1. The Committee consulted with Greece on 22 April 1986, in accordance with its terms of reference, pursuant to Article XII:4(a) of the General Agreement and the Declaration of the CONTRACTING PARTIES on Trade Measures Taken for Balance-of-Payments Purposes (BISD 265/205). The consultation was held under the Chairmanship of Ambassador P.-L. Girard (Switzerland). The International Monetary Fund was invited to participate in the consultation in accordance with Article XV of the General Agreement.

2. The Committee had the following documents before it:

- Basic document by Greece and the Commission of the European Communities BOP/262 & Add.1
- Secretariat background paper BOP/W/99
- Notifications by Greece:
  - Reduction of import deposit (1983) L/5450
  - Abolition of import deposit L/5621
  - Reintroduction of import deposit L/5945/Rev.1
- Reply by the European Communities and member States to the Questionnaire on Import Licensing L/5640/Add.21/Rev.1

3. In his introductory statement, the representative of Greece stated that his Government had undertaken a considerable liberalization of its import régime pursuant to the Treaty of Accession of Greece to the European Communities, including the abolition on 1 January 1984 of import deposits maintained for balance-of-payments purposes. However, in October 1985, it had been obliged to reintroduce a prior import deposit scheme because of a rapid deterioration in the balance-of-payments deficit. The current account deficit had reached a record level of US$3.3 billion in 1985, a rise of 54.4 per cent compared with the previous year. Regarding the trade account, the decline in revenues from commodity exports and the increase in import payments were associated with a loss in competitiveness mainly due to a relative rise in unit labour costs in manufacturing and higher import penetration from the EEC countries. Over the same year, the invisibles account surplus had also declined by 8 per cent and foreign debt and net interest payments had accelerated. In the period 1980-1985 economic growth
had slowed and inflation increased. Public investment and consumption had become the determinant factors in demand and employment, and had increased the public sector deficit. The indexation of salaries and the rising cost of imports had boosted inflation. The structural weaknesses resulting from all these factors had combined with unfavourable external circumstances to accentuate the balance-of-payments deficit.

4. The prior import deposit scheme was the only trade measure adopted in a package of monetary and fiscal measures adopted by the Greek Government on 11 October 1985 including devaluation of the drachma, modification of the wage and price indexation system, reduction of the public sector deficit, and new taxation and credit provisions. It was a short-term measure aimed both at curbing balance-of-payments deficit and absorbing excess liquidity in the economy and would be maintained in anticipation of the results of other macro-economic policies. The lists of products covered were subject to change with a view to making the system more flexible, in the light of the evaluation of the economy and its production requirements.

5. The representative of the European Communities said that the import deposit scheme was an integral part of a wide-ranging economic stabilization programme adopted by Greece, and had been authorized by the Commission under Article 108 of the Treaty of Rome. The deposit scheme was less restrictive in its effects than other measures which could have been justifiable under GATT balance-of-payments provisions. The scheme was non-discriminatory and its major impact had been on the other member States due to the structure of Greece's trade links. The Commission was following carefully the development of the economic situation in Greece and held regular quarterly reviews with the Greek authorities with a view to the progressive dismantling of the scheme. Such reviews had so far taken place in January and April 1986.

6. The macro-economic adjustment programme undertaken by the Greek authorities comprised fiscal, monetary, price and income policy measures. The aim of this programme, which would stretch over a number of years, was to reduce domestic disequilibrium, improve the competitiveness of the Greek economy, and eliminate all net public-sector external borrowing by 1988. The public sector borrowing requirement was expected to fall from a level of 18 per cent of GDP in 1985 to a projected 13 per cent in 1986 and 9 per cent in 1987. Strict limits had been placed on pay increases in the private and public sectors, at levels considerably lower than existing inflation; this was expected to reduce real incomes of wage and salary earners by some 7 per cent in the current year. Monetary policy measures had reduced the growth of the broadly-defined money supply from an annual 32.6 per cent in May 1985 to 26 per cent in December, and further reductions were expected. The Community had granted Greece a conditional medium-term loan of 1.75 billion ECU, disbursed in two equal tranches. The first disbursement was made in January 1986 and the second was expected to be made in January 1987.

