withdrawals of funds which had been deposited in escrow accounts in 1975 with the Consignations and Loans Fund for the compulsory purchase of property by the government. In comparison with the previous two years, certain changes were observed in 1976 concerning the ability of various credit institutions to attract private deposits. In 1976, commercial banks attracted 70 per cent of the increase in deposits, the Postal Savings Bank 20 per cent and the other 10 per cent went to all other credit institutions. The increased share of other credit institutions in the total (1976: 10.6 per cent; 1975: 5.8 per cent) reflects the Agricultural



Bank's efforts to attract new deposits, which started in the second half of 1976 and has produced good results. The encouraging results thus far realized, coupled with the favourable climate for floating new bank bonds, suggest that there are strong possibilities to reduce existing asymmetries in the distribution of deposits among the various types of



BREAKDOWN OF ANNUAL CHANGES IN PRIVATE DEPOSITS BY CREDIT INSTITUTION  
(Per cent)

Credit institution	Total private deposits			Savings deposits		
	1974	1975	1976	1974	1975	1976
Commercial banks	73.4	72.3	70.4	65.7	67.9	61.0
Postal Savings Bank	20.5	18.7	20.0	26.7	26.3	28.4
Other	6.1	9.0	9.6	7.6	5.8	10.6
Total	100.0	100.0	100.0	100.0	100.0	100.0

credit institutions. It is therefore essential to take this opportunity to enhance the effectiveness of monetary and credit policy.

*b. Foreign Exchange Deposits*

The outstanding balance of foreign exchange deposits increased at a particularly high rate in 1976 compared with the previous two years (1976: Dr. 23,000 million or 57.4 per cent; 1975: Dr. 13,655 million or 51.8 per cent; 1974: Dr. 5,588 million or 26.9 per cent). The largest part of these deposits is held by Greek emigrants and seamen. The rapid pace of increase of these deposits (1976: 71.6 per cent; 1975: 66.4 per cent) was in large part due to widening differentials between Greek interest rates and comparable rates abroad, especially in West Germany. The interest rate differential on savings deposits between Greece and West Germany rose by 2 percentage points, i.e., a differential of 2 percentage points at the beginning of 1975 to 4 percentage points in 1976. As the interest rate differential continues to be large, the small reduction in the interest paid on foreign exchange deposits as of January 1977 is not expected to affect adversely the inflow of these deposits.

*c. Deposits of Public Entities*

Deposits by social security funds and other public entities increased by Dr. 13,916 million in 1976, reaching Dr. 66,322 million at the end of the year. The corresponding increases for the last two years were Dr. 6,993 million in 1975 and Dr. 7,763 million in 1974. An increase of Dr. 4,520 million was also recorded in 1976 in public entities' holdings of treasury bills and other securities. Investments in treasury bills increased by Dr. 1,246 million while investments in other securities, mainly shares issued by the Commercial Bank, by Dr. 3,274 million. Total funds invested by public entities increased by Dr. 18,436 million in 1976, compared with increases of Dr. 11,220 million in 1975 and Dr. 7,925 million in 1974.

#### 4. CAPITAL MARKET

New security issues achieved a sizable increase in 1976, chiefly as a result of doubling the share capital of the Commercial Bank of Greece. The value of new share and bond issues

amounted to Dr. 6,617 million in 1976 (1975: Dr. 1,451 million; 1974: Dr. 980 million). Of the 1976 total, Dr. 5,523 million was due to the increase in the Commercial Bank's share capital. Social security funds and other public entities absorbed Dr. 4,971 million, while private firms and individuals acquired Dr. 552 million. New equity and bond issues floated by other private firms amounted to Dr. 992 million in 1976 (1975: Dr. 614 million).

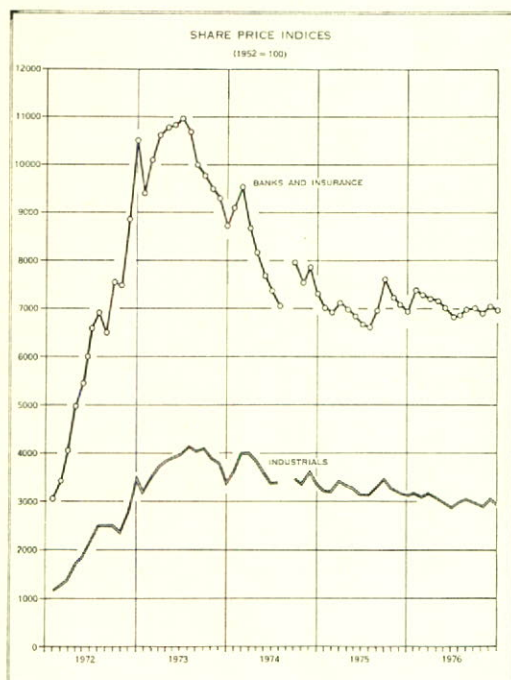
New issues of bank bonds reached Dr. 2,645 million in 1976 (Hellenic Industrial Development Bank: Dr. 1,755 million, National Mortgage Bank: Dr. 623 million, National Investment Bank for Industrial Development: Dr. 267 million). These issues were mostly absorbed by ordinary savers. The special features of this new financial asset, especially its high liquidity and satisfactory yield, were the basic factors which ensured its success.

Capital market developments in the course of 1976 once again showed that private firms did not provide an adequate supply of attractive equity issues. It is notable that whenever new share issues were offered by new and dynamic private concerns, demand for these issues exceeded the supply by a considerable margin. This shows that the basic problem of the capital market continues to be the inadequate supply of attractive new share issues. This inadequacy is essentially due to the family control of firms and to the policy pursued by credit institutions. Bringing private firms, government, and public agencies to the capital market for their long-term capital requirements is, as has already been stressed, of basic importance for controlling liquidity. At the same time it constitutes a prerequisite for the realization of an efficient allocation of resources and the

improvement of the capital structure of many firms. Inadequate supply of attractive new long-term issues forces a large segment of private savings to flow into banks. This results in an excessive increase in liquidity, which is a potential source of inflation. Concurrently, it creates a favourable setting for the rapid expansion of bank credit to large firms which, under these conditions, are not induced to resort to the capital market to meet their financial requirements.

Under these circumstances, demand for new share issues of dynamic firms is buoyant; for large groups of savers have limited outlets in hedging against inflation. This inadequate supply of new equity issues also creates the setting for the development of speculative tendencies in the Stock Exchange. And, of course, speculation must be averted as it may discourage potential investors.

For the same reasons but mainly in order to reduce the rate of increase of liquid funds, the government and public enterprises must begin to raise funds in the capital market in order to finance part of their loan requirements. The success of the new bank bond issues has proved that floating bond issues is possible, even under inflationary con-





ditions, provided that the terms of the issue reflect current market conditions. Developments in many European countries suggest that the process of floating new bond issues was not disrupted even in those countries where inflation rates were higher than those in Greece during the last two years. Evidently, this experience lends support to the above argument.

Share prices moved downward in 1976, though prices of certain industrial and commercial shares increased. The index for industrials dropped by 6.8 per cent in 1976, while that for banks and insurances increased by 1.2 per cent. The market for industrials was affected by new taxes and, particularly, by higher taxes levied on dividends and capital gains resulting from the revaluation of land and buildings which was required by new legislation.

Prices of post-war government bond issues remained unchanged in 1976. However, prices of pre-war government bonds and bonds of public and private enterprises increased at a lower rate than in 1975. The relevant price index for government bonds dropped by 0.4 per cent in 1976, while the index for bonds of public and private enterprises increased by 8.6 per cent and 6.3 per cent. Bond prices of both public and private firms improved, basically because most of these issues contained a foreign exchange clause.

The volume of stock exchange transactions grew at a rapid pace in 1976. Compared with 1975, their total value reached Dr. 7,523 million, making for a 26 per cent increase. Particularly large increases were recorded in the value of transactions in commercials (99 per cent) and industrials (48 per cent), while the value of transactions in bank shares increased by only 2.3 per cent. Finally, transactions in shares accounted for 90 per cent of the total value of transactions at the Stock Exchange.

## V. PUBLIC FINANCE

### 1. BUDGETARY RESULTS

The 1976 overall government budget was in deficit for a third consecutive year. These deficits have contributed significantly to the rebound of the economy, but have also exerted an expansionary effect on the money supply. According to available data<sup>1</sup>, revenues of the overall government budget (ordinary and public investment budgets) reached in fiscal 1976 the Dr. 174,630 million mark, while expenditures were estimated at Dr. 211,550 million. Consequently, the deficit was estimated at Dr. 36,920 million compared with Dr. 31,412 million for 1975. This deficit is exclusively attributed to the public investment programme, whereas the ordinary budget has, for the first time in recent years, shown a surplus of Dr. 2,500 million.

The budgetary deficit has been covered by (a) selling Dr. 33,378 million of treasury bills to the banking system and public entities, (b) borrowing Dr. 2,500 million from the Bank of Greece, and (c) borrowing from foreign sources Dr. 1,042 million. The deficit resulting from agricultural price support schemes and the procurement of government supplies has been estimated at Dr. 12,800 million for 1976 compared with Dr. 9,200 million for 1975. Adding this amount to the budget deficit, the total deficit reached approximately Dr. 49,700 million, against Dr. 40,600 million deficit in 1975. The deficit resulting from the various subsidies was financed by the Bank of Greece. The compensatory financing of these schemes aimed at increasing agricultural incomes and containing price rises of basic foodstuffs.

Putting the budget on a cash basis, i.e., analyzing the activity of the Government's accounts with the Bank of Greece, the computed deficit is significantly different. This is considered a more appropriate method of assessing the economic and monetary implications of fiscal policy. The activity of these accounts, including the Agricultural Bank's fertilizer account, showed a deficit of Dr. 48 billion compared with Dr. 47.3 billion for 1975 and Dr. 30.2 billion for 1974. This deficit, as a per cent of GDP, declined to 5.9 per cent from 7 per cent in 1975. In 1974 it was 5.3 per cent. The fall in this ratio is a step in the right direction and ought to continue, especially after the economy has assumed a satisfactory steady growth.

### 2. ORDINARY BUDGET

The ordinary budget revenue amounted to Dr. 173,850 million in 1976 as compared with Dr. 137,246 million in 1975, making for an increase of Dr. 36,604 million or 26.7 per cent. Tax receipts increased by Dr. 40,135 million or 33.2 per cent as compared with a 24.6 per cent increase in 1975. The "special tax levy" that was imposed on the outstanding

(<sup>1</sup>) Budget data (from the Ministry of Finance) are not on a cash basis, unless otherwise stated.



bank loan balances and/or corporate profits yielded approximately Dr. 11,500 million. A high rate of increase was realized in 1976 among almost all basic categories of regular tax revenue, with the exception of the special sugar consumption tax. The lower yield of this excise tax resulted from a new method of distributing domestic production in the home market.

Income tax receipts increased by 23.8 per cent due to (a) the increase in profits and money incomes, (b) the graduated progressivity of income tax rates, and (c) the increase in both employment and wages and salaries coupled with improved collection procedures which led to higher tax revenues from wages, salaries and pensions. The improved collection procedures enabled the Government to collect promptly the entire amount of taxes withheld by employers. The rate of increase of property tax revenues has been even higher (38.2 per cent) owing to increased revenues from state lotteries and prompt payment of taxes on inheritance, gifts and dowries. Conversely, the increase of real estate tax revenues was relatively small, mainly due to technical delays in auditing tax forms submitted in 1975 and 1976.

Receipts from import duties increased by 17.9 per cent and those from general consumption taxes on imported goods by 44 per cent. The increase was 1 per cent and 28.5 per cent respectively in 1975. The substantial increase in revenues in 1976 was realized despite tariff reductions which were put into effect in accordance with the Athens Agreement of Association. The rapid increase of manufactured final consumer goods imports, taxed at relatively higher rates, contributed to this increase in tax revenues. Another significant contributory factor was the improved method of assessing the tax base, following Law 363/1976 which instituted a more efficient, equitable and simple way of taxing imported cars; and Law 398/1976 which harmonized Greek legislation, concerning the taxable value of imports, with EEC regulations. Finally, turnover tax revenues on domestic goods and services increased by 32.7 per cent; transaction taxes by 31.9 per cent; and transport fees and dues by 41.9 per cent. In short, increased revenues reflect the revival of economic activity and price rises. Additionally, higher tax rates, which were introduced in 1975, affected revenues in 1975 and in 1976.

