Christian Noyer: Presentation of the ECB Convergence Report 2000

Introductory statement by Mr Christian Noyer, Vice-President of the European Central Bank, at the presentation of the ECB Convergence Report 2000 to the Committee on Economic and Monetary Affairs of the European Parliament, Brussels, on 3 May 2000.

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It is a great pleasure for me to have the opportunity to present this year's Convergence Report, prepared by the European Central Bank (ECB), to your Committee. The report examines in-depth, with regard to Greece and Sweden, the achievement of a high degree of sustainable convergence, as well as compliance with the statutory requirements to be fulfilled by national central banks in order for them to become integral parts of the European System of Central Banks (ESCB).

In producing this report, the ECB fulfilled the requirements of Article 122 (2) in conjunction with Article 121 (1) of the Treaty to report to the Council of the European Union on the progress of Member States with a derogation, with regard to their obligations concerning the achievement of Economic and Monetary Union (EMU). It will now be up to the Council to decide, on the basis of the Convergence Reports prepared by the European Commission and the ECB, and of the Parliament's opinion and a proposal from the European Commission, whether or not the current derogation status of Greece and Sweden can be abrogated.

In view of the comprehensive assessment provided in our report, it goes without saying that I can only touch upon its main conclusions. However, in the following discussion we should have an opportunity to consider in more depth one or other aspect in which you might be particularly interested. I should like, first, to refer to our assessment of economic convergence in Greece and Sweden and then to address the requirements of legal convergence.

I. Assessment of economic convergence in Greece

As far as economic convergence in Greece is concerned, it is noted that Greece achieved an average rate of HICP inflation of 2.0% during the reference period (April 1999 to March 2000). This is below the reference value of 2.4%. Looking back, a clear trend towards lower inflation is discernible in Greece, with the CPI rate falling from 20.4% in 1990 to 2.6% in 1999. Inflation in Greece is now closer to a level which can generally be considered to be consistent with price stability. However, due attention needs to be paid to the fact that the recent reduction in inflation rates is partly attributable to temporary factors such as cuts in indirect taxes.

At the same time, future price developments in Greece are subject to a number of upward risks, in particular in 2001. Inflation rates will be influenced upwards as the recent cuts in indirect taxes will cease to have a moderating impact. Moreover, an eventual alignment of Greek interest rates with those in the euro area and the further convergence of the drachma towards its conversion rate will exert upward pressure on prices.

Turning to fiscal policy, the 1999 general government deficit ratio was 1.6%, well below the 3% reference value. By contrast, the debt ratio was 104.4%, ie far above the 60% reference value. Looking back over the years from 1990 to 1999, the deficit has been reduced considerably and in 2000 the deficit ratio is forecast to decrease further to 1.3% of GDP, while the debt ratio is projected to decline to 103.7%.

However, notwithstanding the efforts and the substantial progress made towards improving the current fiscal situation, there is an ongoing concern as to whether the ratio of government debt to GDP will be "sufficiently diminishing and approaching the reference value at a satisfactory pace" and whether sustainability of the fiscal position has been achieved.

Greece's public debt is falling only slowly, despite high primary surpluses and privatisation receipts. As a consequence, substantial primary surpluses and persistent, sizeable overall fiscal surpluses outperforming the targets of the updated Greek Convergence Programme are crucial if the debt ratio is to be reduced to 60% within an appropriate period of time. Tight fiscal policy will also be needed in order to contain the earlier-mentioned inflationary pressures.

As regards the development of long-term interest rates, which constitute another key variable within the overall convergence assessment, their level reached 6.4% on average during the reference period from April 1999 to March 2000. As a result, they stood 0.8%-point below the reference value for the interest rate criterion of 7.2%.

With regard to the fulfilment of the exchange rate criterion, it is noted that the Greek drachma has been participating in ERM and subsequently ERM II since 16 March 1998. During the two-year reference period (April 1998 to March 2000) the drachma traded significantly above its central rates. Exchange rate volatility declined significantly during the reference period and the significant short-term interest rate differentials also displayed a gradual decrease from September 1998 onwards. After a gradual depreciation during most of 1999 and a revaluation of the central rate by 3.5% in January 2000, the drachma was traded on average 2.0% above its new central rate against the euro in March 2000 and came closer to the central rate in April.

I should like to add that, throughout the reference period covered by this report, Greece recorded current account deficits which can be partly interpreted as a result of the country's need to finance investments.