7. The import deposit scheme was to be regarded as a short-term measure aimed at having an immediate effect on import flows. While principally a trade measure, it had contributed to the efficacy of the above-mentioned monetary policy measures.
Statement by the representative of the International Monetary Fund

8. At the invitation of the Committee, the representative of the International Monetary Fund made a statement, the text of which is reproduced in the Annex.

Balance-of-payments position and prospects: alternative measures to restore equilibrium

9. One member welcomed the fact that Greece had actively addressed in its adjustment programme such questions as exchange rate policy, the reduction of the public sector deficit and the diminution of excess liquidity. He encouraged greater efforts by the Greek authorities to pursue internal economic reforms. He asked what further plans would be implemented by Greece to improve its economic growth rate and external competitive position, and in this context asked the representative of Greece to explain the current exchange rate policy.

10. In reply, the representative of Greece distinguished two stages in Greece's economic programme: a short-term stabilization plan and a longer-term economic reconstruction programme. The latter would be directed to questions of employment, the improvement of the functioning of public enterprises, and the promotion of private and public investment. In this, Greece would also benefit from assistance from Community sources, including the Integrated Mediterranean Programmes. These policies were to be seen in the context of Greece's overall long-term development strategy as currently formulated.

11. The Community representative stated that current Greek exchange rate policy was intended to ensure that the competitive position in terms of unit labour costs, established through the October 1985 devaluation of the drachma, was maintained.

12. Another member, recognizing the difficult economic situation in Greece and the deterioration of the current account, expressed the hope that the economic improvement resulting from domestic adjustment policies would soon make it possible progressively to reduce, and eliminate, the import deposit scheme.

System, methods and effects of the restrictions

13. Two members of the Committee asked whether the import deposit was the only measure currently taken by Greece for balance-of-payments reasons, or whether other trade measures, such as import licensing or quantitative restrictions, were also maintained for such purposes. The representatives of Greece and the Community confirmed that the import deposit was the only measure currently maintained in Greece for balance-of-payments reasons.

14. One member asked for an estimate of the trade effects of the import deposit scheme. He also asked whether there was a firm timetable for the elimination of the deposit requirement, and in particular whether it could be expected to be phased out during the present year in view of the expected rapid improvement in the current account situation. In reply, the representative of the Community reiterated that, since its introduction in
October 1985, the scheme had been subject to review every three months by the Commission. A first modification and reduction in the coverage of the scheme had resulted from a review in January 1986; further modifications might come from a review currently underway. It was therefore difficult to give a clear picture of the trade effects at this time. Although there was no timetable established for the phase-out of the import deposit scheme, the quarterly review process was intended to ensure that progressive reductions would take place. All modifications to the import deposit scheme and any other information which might emerge from the quarterly review, would be duly notified to the GATT. The Community representative also confirmed that the phase-out of the import deposit scheme would be done on a non-discriminatory basis.

15. In response to a question on the initial effects of the fiscal, monetary and trade measures included in the Greek adjustment programme, the Community representative stated that, while there had been no apparent improvement in the current account balance in December 1985, the monthly deficit in January 1986 stood at $218 million as against $413 million in January 1985. While it was difficult to make a firm statement on the basis of one month's figures some improvement appeared to be taking place. One member, referring to the Greek Government's aim to reduce the current account deficit by half in 1986, suggested that this might provide an occasion for a substantial reduction of the import deposit scheme. Another member urged the Greek authorities, in the light of this expected improvement, to phase out the import deposit scheme as quickly as possible. The representative of the European Communities noted that the quarterly review process could permit a progressive liberalization of the scheme in the light of the evolution of the economic situation.

Conclusions

16. The Committee observed that there had been a serious deterioration in the Greek economy in 1984 and 1985, with growing external and internal imbalances and increasing inflation. A large part of this deterioration could be ascribed to domestic disequilibria, particularly to a growing public-sector deficit; however, Greece's competitive position in external markets had also worsened, as a result of increasing unit costs of labour and also of the exchange rate policies pursued in preceding years.

17. The Committee noted that the adjustment programme introduced by Greece in October 1985 was principally addressed to redressing internal economic imbalances, restoring price stability and improving Greece's international competitiveness through a variety of fiscal, monetary, price, income and exchange rate policy measures.