The 1976 ordinary budget expenditures were estimated to reach Dr. 171,350 million compared with Dr. 137,220 million in 1975, making for an increase of 24.9 per cent (1975: 31.5 per cent). The rate of increase of public expenditures in 1976 continued to be relatively high despite its slowdown compared with 1975. This increase is explained by higher defence expenditures and by the expansion and improvement of educational and other welfare programmes. These types of expenditures, coupled with the servicing of public debt, subsidies and the transfer of tax revenues collected on behalf of third parties, account for the largest part of the total increase in expenditures.

### 3. PUBLIC INVESTMENT

Expenditures for the government investment programme had been budgeted at Dr. 41,000 million. This sum included a reserve fund of Dr. 5,500 million. The actual expenditures, however, reached approximately Dr. 40,200 million compared with Dr. 32,512



million for 1975, i.e., they increased by Dr. 7,688 million or 23.6 per cent. Transport, irrigation, education, sewerage and water works and local programmes administered by prefectures account for the largest part of the 1976 appropriations.

These expenditures were financed in part by a Dr. 2,500 million surplus of the ordinary budget, by Dr. 780 million from special investment revenues and by Dr. 36,920 million from borrowing.

Investments of the Public Power Corporation (PPC) and the Hellenic Telecommunications Organization (HTO) increased by 7.5 per cent in 1976 against a decline of 29.4 per cent in 1975. The absolute level of these investments was Dr. 13,511 million and Dr. 12,570 million respectively. This increase was due to PPC's investment programme alone, whereas that of HTO remained at the previous year's level. Self-financing and state subsidies to PPC accounted for 18.3 per cent of the total; the balance was raised through borrowing. The main source of loans was Greece's banking system which provided Dr. 7,635 million.

#### 4. GOVERNMENT ACCOUNTS OF CONSUMER GOODS AND AGRICULTURAL PRODUCTS

The overall debit balance in the accounts held at the Bank of Greece regarding government purchases of agricultural products, supplies and the management of the fertilizer account by the Agricultural Bank of Greece amounted to Dr. 67,800 million at the end of 1976, against Dr. 45,800 million at the end of 1975, making for an increase of Dr. 22,000 million against Dr. 11,700 million in 1975. The largest component of this increase was due to losses incurred in managing the accounts mentioned above. The resulting deficit was estimated at Dr. 12,800 million in 1976 against Dr. 9,200 million in 1975. The remaining part of the increase reflects rising inventories of grains, olive oil, tobacco and petroleum products. The 1976 cumulative deficit resulting from the management of consumer goods and government supplies accounts reached approximately Dr. 38,200 million. Thus, in relation to 1975, the debit balance of all relevant accounts was increased. The greatest increase was recorded in the consumer goods and tobacco accounts. However, the currants-raisins and fertilizer accounts exhibited smaller increases.

#### 5. THE BUDGET FOR 1977

The overall government budget for 1977 provides for a total revenue of Dr. 201,300 million and total expenditures of Dr. 245 billion, including reserves of Dr. 14,000 million. Thus, the 1977 deficit is estimated at Dr. 43,700 million and is expected to be financed in part by domestic borrowing through the issue of treasury bills (Dr. 31,700 million) and the balance by foreign borrowing (Dr. 12,000 million).

The 1977 budget provides significant reserves to ensure the financing of contingent high priority needs. It also provides the necessary flexibility for adjusting expenditure policy to short-term fiscal and monetary developments. Another noteworthy feature



of the new budget is the expected retardation in the rate of increase of expenditures from 24.6 per cent in 1976 to 15.8 per cent in 1977. Similarly, the expected rate of increase of revenues will be 15.3 per cent against 26.3 per cent in 1976. The lower rate of increase is explained by the fact that the 1976 revenues included the proceeds of the "special tax levy". Hence, the combined effect of these results may be a larger deficit. A larger deficit may in fact not be realized if the reserves anticipated in the 1977 budget are not utilized.

## 6. TAX REFORMS

The following reforms regarding direct and indirect taxation were introduced by Law 542/1977 early in 1977:

(a) The tax rate on dividends for stocks listed in the Athens Stock Exchange was raised to 38 per cent for "name-bearing-stocks" and to 41 per cent for "stock-to-the-bearer" from a 33 per cent across-the-board rate that was previously in effect. For stocks not listed in the Stock Exchange, the tax rate on dividends rose from 41 per cent to 43 per cent for "name-bearing-stocks" and to 47 per cent for "stock-to-the-bearer". The taxpayer may also report in his income tax return dividends from all "name-bearing-stocks" and dividends from "stock-to-the-bearer" listed in the Stock Exchange. These items will be treated as ordinary personal income. Otherwise, dividends from "stock-to-the-bearer" not listed in the Stock Exchange will be taxed at a flat rate of 47 per cent.

(b) Companies' real estate must be revalued. Specifically, land and buildings will be revalued on the basis of special rates which vary according to the time of acquisition of these assets. Capital gains resulting from the revaluation will be capitalized and taxed at a rate of 10 per cent for land and 20 per cent for buildings.

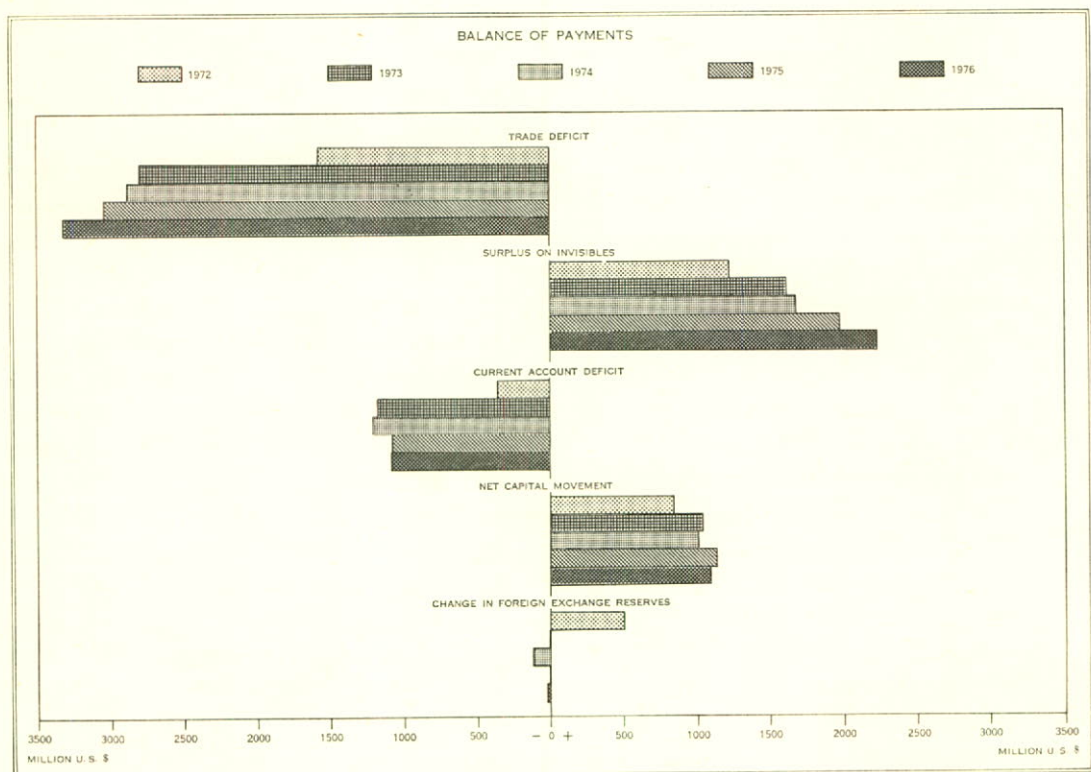
(c) The assessed valuation of real estate for tax purposes will no longer be based on the capitalization of the income stream from either actual or imputed rent. The jurisdiction of assessing real estate taxable values is being transferred from present *ad hoc* committees to the local tax authorities. These reforms ensure a more efficient method of capturing taxable income, while the tax assessment process is also expedited.

(d) Special measures are put into effect to reduce tax evasion. On the basis of consumption expenditure patterns, the level of income from self-employment is determined more effectively. The maximum level of fines imposed for certain tax omissions is increased to Dr. 200,000 from Dr. 20,000 which was put in effect in 1955.

The new legislation closed certain loopholes in the tax law, simplified the process of assessment and payment of taxes and expanded tax incentives to promote regional development and company mergers. Finally, as of May 1977, a new tax code is put into effect which will facilitate the functioning of the Internal Revenue Service.

## VI. BALANCE OF PAYMENTS

The current account deficit in 1976 remained at about the same level as in 1975 (1976: \$1,091 million; 1975: \$1,088 million) despite the fact that in this period the pace of Greece's economic recovery was substantially faster than that of other industrial countries, especially those in Western Europe. The 1976 deficit was completely financed by autonomous inflows of private capital, chiefly foreign exchange deposits of Greek seamen



and emigrants. A large part of these deposits is converted into drachmas and spent in Greece and does not necessitate debt service payments.

This favourable development occurred as the trade deficit increased further while the rate of growth of the invisible trade surplus slowed down. These two trends indicate that the foreign sector balance was not the result of structural changes in the Greek economy.

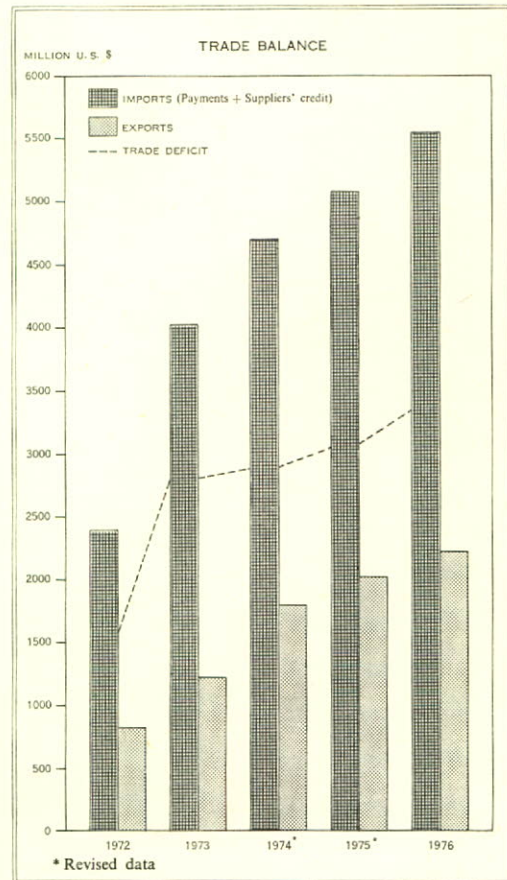
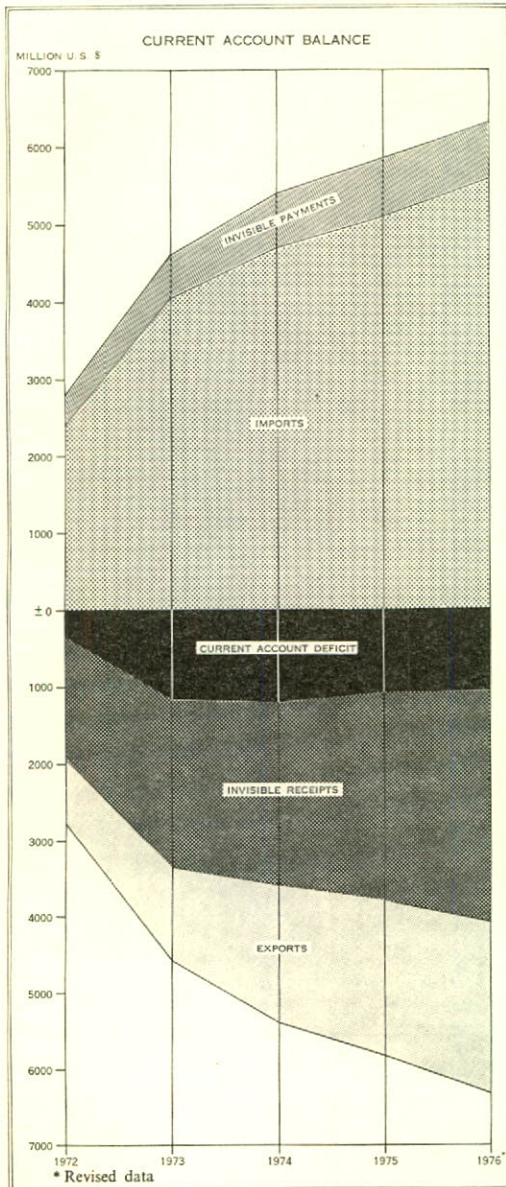
### 1. CURRENT TRANSACTIONS

The 1976 retardation in the growth rate of foreign exchange receipts from commodity exports reflects the difficulties encountered by Greece's agricultural exports. However,



industrial exports accelerated, partly as a result of the exchange rate policy pursued, from the fall of 1974 to the end of 1975. This policy aimed at improving the competitiveness of the Greek economy.