To sum up the findings concerning the economic performance of Greece, the report identifies a number of positive developments, such as a significant reduction in HICP inflation and substantial progress towards improving the fiscal situation. However, continued efforts to support sustained price stability are of particular importance for Greece. This implies an ongoing need for tight fiscal policies and decisive structural reforms aimed at improving the functioning of product and labour markets. In this context a speedier transposition of Single Market legislation into national law, further progress on the liberalisation of a number of network industries and determined efforts to overcome structural rigidities in the labour market are warranted. Furthermore, increased efforts to reform the social security system are needed, while further progress on privatisation would reduce liabilities in the wider public sector.

II. Assessment of economic convergence in Sweden

Turning now to Sweden, I should like to start with a brief review of price developments. The country achieved an average rate of HICP inflation of 0.8% during the reference period, ie a level which is well below the reference value and consistent with price stability.

Recent trends and forecasts indicate, however, that there is increasing upward pressure on prices and costs. This has to be seen, inter alia, against the background of a period of high growth in Sweden in recent years, led predominantly by domestic demand. At the same time, the fiscal stance has become more neutral, resulting in a rapid closing of the output gap. As a result of these and other factors, forecasts indicate that inflation will be around 1.5% in 2000 and around 2% in 2001.

As concerns fiscal policies, Sweden achieved a fiscal surplus of 1.9% of GDP in 1999, thereby meeting the 3% reference value, and the outlook is for a surplus of 2.4% of GDP in 2000. The debt-to-GDP ratio stood at 65.5% in 1999, somewhat above the 60% reference value. With regard to the sustainability of its fiscal position, the outlook is for a further decline in the debt ratio to 61.3% in 2000 and Sweden is expected to comply with the medium-term objective of the Stability and Growth Pact of having a budgetary position that is close to balance or in surplus. Concerning the ageing of the population, Sweden benefits from a partly funded pension system, which is gradually being supplemented by a new system which will reduce pressures on public finances.

Not least because of the improvement in the country's public finances and the comparatively low rates of inflation, the level of long-term interest rates in Sweden was 5.4% on average during the reference period, ie well below the reference value for the interest rate criterion of 7.2%.

While Sweden has been successful in complying with the aforementioned convergence criteria, the country does not participate in ERM II. In this context it should be noted that Sweden is a Member State with a derogation and does not have a clause allowing it to opt out of Stage Three of EMU. Sweden is thus committed by the Treaty to adopting the euro, which implies that it has to strive to fulfil all the convergence criteria, including the exchange rate criterion.

Throughout 1999 and until April 2000 the development of the krona was characterised by a strong appreciation against the euro. This strengthening reflects a normalisation of the situation after the global crisis in autumn 1998 and Sweden's stronger than expected economic performance. In this context I should like to add that Sweden recorded current account surpluses, while maintaining a net external liability position.

III. Assessment of legal convergence in Greece and Sweden

With regard to the legal chapter of the Convergence Report, I should like to highlight the following points.

The report focuses on the compatibility of Greek and Swedish national legislation, including the statutes of the Bank of Greece and of Sveriges Riksbank, with the requirements for the full participation of Greece and Sweden in Monetary Union laid down in the Treaty and the Statute of the ESCB.

While acknowledging that issues related to central bank independence were already resolved in 1998 and do not, therefore, need to be addressed again, the ECB Convergence Report follows the same approach as that of the Convergence Report prepared in 1998 by the European Monetary Institute (EMI).

It addresses two issues:

- first, the legal requirements for the full legal integration of the Bank of Greece and Sveriges Riksbank into the Eurosystem; and
- second, the adaptation of legislation other than the statutes of these two national central banks.

With regard to Greece it concludes that:

- the Statute of the Bank of Greece has been adapted and, on the basic assumption that the new Statute will be ratified by Parliament and will enter into force on time and that obsolete provisions of a law dating back to 1997 (law 2548/1997) will be repealed, there will be no remaining imperfections in the Statute of the Bank of Greece relating to the requirements of the Treaty and the Statute of the ESCB for the full legal integration of the Bank of Greece into the Eurosystem.
- the ECB also takes note that other legislation will be adapted by means of a law introducing the euro.

With regard to Sweden, the conclusions of the EMI's 1998 Convergence Report remain unchanged. Swedish legislation, and in particular the Statute of Sveriges Riksbank, does not provide for the Bank's legal integration into the Eurosystem and is not, therefore, compatible with the Treaty and the Statute of the ESCB. As far as other legislation is concerned, the ECB notes that legislation on access to public documents and the law on secrecy need to be reviewed in the light of the confidentiality regime set out in Article 38 of the Statute of the ESCB.

I should now be happy to answer any questions you may have with regard to the ECB's convergence assessment of Greece and Sweden.