18. The Committee regretted that the Greek authorities had considered it necessary to reintroduce an import deposit scheme in addition to the domestic adjustment measures aimed at achieving an improvement in the current account of the balance of payments and the desired tightening of liquidity. It noted with satisfaction, however, that the import deposit scheme was non-discriminatory in nature, and welcomed the assurances by Greece and the European Communities that the deposit was a temporary measure intended to have a rapid effect in anticipation of the effects of other adjustment policies. The Committee also noted that certain modifications had already
been made to the import deposit scheme, and welcomed the readiness expressed by the Community and Greek authorities to notify these and any subsequent modifications and any other relevant information.

19. The Committee noted that a marked improvement in the current account was foreseen by the Greek authorities for 1986 and that the programme established by Greece envisaged the elimination of all net public-sector foreign borrowing by 1988. Bearing in mind all the above factors, the Committee expected Greece to phase out the temporary import deposits as soon as possible on a non-discriminatory basis, and invited the Greek and Community authorities to establish a timetable for this purpose, pursuant to paragraph 1(c) of the Declaration on Trade Measures Taken for Balance-of-Payments Purposes.
Greece's economic performance in the first half of the 1980s was characterized by slow growth of output (about 1 percent a year on average), and relatively rapid inflation (20 percent on average). Moreover, substantial deficits were recorded in the current account of the balance of payments (around 6 1/2 percent of GNP), so that external debt more than doubled to the equivalent of 47 percent of GNP by 1985. Unfavorable external developments, including a sizable cumulative loss in the terms of trade, as well as structural weaknesses and rigidities in the economy and accommodating financial policies, contributed to these developments. In addition, exchange rate policy has led to substantial swings in competitiveness in recent years. The beneficial effects of a 15.5 percent devaluation in January 1983 were eroded rather quickly by the subsequent decision to peg the drachma to the appreciating U.S. dollar. For a time from mid-1983, the authorities sought to stabilize—and at times to depreciate moderately—the real exchange rate of the drachma measured by relative consumer prices. However, the economy continued to suffer further losses of competitiveness as unit labor costs increased significantly faster than consumer prices. By September 1985, the real effective exchange rate of the drachma (measured by relative consumer prices) had returned to its post-devaluation level of January 1983, but its value in terms of relative unit labor costs was over 17 percent higher.
The initial policy stance for 1985 involved a moderate tightening of fiscal and monetary policies; the public sector borrowing requirement (PSBR) was targeted to decline by the equivalent of 2 percentage points of GNP (to $12\frac{1}{2}$ percent of GNP), and the rates of growth of broad money and domestic credit were programmed to decelerate significantly. In the event, shortfalls in tax receipts and overruns in various expenditure items led to a marked widening of the PSBR and to an acceleration in the monetary aggregates, especially in the first half of the year. Although the authorities adopted corrective measures in the last quarter of 1985, for the year as a whole the PSBR reached the equivalent of 18 percent of GNP (on a cash basis), and domestic bank credit rose by nearly 25 percent ($5$ percentage points in excess of the target).

The slippages in financial policy hindered the achievement of greater price stability and contributed to a marked deterioration in the external accounts, adversely affecting exchange rate expectations. Consumer prices rose by over 19 percent on average in 1985. The 12-month inflation rate reached 25 percent in December 1985 and January 1986, in the wake of a 15 percent devaluation of the drachma in October and substantial increases in administered prices in the final months of the year. The current account deficit in the balance of payments widened from US$2.1 billion ($6\frac{1}{2}$ percent of GNP) in 1984 to US$3.3 billion (over 10 percent of GNP) in 1985, owing to lower net invisible receipts and a sharply wider deficit on merchandise trade. The growth of imports accelerated in volume terms, while that of exports declined, and the terms of trade worsened significantly. It is likely that the adverse exchange rate expectations played a role in the deterioration of the
current account through their reflection in anticipatory purchases of imported goods, overinvoicing of imports and underinvoicing of exports, and lower growth of some invisibles receipts. Autonomous capital inflows were also negatively affected by perceptions of exchange risk. As a result, compensatory net foreign borrowing by the public sector increased sharply to US$2.3 billion in 1985.