Evidently, the exchange rate policy pursued did not lead to an expansion of agri-



cultural exports. This may be explained by the low price elasticity of demand which apparently characterizes most of these products. Furthermore, the favourable effect of the exchange rate policy on imports, particularly consumer goods imports, has also been limited as a result of the high income elasticity of demand for these goods. Hence, the trade deficit increased from \$3,050 million in 1975 to \$3,328 million in 1976.

The invisible trade surplus increased at a slower rate (1976: 14 per cent; 1975: 17.1 per cent). The 10.9 per cent increase in invisible receipts was mainly due to tourism, and to a lesser extent to shipping. The increase in emigrants' remittances was, however, limited.

## BALANCE OF PAYMENTS

(Million U.S. dollars)

Items	1974	1975	1976
IMPORTS (plus suppliers' credit)	4,691.0	5,079.6	5,556.0
Private	3,507.7	3,866.4	4,270.5
Government	1,183.3	1,213.2	1,285.5
(Payments)	(4,565.6)	(4,850.1)	(5,552.2)
EXPORTS	1,802.9	2,029.4	2,227.5
<b>Balance of Trade</b>	<b>-2,888.1</b>	<b>-3,050.2</b>	<b>-3,328.5</b>
INVISIBLE RECEIPTS	2,399.0	2,726.4	3,023.8
INVISIBLE PAYMENTS	723.5	764.6	786.8
<b>Balance on Invisibles</b>	<b>1,675.5</b>	<b>1,961.8</b>	<b>2,237.0</b>
<b>Balance on Current Account</b>	<b>-1,212.6</b>	<b>-1,088.4</b>	<b>-1,091.5</b>
CAPITAL MOVEMENT (net)	1,021.9	1,144.2	1,093.3
Private venture capital	189.3	199.1	221.2
Other private capital	250.0	320.9	360.6
Capital belonging to banks and credit institutions	193.5	285.8	612.1
Central Bank	262.5	331.1	60.7
Government loans	114.0	93.6	97.0
Public entity and public enterprise loans	66.8	15.0	76.7
Amortization	-180.6	-344.4	-348.0
Foreign suppliers' credit	125.4	229.5	3.8
Aid-Restitutions-Reparations	1.0	13.6	9.2
SDRs (allocation)	—	—	—
Errors and omissions	64.0	-216.2	-129.0
<b>Balance of external transactions</b>	<b>-126.7</b>	<b>-160.4</b>	<b>-127.2</b>
IMF	-42.9	-186.0	-67.4
Change in official reserves	-112.6	6.9	-5.7
Change in SDRs	0.8	-12.1	-0.9
Change in clearing accounts	28.0	30.8	-53.2
Official reserves (end of period)	903.7	910.6	905.0
SDRs	32.7	20.6	19.5
Clearing accounts	-3.1	26.8	-26.4
Suppliers' credit	1,056.9	1,286.4	1,290.2

Note : Data for 1974 and 1975 revised on the basis of current parities.



### a. Imports

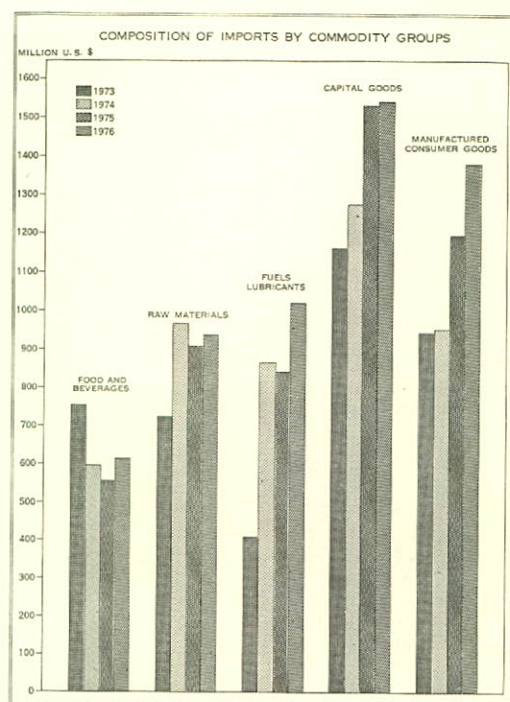
Expenditure for imports (payments and suppliers' credit) increased by 9.4 per cent in 1976, but exhibited considerable variation in the course of the year. Seasonally adjusted data for imports showed a continuous upward trend during the first three quarters of the year. Their rate of growth slowed down, however, in the fourth quarter.

The acceleration in the growth rate of the import bill, which occurred in the second half of 1976, was the result of the strong demand for construction materials, manufactured consumer goods and petroleum products. The strong demand for imported manufactured consumer goods was, in large part, due to the rising incomes of those groups who have a high marginal propensity to consume such goods. Moreover, inflationary expectations, which continue to persist despite the small decrease in inflation, coupled with the diversion of substantial bank funds to the financing of consumer expenditure, contributed to an increase of the import bill, especially consumer durables.

Food imports increased by 11.9 per cent in 1976 following a decline in 1975. Basic foodstuff imports, especially meat and live animals, which increased by 138.5 per cent, account for the largest part of this increase. The upsurge in meat imports is partly explained by stronger home demand and partly by the supply shortages which followed the reduction of livestock population in 1975. Payments for coffee imports also increased substantially (75.2 per cent) as a result of the rise in world coffee prices. Conversely, payments for cereal imports declined while those for sugar imports were completely phased out since domestic production satisfied domestic demand.

The import bill for raw materials increased by 3.8 per cent. This was due to an increase in construction material imports, whereas raw material imports for consumption fell by 6.8 per cent. Moreover, certain indications suggest that the liquidation of raw material stocks, accumulated in 1973/74, continued through the first half of 1976. This development, coupled with the increase in construction activity and the upward price trend of certain materials, such as iron and steel, led to a higher growth rate of imports of construction materials during the second half of 1976. The import bill for consumer raw materials fell despite the rise in industrial production. This was due to the partial substitution of local raw materials for imports (textile raw material inputs, minerals and fertilizers) and the fall in prices of certain goods in this category.

Imports of fuels and lubricants increased by 21.6 per cent in 1976. Compared with a drop of 4.8 per cent in 1975 the petroleum import bill went up by 26.4 per cent as a



**IMPORTS**  
(Payments and suppliers' credit)

Category	Million U.S. dollars			Changes in %	
	1974	1975	1976	1975	1976
I. FOOD	594.0	556.7	622.7	-6.3	11.9
1. Basic	528.4	487.8	535.4	-7.7	9.8
Meat and live animals	85.7	83.7	199.6	-2.3	138.5
Dairy products	60.7	57.1	53.1	-5.9	-7.0
Cereals	210.2	125.6	110.8	-40.3	-11.8
Coffee	18.5	24.2	42.4	30.8	75.2
Sugar	33.9	70.7	0.9	108.6	...
Vegetable oils	42.6	54.5	41.0	27.9	-24.8
Animal feed	53.0	40.6	48.5	-23.4	19.5
Other	23.8	31.4	39.1	31.9	24.5
2. Non-basic	65.6	68.9	87.3	5.0	26.7
II. RAW MATERIALS	966.0	909.0	943.4	-5.9	3.8
1. Consumption materials	511.8	550.5	513.3	5.6	-6.8
Cotton and textile fibers	95.9	76.4	69.5	-20.3	-9.0
Fertilizers	41.2	51.6	38.2	25.2	-26.0
Other chemicals	173.0	195.3	218.0	12.9	11.6
Raw minerals	72.2	76.9	43.7	6.5	-43.2
Other	129.5	150.3	143.9	16.1	-4.3
2. Construction materials	454.2	358.5	430.1	-21.2	20.0
Iron and steel	351.1	256.7	294.8	-26.9	14.8
Timber	66.8	68.8	80.3	3.0	16.7
Other	36.3	33.0	55.0	-9.1	66.7
III. FUELS - LUBRICANTS	863.9	843.5	1,026.1	-2.4	21.6
1. Coal	43.0	62.0	37.9	44.2	-38.9
2. Petroleum products	820.9	781.5	988.2	-4.8	26.4
IV. CAPITAL GOODS	1,276.2	1,536.0	1,542.7	20.4	0.4
1. Machinery	888.0	958.6	964.5	8.0	0.6
2. Transport equipment	278.5	474.5	482.2	70.4	1.6
3. Electrical equipment	109.7	102.9	96.0	-6.2	-6.7
V. MANUFACTURED CONSUMER GOODS	955.4	1,201.4	1,388.5	25.7	15.6
1. Intermediate	128.9	160.5	178.9	24.5	11.5
Plastics, cellulosic and synthetic materials	58.3	84.9	106.9	45.6	25.9
Other	70.6	75.6	72.0	7.1	-4.8
2. Basic	413.7	457.3	483.3	10.5	5.7
Automobile parts and accessories	83.7	102.6	106.9	22.6	4.2
Paper and paper articles	92.2	88.6	94.3	-3.9	6.4
Medical and pharmaceutical products	82.5	93.3	96.0	13.1	2.9
Other	155.3	172.8	186.1	11.3	7.7
3. Non-basic	412.8	583.6	726.3	41.4	24.5
Leather articles and furs	24.1	20.1	25.8	-16.6	28.4
Textile products	67.9	83.6	114.4	23.1	36.8
Electrical appliances	39.0	58.6	61.2	50.3	4.4
Private cars	49.8	106.8	171.0	114.5	60.1
Other	232.0	314.5	353.9	35.6	12.5
VI. FREIGHT	35.5	33.0	32.6	-7.0	-1.2
<b>Total</b>	<b>4,691.0</b>	<b>5,079.6</b>	<b>5,556.0</b>	<b>8.3</b>	<b>9.4</b>

Note : Data for 1974 and 1975 revised on the basis of current parities.



result of greater home demand. Part of the import bill rise occurred during the last months of 1976 and was due to stockpiling in anticipation of the OPEC decision to increase crude oil prices. In this context it should be stressed that limited progress has been made thus far in developing local energy sources (lignite, hydroelectric power).

The value of imports of capital goods remained at approximately the same level as in 1975. Imports of transport equipment increased by only 1.6 per cent, while the import bill for machinery remained unchanged. Considering that substantial price increases for these goods have occurred, it follows that the volume of machinery imports has dropped. The decline of demand for imported capital goods, as of mid-1974, was the result of the sluggish behaviour of industrial investment.

Finally, a high rate of increase (15.6 per cent) was recorded in imports of manufactured consumer goods. In this category, imports of non-basic industrial goods increased at a faster pace (24.5 per cent), particularly private automobiles (60.1 per cent), textile products (36.8 per cent), and leather articles and furs (28.4 per cent). Imports of intermediate industrial products increased by 11.5 per cent. The largest increase recorded in this category was that of plastics and cellulosic and synthetic materials (25.9 per cent). Imports of basic industrial products recorded a smaller rise (5.7 per cent), reflecting the general trend in this class of goods. The high income elasticity of demand for most non-basic manufactured consumer goods led to an upsurge in their import bill.

#### *b. Exports*

Export earnings reached \$2,227 million in 1976 compared with \$2,029 million in 1975 and \$1,803 million in 1974. Their rate of growth was 9.8 per cent in 1976 and 12.6 per cent in 1975. Seasonally adjusted data show that exports were substantially higher in the first quarter of the year compared with the last quarter of 1975. The upward trend accelerated further in the second quarter, slowed down substantially in the third quarter and accelerated again in the fourth quarter of the year.

Demand conditions in world markets for Greek goods were more favourable in 1976 than in 1975. OECD latest estimates of international trade developments indicate that foreign demand (volume of imports) in the main markets for Greek goods increased by approximately 12 per cent in 1976 (1975: 5 per cent).

This improvement in foreign demand is attributed to the upturn of economic activity in the major OECD industrial countries, which began in mid-1975 and continued to pick up momentum through the first half of 1976. The rate of growth of foreign demand for Greek products originating in the OPEC countries remained high, even though the rate of increase was below that which was recorded in 1975.

Although international economic activity improved in 1976, the rate of increase of Greece's export earnings was lower than in 1975. This was caused by the sluggish performance of agricultural and raw material exports (1976: 4.9 per cent; 1975: 18.7 per cent), reflected in the small increase in the volume of these exports and the fall in prices caused by an increased supply of goods by competing countries. Moreover, domestic prices for certain goods (olive oil, sugar, wheat) were substantially higher than world prices. Hence, exports could not be realized without large subsidies.

The upturn of the world economy had affected favourably Greece's industrial

## EXPORTS

Category	Million U.S. dollars			Changes in %	
	1974	1975	1976	1975	1976
1. Food and beverages	380.8	514.5	542.2	35.1	5.4
Currants	37.2	32.6	37.1	-12.4	13.8
Sultana raisins	47.8	48.5	40.3	1.5	-17.0
Olives	23.8	34.7	35.8	45.8	3.2
Olive oil	10.6	20.6	10.7	94.3	-48.1
Citrus fruit	39.1	60.7	61.0	55.2	0.5
Other fresh fruit	39.5	81.2	55.6	105.6	-31.5
Fruit and vegetable preserves	78.5	74.4	84.3	-5.2	13.3
Other	104.3	161.8	217.4	55.1	34.4
2. Tobacco	161.2	166.0	161.7	3.0	-2.6
3. Raw materials and semi-manufactured goods	123.2	109.6	124.2	-11.0	13.3
Cotton	45.5	30.7	39.5	-32.5	28.7
Hides and skins	38.6	44.2	50.5	14.5	14.2
Other	39.1	34.7	34.2	-11.3	-1.4
4. Minerals and ores	104.9	140.8	136.2	34.2	-3.3
Bauxite	14.9	22.8	20.8	53.0	-8.8
Magnesia, dead-burnt	46.5	60.5	50.9	30.1	-15.9
Other	43.5	57.3	64.5	31.7	12.6
5. Petroleum products	123.4	87.0	73.6	-29.5	-15.4
6. Industrial and handicraft products	866.3	982.1	1,160.2	13.4	18.1
Textiles	205.3	241.0	369.5	17.4	53.3
Cement	79.9	131.7	131.1	64.8	-0.5
Other chemicals and pharmaceuticals	40.8	68.0	65.1	66.7	-4.3
Aluminium-Alumina	72.5	59.0	59.5	-18.6	0.8
Nickel-Ferronickel	70.0	59.1	35.9	-15.6	-39.3
Other metals and metal manufactures	144.2	139.6	139.6	-3.2	—
Machinery and transport equipment	16.8	25.8	36.6	53.6	41.9
Footwear and leather articles	28.5	36.6	54.5	28.4	48.9
Other	208.3	221.3	268.4	6.2	21.3
7. Other	43.1	29.4	29.6	-31.0	0.7
Grand total	1,802.9	2,029.4	2,227.5	12.6	9.8

Note : Data for 1974 and 1975 revised on the basis of current parities.

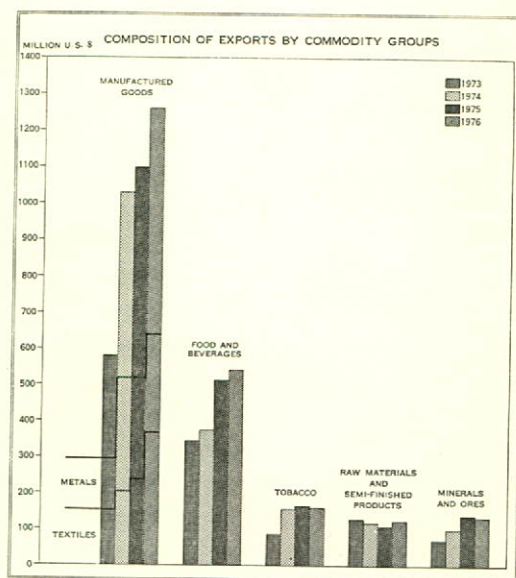


exports whose growth continued to accelerate from mid-1975 to the first half of 1976. The slowdown of economic activity in industrial countries as of the third quarter of 1976 explains the fall in demand for industrial products. As a result, it led to a substantial slowdown in the rate of growth of exports in this category, which increased by only 5.6 per cent between the second and first half of 1976, compared with an increase of 10.0 per cent between the first half of 1976 and the second half of 1975.

Available evidence suggests that domestic supply did not act as a constraint on exports in 1976. Despite the fall in output of some exportable agricultural products, supply bottlenecks were not encountered (with the exception of cotton owing to an increase in home demand). Additional information indicates that supply was quite elastic in the manufacturing sector. National Statistical Service data further suggest that output of export-oriented industries recorded a higher than average rate of growth. In summary, Greek exports in 1976 were chiefly affected by demand factors. This, however, does not imply that had slack industrial investment continued supply constraints would not arise in the future.

Export proceeds from food and beverages increased by only 5.4 per cent in 1976, reflecting a fall in export receipts from olive oil, sultanas and other fresh fruit. The fall in export receipts from sultanas was caused by falling world prices through October 1976, whereas quantities exported remained almost unchanged. During the last months of the year world prices increased substantially as a result of a crop failure in the U.S.A., which led to an increase in foreign exchange earnings from sultanas. The decline in olive oil export receipts was essentially due to a reduction in the volume of olive oil exports caused by the wide differentials between international and domestic prices. Exports of fresh fruit in 1976 remained at a satisfactory level. The apparent fall in the volume of fresh fruit exports reflects the exceptionally large fresh fruit (peaches) exports in 1975, which was the result of the crop failure in Europe caused by adverse weather conditions.

Tobacco export receipts, following a downward trend during the greater part of 1976, exhibited an upturn at the close of the year. Hence, tobacco export receipts almost reached the 1975 level while prices remained unchanged. Time lags between shipments and receipts in 1976 account for the recorded slight fall in receipts (2.6 per cent). Exports of raw materials and semi-manufactured goods increased at a high rate (13.3 per cent) while in 1975 they had fallen by 11 per cent. This upturn was mainly due to increased exports of cotton (28.7 per cent) and skins and hides (14.2 per cent). The increase in cotton exports was entirely due to the substantial rise in international cotton prices.



Potential exports of Greek cotton were curtailed by the rapid increase in production requirements of the export-oriented textile industry.

The slight decline (3.3 per cent) in exports of minerals and ores was due to a 16 per cent drop in exports of dead-burnt magnesia caused by reduced foreign demand; and of bauxite exports by 7.8 per cent. These adverse developments were partially offset by increased exports of marble and caustic magnesia.

Exports of manufactured goods recorded the largest increase of all major export categories (18.1 per cent compared with 13.4 per cent in 1975). The highest rates of increase were recorded in machinery and transport equipment exports (41.9 per cent), textiles (53.3 per cent), shoes (48.9 per cent) and other industrial products (21.3 per cent). The effect of these high rates on total industrial exports was offset by the fall in export proceeds from nickel and ferronickel (39.3 per cent). Cement export proceeds remained at 1975 levels as a result of lower world prices, which offset larger quantities exported in 1976. Increased textile exports are, to a large extent, explained by the gradual shift of the textile industry from the industrial countries of Western Europe to the less developed countries of Southern Europe.

### *c. Invisible Earnings and Payments*

The invisible trade surplus reached \$2,237 million in 1976 (1975: \$1,962 million). As in 1975, this improvement was due to the more rapid growth of invisible receipts (10.9 per cent) compared with invisible payments (2.9 per cent). The increase in invisible earnings was mainly due to tourism (28 per cent) and shipping (8.2 per cent). However, emigrants'

#### BALANCE ON INVISIBLES

RECEIPTS	Million U.S. dollars			Changes in %	
	1974	1975	1976	1975	1976
1. Shipping	867.1	845.0	914.1	-2.5	8.2
2. Tourism	447.6	643.6	823.7	43.8	28.0
3. Emigrants' remittances	673.5	783.0	803.2	16.3	2.6
4. Interest-Dividends-Profits	85.8	95.1	108.5	10.8	14.1
5. Other services	325.0	359.7	374.3	10.7	4.1
<b>Total</b>	<b>2,399.0</b>	<b>2,726.4</b>	<b>3,023.8</b>	<b>13.6</b>	<b>10.9</b>
<b>PAYMENTS</b>					
1. Transportation	152.9	172.3	144.6	12.7	-16.1
2. Tourism	129.1	154.8	150.7	19.9	-2.6
3. Interest-Dividends-Profits	183.0	195.1	219.6	6.6	12.6
4. Government services	88.4	67.2	67.6	-24.0	0.6
5. Other services	170.1	175.2	204.3	3.0	16.6
<b>Total</b>	<b>723.5</b>	<b>764.6</b>	<b>786.8</b>	<b>5.7</b>	<b>2.9</b>
<b>BALANCE ON INVISIBLES</b>	<b>1,675.5</b>	<b>1,961.8</b>	<b>2,237.0</b>	<b>17.1</b>	<b>14.0</b>

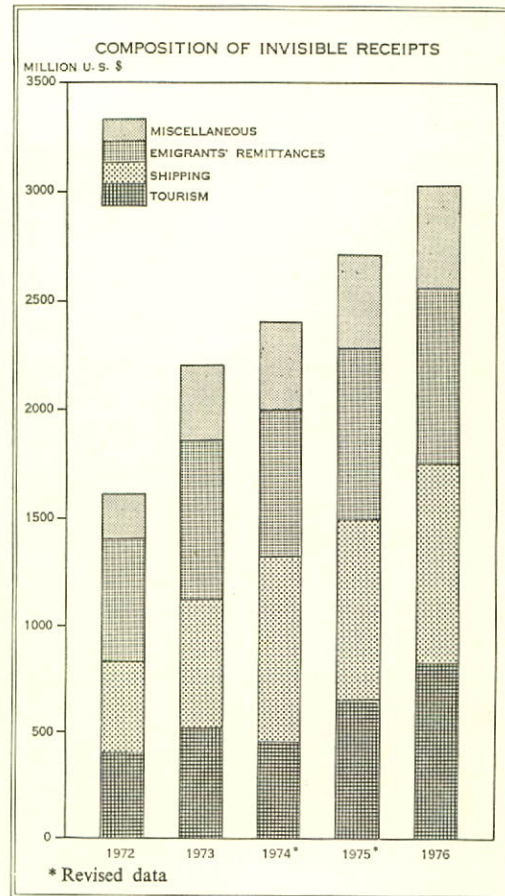
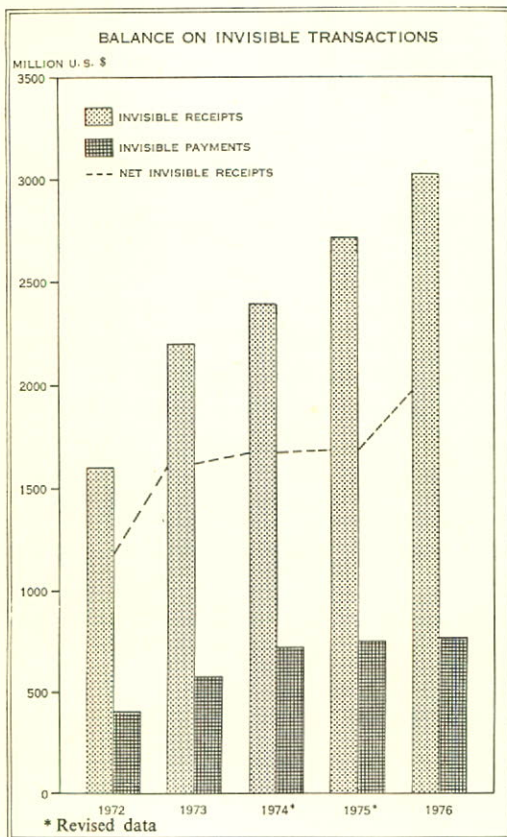
Note: Data for 1974 and 1975 revised on the basis of current parities.



remittances and "other services" recorded small increases (2.6 per cent and 4.1 per cent respectively).