In these circumstances, in October 1985 the authorities announced a series of measures aimed at reducing domestic inflationary pressures and stabilizing the external debt by 1988. This adjustment program has been supported by the European Community through an ECU 1.75 billion loan. For 1986, the Government aims to reduce the rate of consumer price inflation to 16 percent by year-end and to halve the current account deficit to US$1.7 billion (4.8 percent of GNP). The measures introduced in support of these objectives include a 15 percent depreciation of the drachma; the imposition of an import deposit scheme; sizable increases in some administered prices; a strict incomes policy; increases in some bank lending rates; and a budget that aims to reduce the PSBR in 1986 by 4 percentage points of GNP, followed by a similar reduction in 1987.

The incomes policy measures announced in October 1985 involve a major change in the system of wage indexation, which is causing a marked decline in the growth of nominal wages and a substantial reduction in real terms. As from January 1, 1986, wages and salaries are to be set every four months with reference to an official target for the inflation rate for the following four-month period, adjusted to exclude the effects of increases in import prices. The wage and salary increases so determined are to be the legal maxima in both the public and private
sectors in 1986 and 1987, except that some salary restructuring in the public sector, agreed before last October, will be allowed. Wage increases exceeding the new limits will be treated as illegal and subject to fines and exceptional taxation.

The planned reduction in the PSBR is to be achieved despite rapidly rising interest payments on public sector debt. Noninterest expenditures of the budget are targeted to rise by 17\(\frac{1}{2}\) percent, compared with an expected increase in nominal GDP of 20 percent in 1986. Incomes policy is expected to play a significant role in containing the growth of expenditures. Revenues are projected to increase by 33\(\frac{1}{2}\) percent, reflecting a renewed drive (supported by new legal sanctions) to collect outstanding back taxes and reduce tax evasion, as well as the effects of fiscal drag (income tax brackets have been frozen and tax allowances raised only modestly). The Government also expects to significantly reduce the deficits of the public enterprises.

As part of this package of measures, the Bank of Greece announced the introduction of a minimum lending rate (currently set at 16 percent) to apply to short-term loans. Prevailing interest rates are mostly below the current rate of inflation; they will turn positive during the year if the Government's inflation target is realized. In October 1985, the Bank of Greece also took steps to absorb the excess liquidity that had accumulated in the banking system earlier in the year. In the last few months of 1985, the growth rates of the money and credit aggregates declined noticeably. The monetary program for 1986 foresees a slowdown in the growth of broad money from 26 percent in 1985 to 20 percent in the 12 months to December 1986.
The exchange and trade system was liberalized between 1979 and October 1985, partly in connection with Greece's entry into the EC. Some temporary import barriers raised in 1979 were eliminated by end-1980. By January 1984, all bilateral payments agreements were terminated, the requirement of prior approval by banks for imports was lifted, the restrictions on import financing were removed, and an import deposit scheme was eliminated. Quantitative import restrictions on five commodities, accounting for around 1 percent of total imports, were removed on December 31, 1985.

The reintroduction of an import deposit scheme as part of the October 1985 series of measures partly reversed the liberalization achieved in recent years. The scheme requires private sector importers to maintain noninterest-bearing deposits in drachmas with the Bank of Greece for six months. The deposit rates are 40 percent or 80 percent of the c.i.f. value (excluding import duties) of specified imports. Essential imports, including oil, other raw materials, and most food products, are exempt from the scheme. The deposit requirements would have applied to approximately US$2 billion of imports in 1984, corresponding to just over 20 percent of the total. In the first four months of the scheme's operation, Dr 38 billion, equivalent to US$260 million, were placed in import deposits. The import deposit scheme appears to involve a concurrent exchange restriction and a multiple currency practice under Article VIII, Sections 2(a) and 3, of the Fund's Articles of Agreement. No approval has been granted.

The October package of measures represents a significant step in the difficult process of tackling the severe economic problems facing
the Greek economy. The Fund welcomes the authorities' efforts to secure a marked and sustained reduction in both the rate of inflation and the deficit in the balance of payments through a strict incomes policy, a strong improvement in the public sector finances, and a deceleration in the growth of monetary and credit aggregates. However, it regrets that the authorities have found it necessary to introduce an import deposit scheme for a large number of imported products, thereby reversing the trend toward liberalization of the trade and payments system. The Fund would have preferred the use of different instruments to achieve the desired tightening of liquidity and improvement in the current account of the balance of payments. The Fund hopes that the Greek authorities will stand ready to take additional measures, should developments in the course of 1986 indicate a shortfall in their financial policy objectives, and urges the termination of the import deposit scheme as soon as possible.