The substantial growth in tourism receipts in 1976 was the result of the increase in tourist arrivals (35 per cent, excluding cruise passengers), as in 1975. Dollar prices of tourist services fell, however, in 1976, owing to the negotiated low package tour prices and to changes in the drachma-dollar parity. Relative price stability of tourist services induced an increased tourist inflow while, at the same time, it led to a drop of 5.5 per cent in the per capita tourist expenditure which in 1975 had remained almost unchanged.

The downward trend in earnings from shipping, which began in mid-1975, per-



sisted during the first half of 1976, because of adverse developments in virtually all sectors of the world shipping market. These developments led to the lay-up of part of the Greek-owned merchant fleet. During the second half of 1976, conditions improved in the oil and dry bulk cargo trades as a result of the increase in crude oil imports by OECD member countries, especially Japan, and OPEC imports. These developments led to an increase in the active Greek-owned fleet, and explain the rapid pace of increase in shipping receipts recorded during the second half of 1976.

Emigrants' remittances increased by only 2.6 per cent in 1976. This slight increase resulted from the substantial rise in drachma conversions of emigrants' foreign exchange deposits which offset the drop in direct emigrant remittances. The adverse conditions which prevailed in Western Germany's labour market led to a fall in the employment of Greek workers and to an increase in repatriation. If account is taken of the unfavourable climate persisting in the German labour market and the policy therein of restricting the number of foreign workers, it is expected that in 1977 the number of Greek workers in Germany will continue to decrease. Consequently, further increases in unilateral transfers will depend on wage developments in Western Germany and economic activity in the U.S.A. Other categories of invisible receipts, namely "other services", "interest and dividends" and "government services" (the latter as a result of increased expenditure by foreign missions in Greece) also increased at a good pace. The slow rate of increase in invisible payments was due to a fall in tourism and transportation payments, and no increase in payments for government services. Higher payments for interest, dividends and profits had, however, an expansionary effect on total invisible payments.

## 2. CAPITAL MOVEMENT

The autonomous inflow of private capital increased substantially in 1976 and was sufficient to finance the deficit on current account. This development was specifically caused by the large increase in the inflow of capital through commercial banks (deposits in foreign exchange, loans and credits), which more than offset the fall in foreign suppliers' credit. As a result, foreign borrowing by the Bank of Greece and the government were substantially reduced in 1976.

The inflow of private venture capital and capital intended for real estate investment (which constitutes the largest part of "other private capital") increased by 11.9 per cent in 1976 (1975: 18.4 per cent). The slowdown was basically due to the reduced rate of growth of capital intended for real estate investment (1976: 12.4 per cent; 1975: 28.4 per cent), which was only partly offset by the increased inflow of private venture capital (1976: 11.1 per cent; 1975: 5.2 per cent).

Net foreign suppliers' credit was substantially lower in 1976 as a result of a fall in new short-term suppliers' credit, whereas payments for settlement of outstanding suppliers' credit continued to increase. Hence, the outstanding balance of suppliers' credit remained unchanged; specifically, the share of short-term credits in the total outstanding balance was reduced.

Inflow of capital via the commercial banks increased by 114 per cent in 1976 (1975: 48 per cent). Foreign exchange deposits of Greek emigrants and seamen, which constitute the largest share in this category, increased by 77.0 per cent compared with 50.0 per cent in 1975.

The high level of foreign exchange deposits attained was, to a large extent, due to the substantial interest rate differential between Greece and Western Germany, where most of these deposits originate. Moreover, the repatriation of Greek workers, especially



## FINANCING OF THE CURRENT ACCOUNT DEFICIT

	Million U.S. dollars			Changes in %	
	1974	1975	1976	1975	1976
BALANCE ON CURRENT ACCOUNT	-1,212.6	-1,088.4	-1,091.5	-10.2	0.3
<b>Private capital</b>	<b>676.0</b>	<b>937.4</b>	<b>1,133.3</b>	<b>38.7</b>	<b>20.9</b>
Venture capital	189.3	199.1	221.2	5.2	11.1
Other (net movement)	250.0	320.9	360.6	28.4	12.4
Suppliers' credit (net change) <sup>1</sup>	125.4	229.5	3.8	83.0	-98.3
Inflow through commercial banks and credit institutions	193.5	285.8	612.1	47.7	114.2
Deposits in foreign exchange (net movement)	(183.0)	(274.1)	(484.5)	(49.8)	(76.8)
Loans and credit	(10.5)	(11.7)	(127.6)	(11.4)	(990.6)
Amortization	-82.2	-97.9	-64.4	19.1	-34.2
BALANCE OF PAYMENTS BEFORE CENTRAL BANK AND PUBLIC SECTOR BORROWING	-536.6	-151.0	41.8		
<b>Central Bank and Public Sector Borrowing</b>	<b>345.9</b>	<b>206.8</b>	<b>-40.0</b>		
Central Bank	262.5	331.1	60.7		
Public sector	115.0	107.2	106.2		
Public enterprises	66.8	15.0	76.7		
Amortization	-98.4	-246.5	-283.6		
<b>Errors and omissions</b>	<b>64.0</b>	<b>-216.2</b>	<b>-129.0</b>		
BALANCE OF EXTERNAL TRANSACTIONS	-126.7	-160.4	-127.2		
IMF <sup>2</sup>	-42.9	-186.0	-67.4		
Change in foreign exchange reserves	-112.6	6.9	-5.7		
Change in SDRs	0.8	-12.1	-0.9		
Change in clearing accounts	28.0	30.8	-53.2		

(1) Public and private sector.

(2) Minus (-) sign denotes credit drawdown.

Note: Data for 1974 and 1975 revised on the basis of current parities.

from Western Germany, has apparently contributed to the increase in these deposits. A DM 300 million loan on behalf of the National Bank of Greece constituted the largest part of commercial bank foreign loans. The first part of this loan (DM 150 million or \$62.7 million) was absorbed in 1976.

Amortization payments for public and private debts increased slightly (1 per cent compared with 90.7 per cent in 1975), reflecting an uneven scheduling of payments for servicing the country's foreign debt.

The financing of the current account deficit by the inflow of autonomous private capital greatly reduced the country's foreign borrowing requirements. In 1976 public sector borrowing was smaller than the corresponding amortization payments, thus reducing the outstanding public foreign debt. The largest share of government borrowing consisted of American bank credit for the financing of imports of agricultural products. The largest part of public enterprises' borrowing is accounted for by a \$75 million loan to the Public Power Corporation. Finally, IMF has granted to the Bank of Greece 58 million SDRs (equivalent to \$67.4 million) as a compensatory financing.





## BANK OF GREECE

49TH YEAR

## GENERAL BALANCE SHEET

31st December 1976

(In drachmae)

ASSETS			1976			1975			LIABILITIES			1976			1975		
GOLD AND FOREIGN EXCHANGE									SHARE CAPITAL			262,500,000.—			262,500,000.—		
I. Bank's holdings			39,241,677,337.05			37,157,337,258.55			RESERVES								
II. Gold tranche with IMF			—			—			I. Regular reserve			262,500,000.—			262,500,000.—		
III. Special Drawing Rights on IMF			727,740,572.30			733,264,468.90			II. Special reserve from the sale of shares above par			486,428,000.—			486,428,000.—		
BALANCES UNDER BILATERAL TRADE AGREEMENTS			—			936,044,780.35			III. Provision according to Art. 71 of the Statutes			860,588,000.—			694,394,000.—		
COIN			420,823,902.60			82,719,195.75			IV. Provision for foreign exchange risks			304,600,000.—			304,600,000.—		
DOMESTIC BILLS DISCOUNTED			3,437,127,622.—			1,765,488,122.30			V. Other provisions			215,746,273.50			194,796,082.60		
LOANS AND ADVANCES									FUND RESULTING FROM THE REVALUATION OF ASSETS (R.D. 14/27.11.56)			31,691,569.35			31,691,569.35		
I. To the Government									FUND RESULTING FROM THE REVALUATION OF LAND AND BUILDINGS (LAW 542/14.2.77)			807,147,959.—			—		
1. Current Receipts & Payments account			—			2,463,367,916.15			NOTES IN CIRCULATION			112,726,795,900.—			93,995,896,050.—		
2. Purchases under Consumer Goods account			47,490,434,433.30			31,010,453,173.20			I. Government Current Accounts								
3. Treasury bills			2,705,600,000.—			1,087,650,000.—			1. Government Departments accounts ...			5,927,643,736.75			4,716,074,883.40		
4. Loans under special agreements									2. Public Investment accounts			3,732,630,735.65			2,453,351,984.55		
a. Loans for membership in international financial institutions			6,140,959,747.15			5,125,122,607.35			3. Special accounts			4,698,108,820.55			4,506,630,950.80		
b. Long-term loans			6,425,786,313.—			8,235,683,273.—			4. Current Receipts & Payments account			2,946,290,206.85			—		
II. To Banks and Others									II. Deposits								
1. Advances			90,128,381,245.80			77,318,463,175.35			1. Banks			22,614,843,370.85			15,806,107,292.05		
2. Advances out of public entity funds deposited with the Bank			46,269,115,393.40			41,798,423,006.15			2. Advance deposit requirements on imports			3,508,471,143.50			6,612,802,423.15		
INVESTMENTS			76,267,110.30			167,039,163,151.20			3. International institutions			17,275,037,725.80			11,807,844,103.85		
PREMISES AND EQUIPMENT									4. Public entities			51,898,026,972.60			46,541,758,014.95		
1. Land			787,947,525.85			163,390,986.80			5. Other deposits			1,914,058,788.55			1,680,148,894.15		
2. Buildings and equipment			1,614,960,340.—			778,912,923.60			6. Dividends for 1976			172,500,000.—			150,000,000.—		
Less depreciation:									SIGHT LIABILITIES IN FOREIGN EXCHANGE			5,731,398,774.85			4,692,733,478.20		
Up to 1975			1,113,293,308.80						BALANCES UNDER BILATERAL TRADE AGREEMENTS			983,714,463.05			—		
In 1976			50,434,272.25			527,879,811.50			ALLOCATION OF SPECIAL DRAWING RIGHTS (IMF)			1,987,438,032.55			1,927,861,735.65		
1,163,727,581.05			451,232,758.95			155,843,154.55			OTHER LIABILITIES			68,311,826,703.25			70,870,249,126.10		
VALUE OF BANK-NOTE PRINTING MATERIALS			210,686,944.60			122,623,774.75											
Less depreciation			35,374,387.30			59,674,956,097.05											
OTHER ASSETS			63,481,580,657.65			267,998,368,588.80											
			307,659,987,176.65									307,659,987,176.65			267,998,368,588.80		

## PROFIT AND LOSS ACCOUNT

DEBIT		1976		1975		CREDIT		1976		1975	
Personnel Remuneration - Pensions						Earnings from transactions with the Govern- ment .....		574,222,937.10			
Wages and salaries.....		1,275,469,985.35				Earnings from foreign exchange transactions		746,944,693.20			
Pensions (Laws 759/1937, 2510/1953 etc.)		119,745,622.—				Earnings from other transactions.....		4,552,971,791.05		5,874,139,421.35	
Principal and supplementary pensions to retired personnel		400,996,545.—									
Payment of contributions to personnel insurance funds outstanding from previous financial years		41,833,972.—		1,838,046,124.35							
Contributions to Personnel Insurance Funds:											
Pension Fund .....		182,691,347.—									
Supplementary Pension Fund.....		116,993,552.—									
Self Insurance Fund .....		46,258,837.—									
Health Insurance Fund .....		52,998,605.50		398,942,341.50							
Contributions to other Social Insurance Funds and Organisations .....				61,577,782.—							
Other Administrative Expenses				144,875,977.30							
Depreciation:											
Bank-note printing materials .....		35,374,387.30									
Buildings and equipment (other than office equipment) .....		39,510,437.15									
Office equipment .....		10,923,835.10		85,808,659.55							
Provisions											
Provision according to Art. 71 of the Statutes		166,194,000.—									
Sundry provisions .....		21,000,000.—		187,194,000.—							
				2,716,444,884.70							
Net Profit for 1976				3,157,694,536.65							
				5,874,139,421.35				5,874,139,421.35		5,679,516,347.05	









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BANK OF GREECE

SUMMARY  
OF THE  
STATEMENT

OF  
GOVERNOR XENOPHON ZOLOTAS  
AT THE ANNUAL MEETING  
OF SHAREHOLDERS, 29 APRIL 1976



ATHENS  
1976

HOWARD ROSS LIBRARY  
OF MANAGEMENT

MAY 13 1976

McGILL UNIVERSITY











BANK OF GREECE

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ATHENS  
1976



Printed in Athens, Greece  
at the Bank of Greece Printing Works

## I. PROBLEMS AND PROSPECTS OF THE GREEK ECONOMY

### 1. ECONOMIC RECOVERY AND CONTROL OF INFLATION

Taken as a whole, economic developments in 1975 may be considered satisfactory. Thus, economic activity last year recovered at a slow but steady pace, which is reflected in the growth of GDP at factor cost by 3.7 per cent. Economic recovery is continuing this year, in which the forecast is for a 4 to 5 per cent increase in GDP.

A further positive development was the reduction of the deficit on current account by \$209 million, i.e. from \$1,218 million in 1974 to \$1,009 million last year. At the same time, there was a significant increase in the ordinary inflow of capital and an improvement in its composition. As a consequence, requirements for accommodating borrowing were about 50 per cent less than in 1974.

Finally, the consumer price index in 1975 rose by 15.2 per cent against 13.5 per cent in 1974. The latest increase lies within the limits of initial forecasts and is due to higher indirect taxes (for at least a quarter of it) and the continuing rise in the prices of many imported goods. However, regardless of specific causes, the acceleration of inflationary trends in 1975 — even though slight — was an adverse development, especially since the rate of inflation in most other countries is slowing down. The Government is right, therefore, in having made it a central objective of its economic policy for 1976 to hold the rate of inflation below 10 per cent. This rate is close to the average forecast for the European members of the OECD and is consistent with the aim of accelerating economic growth and bringing about a further improvement in the balance of



payments. The attainment of this goal depends primarily on (i) the implementation of prudent monetary and credit policies, (ii) a sound fiscal policy, and (iii) equally important, keeping the increase in incomes within the limits of the economy's capabilities.

## 2. THE ROLE OF MONETARY POLICY : TARGETS AND MEANS

The rate of increase in currency circulation started slowing down in the second half of 1975. Although borrowing requirements in both the private and the public sector were and still are large, currency circulation grew at a slow rate in the first quarter of 1976. During this quarter its average level was only 5 per cent higher than in the same quarter of 1975.

On the other hand, credit expansion in 1975 was very high. It approached a total of Dr. 113 billion, of which 57.9 per cent went to the private sector and 42.1 per cent to the public sector of the economy. The substantial credit expansion that took place in the second half of 1974 and continued for the best part of 1975 was aimed at helping the economy out of the recession.

As for 1976, the monetary authorities are determined to keep the rate of increase in currency circulation around 12 per cent. This is consistent with the other objectives of economic policy, namely to ensure an increase of 4 to 5 per cent in real GDP, to hold the rate of inflation below 10 per cent, and to bring about a further improvement in the balance of payments. In this context, the Currency Committee and the Bank of Greece will continue supporting economic recovery by ensuring a sufficient supply of funds to satisfy the demand for both long-term investment and short-term credit to meet current production requirements in working capital. However,



they are not prepared to permit an excessive expansion of currency circulation, which might be used for financing, even indirectly, less productive or socially undesirable activities and could have serious inflationary implications.

To this effect, credit expansion and the liquidity of the banking system have been brought under stricter control. At the same time, steps are being taken to rationalise the distribution of available financial resources so as to reduce the dependence of certain credit institutions on Bank of Greece funds and thus prevent burdensome increases in currency circulation. Under this policy, the flow of funds from the Bank of Greece to institutions specialising in long-term credit financing will be cut off completely or to a very significant extent during the current year. In anticipation of these developments a number of investment banks have recently started selling bonds (one-year maturity with the option of being extended for two more years on the same terms) directly to the public. The issue of these bonds is expected to increase the amount of savings mobilised through these intermediaries and bring about a more rational allocation of available funds among the various financial institutions, thereby also enhancing the effectiveness of monetary policy.

For the same purpose, redepositing by the Postal Savings Bank with the commercial banks has in effect been stopped since the last months of 1975. Moreover, withdrawals may be decided during the course of the year if this is felt necessary for controlling the liquidity and credit expansion of commercial banks. At the same time, the banks have been offered the option of placing funds intended for investment in interest-bearing treasury bills in an interest-bearing account with the Bank of Greece. In essence, this permits proper timing of government borrowing from domestic sources, in line with monetary policy objectives.



One of the basic problems that will have to be dealt with over the next few years is to restore the savings to national income ratio to its pre-inflation level. Since 1973, under the influence of inflation and economic recession, this ratio has fallen by 7.2 percentage points, i.e. from 22.9 per cent of national income in 1972 to 15.7 per cent in 1975. To restore this ratio to the level attained prior to the inflationary phase and the recent economic slump is a fundamental requirement for supporting the large amount of investment needed to achieve the desired rate of economic development, under conditions of monetary stability. Otherwise, the inadequacy of savings may in the near future become a serious constraint on the country's economic development.

### 3. CREDIT POLICY AND CONTROL OF THE BANKING SYSTEM

Since the autumn of 1974, the objective of credit policy has been to ensure a responsive supply of bank credit for financing productive investment, primarily in the industrial sector, and for promoting exports. For this purpose, long-term lending for industrial investment and short-term export financing by the commercial banks have been excluded from the ceiling on bank credit to the private sector since August 1974. At the same time, public and private special credit institutions have been supplied with sufficient funds to satisfy the demand for long-term capital to finance productive investment.

Short-term lending by the commercial banks was kept under an overall ceiling last year, which, however, was high enough to satisfy working capital requirements arising from increased output and the growing cost of inputs. The monetary authorities permitted a large expansion of credit to the private sector for the best part of last year, mainly for the purpose of



halting the recession and assisting in the recovery of the economy. In fact, credit policy played a significant part in putting an end to the decline in industrial production, both by relieving the liquidity problems of a large number of firms and by promoting their sales through increased amounts of suppliers' credit.

For the current year, the objective of the monetary authorities is to prevent the undertaking of new economically sound investment projects (chiefly in manufacturing, agriculture and tourism) from coming up against an insufficient supply of long-term bank credit. To encourage industrial investment, long-term lending rates are kept lower than those applicable to short-term loans by the commercial banks. Also, the system of interest rate subsidisation by the Government has been retained in the case of long-term loans intended to finance industrial investment outside the Greater Athens area. As a result, the cost of long-term bank credit for industrial projects can be, and often is, substantially less than the cost of the corresponding funds.

Cooperation between the Currency Committee and the management or executive staff members of the banks is instrumental in ensuring a flexible credit policy that can be adjusted promptly to the course of economic activity and to developments in prices, the balance of payments, the resources available to the credit system and public sector requirements for borrowing. Such cooperation provides the opportunity for proper evaluation of prevailing credit conditions, while at the same time credit institutions can be given general and/or specific directions regarding their portfolio policies in response to current conditions and requirements. Needless to say, credit expansion is kept in line with the overall monetary and credit policies laid down by the Currency Committee.

For the near future, the authorities are contemplating



a reform of the present system of credit controls and regulations. This reform will be based on :

First, the abolishment of a number of selective credit controls and the simplification of credit regulations. The aim is to give the banks greater responsibility and initiative in selecting their loans according to certain general principles and criteria that will be established by the Currency Committee. In addition, some general rules relating to the asset structure of commercial banks will also be adopted so as to favour the financing of economic sectors and activities of higher priority, while at the same time safeguarding the stability of the banking system.

Second, the consolidation of interest rates on bank loans. The interest rate structure must gradually come to reflect to a greater extent the customary banking criteria of security, liquidity and yield. Instead of the prevailing interest rate subsidisation system, whenever subsidies are considered necessary for development purposes, they will be paid out of a special account, according to the provisions of a law enacted in 1975.

Finally, the emphasis of credit inspection will be shifted from checking for formal violations of credit regulations to a broader evaluation of the banks' lending activities and to an investigation of whether, and to what extent, credit institutions select their assets according to principles and criteria consistent with the objectives of credit policy.

It is expected that the foregoing measures, together with those designed to bring about a reallocation of savings among the various sections of the credit system, will enhance the effectiveness of monetary policy and help distribute bank credit in such a way as to serve development purposes.



#### 4. PUBLIC SECTOR BORROWING REQUIREMENTS AND ECONOMIC EQUILIBRIUM

The high borrowing requirements of the public sector over the last two years had a strong expansionary effect on currency circulation, which is continuing this year. For 1975, public sector borrowing from domestic and foreign sources is estimated at Dr. 46 billion and corresponds to 6.8 per cent of GDP. For the current year, the borrowing requirements of the public sector are put at Dr. 53 billion, representing about the same percentage of GDP as in 1975. In effect, however, the pressure to be exerted by the public sector on currency circulation this year will be substantially greater if the special levy on business enterprises, reckoned on the basis of the outstanding balance of their bank borrowing, is also taken into account.

The financing of cash deficits in the public sector was economically advisable and did not cause monetary disturbances so long as the economy was in a recession. Following the recovery of economic activity, however, it is essential that public sector borrowing requirements be gradually restrained and eventually stabilised at a level which will be in line with normal rates of increase in currency circulation. Otherwise, it will either become necessary to restrict credit expansion to the private sector of the economy or the amount of public expenditure will give rise to serious monetary disturbances.

The rapid growth of public expenditure in recent years is partly due to special reasons, such as the need to strengthen the country's defence capability and at the same time expand and improve public education and health facilities as well as other social services. To a significant extent, it is also due to the increase in the money incomes of those employed in the public sector. Although this increase has been necessary in



order to compensate for the erosion of real incomes caused by inflation, it has been only slightly offset by improvements in productivity. This is true both of Central Government departments and of public organisations and enterprises. Inept interventions in important government agencies during the dictatorship and the absence of any effort to improve their organisational structure and methods of operation led to reduced productivity.

Similar conditions have been created in the case of public enterprises. The result has been a sharp increase in their operating cost and a reduction in the capability of financing their own investments. These conditions have led to a large increase in the dependence of public enterprises on borrowed funds. Moreover, the worsening of their financial position tends to become permanent.

The slowdown of inflation and the gradual recovery of economic activity will eventually reduce the severity of the problem of financing public expenditure. However, unless the authorities take steps to eliminate the structural causes of deficits in Central Government and public enterprises, a substantial decrease in public sector borrowing requirements does not seem likely, even if inflation is brought under control and economic activity returns to normal.

Furthermore, it is of paramount significance that the best methods of financing public sector deficits be chosen so that the burden on currency circulation can be reduced as far as possible. In this respect, a basic aim since last year has been to transfer the financing of investment programmes of public enterprises from the Bank of Greece and the Postal Savings Bank to the commercial banks, which attract a large proportion of private savings. In addition, however, it is essential that the Central Government's investment programme, which seems to include projects of low productivity, be revised.



Similar remarks can be made about the investment programmes of public enterprises and organisations.

## 5. INCOMES POLICIES

Since the summer of 1974, government policy has been aimed at restoring the purchasing power of wage-earners, which had been eroded by inflation during the preceding period. The high rate of increase in money wages pushed up the cost of labour per unit of output (the increase in labour cost for manufacturing between the third quarter of 1974 and the fourth quarter of 1975 is estimated at 23.6 per cent) and was the principal factor underlying the rise in prices. Nevertheless, the incomes policy pursued by the Government was justified both on social and economic grounds. Initially it helped stimulate consumer demand and bring recession to a halt, while later on it promoted economic recovery.

The increase in money wages, however, must not exceed a certain limit, beyond which it would create serious risks concerning the future course of the economy. Hence, to hold the rate of inflation below 10 per cent during the current year, it is imperative that the increase in wages and salaries be slowed down.

At the same time, support prices for agricultural products cannot be set higher than international prices, since the result would be to impair the competitiveness of Greek agriculture or lay an excessive burden on the government budget for subsidies. Nor is it advisable for government intervention to lead to a price structure unfavourable to the changes which are necessary in restructuring agricultural production. Therefore, it is expedient that the improvement of farmers' incomes should be sought primarily by means other than price supports.



For this purpose, effective measures should be taken to reduce the high cost of marketing and the high profits realised from selling agricultural products, especially perishables. The solution might be found partly in stricter market inspection. Primarily, however, it should be sought to encourage new forms of trade organisation, with the ultimate objective of reducing the number of middlemen and the cost of product handling and profit margins. It should be stressed that the maintenance of prices at high levels, owing to the uneconomic organisation of product marketing or the unjustifiably high profits of middlemen, restricts the demand for agricultural products and often bars a good part of agricultural output from reaching the market. Thus, the conditions prevailing in the marketing of agricultural products turn out to be harmful to the country's agricultural economy.

Finally, the authorities must take effective steps so as to prevent an excessive increase in profits, especially through the abuse of monopoly power. This is a serious risk, considering the present structure of many markets for goods and services. To avert this risk, it is imperative that the proposals concerning the exercise of effective control over monopoly and oligopoly situations be implemented the soonest possible. Similarly, careful government interventions through the price mechanism and the timely introduction of suitable measures to supply the market with staple foodstuffs can avert maladjustments in the operation of the market and prevent or neutralise speculative price increases, which do not originate in the increased cost of production and are economically unjustified.

The preceding remarks point to the pressing need for an effective prices and incomes policy, which must be the principal element in the country's anti-inflationary strategy. Without a suitable incomes policy, strict and effective control



of speculative price increases, and self-restraint in the pursuit of the legitimate income claims of various social groups, it will be difficult to bring inflation under control.

## 6. RESTORATION OF BALANCE-OF-PAYMENTS EQUILIBRIUM

In spite of last year's improvement, the balance of payments is still a serious problem for the country, considering that for the third successive year the deficit on current account exceeded \$1 billion. To a significant extent, the improvement in 1975 is associated with a reduction in the volume of imports, owing largely to the slackness of economic activity or perhaps the liquidation of stocks of imported goods, which had been accumulated for speculative reasons during the preceding period of high inflation.

Specifically, while imports at constant prices declined for two consecutive years, exports of goods moved at relatively high levels throughout 1974 and most of 1975. The international recession affected mainly invisible earnings, although not uniformly as regards their three basic sources. Tourism, after its sharp decline in the summer of 1974 under the influence of non-economic factors, showed an impressive increase last year and helped to reduce the deficit on current account. Receipts from emigrants' remittances displayed relative stability and also showed an increase last year. Finally, foreign exchange earnings from shipping showed considerable gains for most of 1974 but were affected by the decline in the volume of international trade in 1975.

These considerations and the investigation of the nature of the balance-of-payments deficit lead to the conclusion that even if the cyclical effects of foreign exchange receipts and payments are eliminated, the current account deficit will



not be substantially reduced. This means that the balance-of-payments problem is basically structural. Nevertheless, the gradual reduction of requirements for accommodating borrowing — particularly the fact that these requirements were reduced in 1975 to about half of the corresponding needs in 1974 — shows that it will not be difficult to restore equilibrium in the balance of payments.

The recent improvement in the international competitiveness of the Greek economy has been based, to a significant extent, on foreign exchange policy. Specifically, by following the dollar in its depreciation, between the beginning of September 1974 and the end of January 1975, the competitive position of Greek products was strengthened, both in foreign markets and in the home market. Since March 1975, when the drachma was disengaged from the dollar, the parity of the drachma has been linked to the weighted average rates of a basket of currencies of Greece's major trading partners. In this way, the weighted average exchange rate of the drachma remained almost unchanged up to the beginning of last July. In July, following the renewed appreciation of the dollar, it was decided to link the drachma to the movements of the European currencies. The same policy will also be followed in the future, based mainly on the criteria of preserving the competitiveness of the Greek economy and avoiding any serious consequences on the level of domestic prices.

It should be stressed, however, that the policy regarding the parity of the drachma can only be used as a supplementary means of improving the balance of payments. For it is impossible to maintain a permanent balance in the country's external transactions through readjustments in the parity of the drachma, given that they increase the cost of imports and strengthen inflationary pressures. In addition, exchange rate readjustments do not provide a lasting solution since other



countries also proceed to competitive devaluations which easily neutralise the comparative advantage gained from readjustments in the parity of the drachma.

## 7. ACCESSION TO THE EEC AND ECONOMIC DEVELOPMENT

Accession to the EEC requires considerable changes in the structure of the economy, a higher degree of specialisation, increased export orientation, institutional reforms, and a change in working methods and habits. Private businesses as well as government agencies must realise that accession to the EEC means that competition, both foreign and domestic, will become keener and that business choices and decisions will have to rely, to an increasing extent, on market information. This implies that the adjustment of the Greek economy to the conditions prevailing in the EEC, combined with a minimisation of social cost, presupposes (i) that competitive conditions will be established as soon as possible in the domestic market, and (ii) that private and public enterprises will be forced to establish suitable conditions and mechanisms for selecting, planning and implementing their investment projects, and for improving their managerial methods and the quality testing and marketing of their products.

The first of these prerequisites means that the present system of government interventions and regulations must be reviewed for the purpose of eliminating existing obstacles in the operation of the market mechanism. It should be noted that many forms of such intervention and regulation, as well as the structure of financial incentives, often generate conditions of unequal competition between business firms, even within the same industry. In addition, they hinder the entry of new firms and foster oligopoly and monopoly situations, which dis-



courage investment and enable business firms to maintain high profit margins. Finally, it seems that the whole system of incentives and government interventions often favours less efficient firms or firms with no growth potential at the expense of other firms in the same field, which promise to grow and become internationally competitive.

Broadly speaking, the rationalisation of the system of government interventions and regulations, the simplification or elimination of superfluous bureaucratic procedures and the restoration of competitive conditions are essential for creating an appropriate industrial environment, which is of basic importance for increasing private industrial investment and improving its composition. These questions can and must be dealt with successfully in the new five-year economic development plan which is being drawn up by the Government.

Furthermore, the achievement of a satisfactory pace of economic development over the next few years depends on the rapid expansion of investment activity, especially in the manufacturing sector. According to existing indications, the stagnation of industrial investment continues, even though this year the Greek economy has entered a phase of recovery, uncertainty has receded and the business world is, in its majority, optimistic about the future progress of the economy. The latter is clearly evident from the monthly survey carried out by the Economic and Industrial Research Institute.

The recovery of industrial investment is imperative not merely in order to expand productive capacity and satisfy growing demand in the near future. It is equally important, especially in view of the country's accession to the EEC, for ensuring the restructuring of the economy and enhancing its export orientation and competitiveness. It is only in this way that accession will enable Greece to benefit from the reallocation of industrial activity within the European area. Further-



more, it should be kept in mind that the process of tariff elimination will be speeded up during the next few years and that other forms of protection against foreign competition will be gradually abandoned.

Needless to say, private investment cannot be increased merely by ensuring an elastic supply of long-term bank credit. The process of industrial investment necessarily begins within each firm with the identification of new development opportunities, which guarantee a satisfactory return on investment. The problem of insufficient profitability in certain lines of industrial production seems to co-exist with the problem of unjustifiably high monopolistic profits in other lines of industrial activity. Consequently, while the improvement of the growth rate of investment calls for the creation of favourable conditions and possibilities for increasing profitability in industries of the first group, it is also imperative to take effective measures in order to neutralise monopoly power and reduce profit margins in industries of the second group. The control of monopoly profits and the establishment of competitive conditions will have favourable effects on the allocation and use of available financial resources and can help to accelerate the growth rate of investment and economic development.

Finally, it is essential to mobilise the state agencies established to supplement the task of private business initiative. Both the Hellenic Industrial Development Bank (HIDB) and the Hellenic Industrial and Mining Investment Company (HIMIC) consortium have been set up to contribute to the realisation of investment projects of primary importance to the country's industrial development. It is necessary to activate both these organisations, particularly during the present period, in which private investment activity is inadequate for reasons partly related to international economic conditions and to the existence of idle productive capacity in certain industries.



It should be stressed that the HIDB and the HIMIC do not intend to compete with private enterprise, nor to establish bureaucratic enterprises, which would remain permanently under the control of the state or the banks. The shares and control of the companies to be formed will be transferable to the public and it is advisable for the organisations in question to set up enterprises in cooperation with private venture capital wherever this is possible.

## II. ECONOMIC DEVELOPMENTS IN 1975

### 1. NATIONAL INCOME IN 1975

During 1975 real GDP at factor cost increased by 3.7 per cent (1974 : -1.0 per cent). Real output of the agricultural sector in value added terms grew at a rate of 3 per cent, compared with 11.4 per cent in 1974. Secondary production and manufacturing output both grew at a rate of 4.3 per cent, while that of mining rose by 2.5 per cent, of construction by 3.9 per cent and of public utilities by 6.1 per cent. Finally, the service sector grew by 3.6 per cent and net income from abroad recorded a 13 per cent fall, against a 9.3 per cent decrease in 1974.

### 2. EXPENDITURE OF THE ECONOMY

The growth rate of final demand for 1975 was 5 per cent at constant market prices. Aggregate consumption is estimated to have risen by 5.9 per cent. Public current expenditure rose by 12.3 per cent and private consumption grew by 4.7 per cent, having partly adjusted to the present level of disposable private income.

Gross fixed capital formation increased by 1.7 per cent. The declining trend was reversed by a 5.6 per cent increase in private investment, which was partly offset by a reduction in public capital expenditure.

In the past two years, private capital formation was primarily influenced by developments in the housing sector. Investment in capital equipment fell by 5 per cent as a result of a reduction in capital expenditure of public enterprises. On the contrary, the indications are that private investment in capital equipment increased during 1975. However, this development should not be interpreted as indicating the course of investment in manufacturing in the near future, since insufficient demand remains the principal negative factor in this respect.

### 3. AGRICULTURAL OUTPUT

It is estimated that the volume of agricultural output rose by 2.9 per cent in 1975, compared with 9.2 per cent in 1974. The slow growth rate of



agricultural output during the year was primarily caused by small gains in livestock production and in crop output. The increase in agricultural output was the final outcome of fluctuations in the production of a small number of crops, which represent less than 30 per cent of the total gross value of agricultural output. Specifically, large increases were recorded in the output of sugar beet, tobacco, fruit and olive oil.

These developments are in line with the policy aimed at improving crop structure by encouraging producers to shift to crops which are of high income yield per unit of land input, and for which demand conditions are favourable. However, no progress was made in 1975 towards increasing meat and animal feed production.

#### 4. INDUSTRIAL OUTPUT

The recovery which started in the autumn of 1974 continued throughout 1975, although at a slower pace. Manufacturing output increased by 4.5 per cent. The increase in the output of this sector was primarily caused by an 8.4 per cent rise in the production of consumer goods. The output of capital goods rose by only 1.5 per cent, whereas the production of consumer durables fell by 11.2 per cent.

Output from the mining sector was influenced by the decline in the metallurgical industry's demand for raw materials and by a substantial rise in lignite output for the production of electricity. Finally, the production of electricity increased by 6.5 per cent.

#### 5. EMPLOYMENT AND WAGES

There were no significant changes in the level of employment. The number of placements remained virtually unchanged, and dismissals recorded only a slight increase. However, there was a rise in the unemployment rate, which was caused by persons seeking employment for the first time and by the repatriation of Greek workers from Western Europe. Specifically, there was a slight rise of employment in manufacturing (0.8 per cent), but the number of working hours per person fell by 2 per cent and total time of employment by 1.2 per cent.

During 1975, nominal wages and salaries recorded substantial increases. In the manufacturing sector, average hourly wage rates grew



faster than average weekly earnings, owing to the reduction in the number of working hours per employee. In real terms, the hourly wage rate in the manufacturing sector showed gains of 9.3 per cent, while the rise in average weekly earnings was 7.1 per cent.

## 6. PRICES

Prices continued to rise in 1975, but with considerable fluctuations. The consumer price index rose by 15.2 per cent and the wholesale price index by 10.1 per cent. The substantial rise in the prices of services accounted for about 36 per cent of the increase in the overall index, while another significant percentage was contributed by the increase in food prices.

The increase in the wholesale price index was caused primarily by a 14.6 per cent rise in the price index for "final products of domestic primary production for home consumption" and by an 8.6 per cent rise in the price index for "final products of domestic industrial production for home consumption", with both increases accounting for approximately 83 per cent of the total rise in the wholesale price index.

## 7. MONETARY DEVELOPMENTS

During 1975, money supply (currency in circulation plus sight deposits) grew at the rate of 15.6 per cent compared with 19.7 per cent in 1974. This slowdown in the rate of growth of money supply was caused primarily by developments in the private sector, and specifically by the high growth rate of savings deposits. On the other hand, liquid assets of the private sector in their broader sense (currency in circulation plus private deposits in drachmas) increased faster than GNP at current prices. Of the components of money supply, currency in circulation increased at a rate substantially lower than in 1974, whereas the growth rate of sight deposits was much higher than in 1974.

After 1972, income velocity of currency circulation was influenced by several economic and non economic factors. Specifically, rapidly rising prices and the ensuing psychological climate led to a tendency to reduce assets in the form of cash holdings. This tendency started in the last months of 1972, became more pronounced in 1973 and continued into the first months of 1974. However, in July and August 1974, under



the impact of non economic factors, a part of deposits was converted into cash. Thus, demand for money rose sharply in those two months. In September 1974, the deposits which had been withdrawn started flowing back into the banking system.

By mid-1975, the influence of non economic factors receded and demand for money started to regain normal levels. The decline in the demand for money was accompanied by an upturn in the growth rate of deposits. However, the average level of currency in circulation continued to be high in 1975, owing to developments in the second half of 1974 and the first half of 1975. As a result, last year there was a drop in the income velocity of currency circulation. It should be stressed, however, that since mid-1975, currency in circulation has tended to move back to normal levels, which is confirmed by the further drop in the growth rate of currency in circulation during the first months of 1976.

In 1975, the public sector had an expansionary effect on money supply amounting to Dr. 38,198 million, against Dr. 24,626 million in 1974. The expansionary effect was primarily exerted by the Central Government and secondarily by public enterprises, whereas public entities exerted a contractionary effect. On the other hand, the private sector had a contractionary effect on money supply amounting to Dr. 4,407 million, compared with an expansionary effect of Dr. 10,202 million in 1974. The substantial growth of private deposits more than compensated for the fact that credit expansion in 1975 was much higher than in 1974. Similarly, the foreign sector exerted a contractionary effect on money supply in 1975 to the extent of Dr. 26,714 million.

## 8. MONETARY AND CREDIT POLICIES

The monetary and credit policies implemented in 1975 aimed at helping economic activity to recover, and at the same time at curbing price increases and improving the balance of payments. The main measures taken under the monetary and credit policies in 1975 can be summarised as follows :

- Credits granted by commercial banks and subject to the overall credit ceiling were permitted to grow by 17 per cent.

- The suspension of new housing loan approvals, in force since



1972, was discontinued in 1975. At the same time, the amounts granted under each category of loans were increased.

—In mid-1975, the percentage of compulsory interest-bearing deposits with the Bank of Greece on savings deposits was raised from 0.5 to 7 per cent, while the percentage of compulsory non interest-bearing deposits on private sight and restricted deposits was raised from 5 to 7 per cent.

—In September 1975, the rediscount rate was raised from 8 to 10 per cent. This is in line with the new levels and structure of interest rates applicable to deposits and loans as from October 1975.

—In July 1975, interest rates on time and savings deposits were lowered by half a percentage point. In October 1975, interest rates on savings deposits were reduced by another percentage point, while interest rates on time deposits, savings deposits on notice and checking accounts held by individuals were lowered by half a percentage point.

—Moreover, the interest rate on sight deposits was abolished, while the interest rate on restricted deposits held by persons permanently residing abroad was raised from 0.75 to 7 per cent.

—In October 1975, the interest rates charged on bank loans were lowered by half a percentage point, excluding credits to the agricultural sector.

## 9. BANK CREDIT

The outstanding balance of bank credit to the private sector rose by 24.4 per cent in 1975, compared with 20.1 per cent in 1974 and 18 per cent in 1973. The higher rate of credit expansion in 1975 resulted mainly from short-term credit, which rose by about 32 per cent. On the contrary, long-term credit recorded a smaller growth rate for the second consecutive year, owing to low investment activity.

Commercial bank credit recorded high growth rates in 1975 and accounted for approximately 60 per cent of total credit expansion to the private sector. Short-term bank credit to the private sector increased at the rate of 32.7 per cent, whereas long-term credit grew by 22.7 per cent. Almost half of the overall increase in bank credit to the private sector was extended to manufacturing and mining. Furthermore, there was a significant increase in credit to handicraft and trade.



Finally, credit to the agricultural sector grew at the rate of 27.3 per cent.

#### 10. DEPOSITS

Private deposits recorded high rates of growth in 1975, when they increased by 32 per cent, compared with 18.5 per cent in 1974. The rapid growth of deposits is related to the slowdown in the price rise as from the second half of 1974, and to more favourable prospects as regards future developments.

A rapid increase was also recorded by private deposits in foreign exchange, which increased by 51.5 per cent, compared with 26.9 per cent in 1974.

#### 11. PUBLIC FINANCE

Total revenue under the overall government budget for the fiscal year 1975 amounted to Dr. 138,304 million, while total expenditure amounted to Dr. 169,780 million. Thus, there was a deficit of Dr. 31,476 million. If the deficits resulting from the government's policy of supporting agricultural incomes and subsidising the consumption of essential food-stuffs are added, the total deficit of the Central Government budgets comes up to Dr. 41,176 million. Of this deficit, 39 per cent was financed by domestic borrowing through issuing interest-bearing treasury bills, 37.4 per cent by borrowing from abroad and 23.6 per cent by borrowing from the Bank of Greece.

The ordinary budget for the fiscal year 1975 was balanced. Tax revenue rose by 24.6 per cent mainly from indirect taxation. This increase was largely due to tax measures introduced early in 1975. Revenue from direct taxation recorded a 4.1 per cent increase, exclusively due to new taxes on ships and real estate. Receipts from the other direct taxes were adversely affected by changes in income taxation, especially by the reduction of the tax burden of the lower and middle income groups. On the expenditure side, outlays for strengthening national defence showed the highest increase. High growth rates were also observed in outlays for health, education and other social services, as well as for servicing the public debt.



Expenditure of the Central Government investment programme totalled Dr. 32,550 million in 1975, and recorded a 39.8 per cent increase. The growth in government investment was one of the main factors that contributed to the stimulation of the economy. Government capital expenditure was financed to the extent of Dr. 1,074 million from public investment revenue, while the balance came from domestic borrowing (through the issue of interest-bearing treasury bills) and borrowing from abroad.

The overall government budget for the fiscal year 1976 provides for total revenue of Dr. 172,500 million and total expenditure of Dr. 212,500 million. The resulting deficit of Dr. 40,000 million is expected to be financed from domestic borrowing (62 per cent) and from foreign borrowing (38 per cent).

In particular, the revenue of the ordinary budget is estimated at Dr. 171,500 million, of which Dr. 46,000 million will originate in direct taxation, Dr. 112,300 million in indirect taxation and Dr. 13,200 million will come from other ordinary and extra-ordinary revenue. Tax revenue is expected to increase by Dr. 37,600 million. Of this, Dr. 11,500 million will accrue from the yield of the special tax, reckoned on the outstanding balances of bank lending to businesses, and from other taxation arrangements. Finally, the public investment budget anticipates total payments of Dr. 41,000 million.

## 12. BALANCE OF PAYMENTS

Despite unfavourable international conditions during 1975, there was an improvement in the balance of payments. The current account deficit was reduced to \$1,009 million (1974 : \$1,218 million). At the same time there was a significant increase in the inflow of autonomous capital and an improvement in its structure.

The reduction of the deficit in the balance of payments resulted from, among other things, the exchange rate policy that was pursued during 1975. This policy helped maintain the competitiveness of Greek exports and exerted a downward influence on the private demand for imports. It should be stressed, however, that along with the improvement in the balance of payments, there was a substantial deterioration in the external terms of trade. Finally, the increase in the surplus of



invisibles contributed significantly to the improvement of the balance on current account.

The value of imports (payments plus suppliers' credits) reached \$4,876 million in 1975, against \$4,635 million in 1974. Considering import price increases, there was a decrease in the volume of imports for the second consecutive year. In value terms, there took place a decline in the imports of foodstuffs, raw materials and fuel, while imports of capital goods and manufactured consumer goods recorded an increase.

Export earnings grew by 10.4 per cent in 1975 and totalled \$1,960 million, against \$1,774 million in 1974, and there was a slight change in the structure of export earnings. In particular, the share of foodstuffs and minerals increased, while that of tobacco, raw materials and semi-finished products, and petroleum products decreased. Finally, the share of industrial and handicraft products, which is the most important item, remained unchanged during the last two years.

The aforementioned developments in exports and imports of goods restrained the trade deficit, the level of which during 1975 was only slightly higher than in 1974, and resulted in an increase in the export to import ratio from 38.3 per cent in 1974 to 40.2 per cent in 1975.

Invisible earnings were \$2,652 million and payments amounted to \$745 million. As a result of these developments, there was a \$264 million increase in the surplus of invisibles (in comparison with 1974), and this was the main factor in the improvement of the balance on current account during the year under review. The growth of invisible earnings was primarily due to tourism, and to a lesser extent to emigrants' remittances. On the other hand, the crisis that hit international shipping started to affect earnings from shipping late in 1974 and brought about a slight decline in 1975.

The financing of the current account deficit was relatively easy, mainly owing to the rapid growth of the autonomous inflow of private capital, which drastically reduced accommodating borrowing requirements. The increase in capital inflow was mainly due to the restoration of confidence in the stability and future prospects of the Greek economy, and was enhanced by the interest rate policy on deposits in foreign exchange. Moreover, the structure of capital inflow was improved, considering that very high rates of increase were noted in deposits in foreign

exchange by Greek seamen and workers abroad, as well as in other private capital from Greeks residing abroad. It should be noted that a large part of these two items ultimately turns out to be unilateral transfers and thus does not require debt servicing. Total net capital inflow (including borrowing by the Government, the Central Bank and public enterprises) amounted to \$1,267 million, compared with \$1,047 million in 1974.





















