

INTERNATIONAL MONETARY FUND

December 23, 1947

To: Members of the Executive Board
From: The Secretary
Subject: Recent Economic Developments in Greece

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INTERNATIONAL MONETARY FUND

Research Department

Recent Economic Developments in Greece

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The purpose of this paper is to cover economic and financial developments in Greece since February, 1946, and to supplement and bring up to date R.D. Memorandum 221, of April 1, 1947, Economic Conditions in Greece. The information at present available is still too fragmentary to permit a complete or accurate picture of the situation.

Summary and Conclusions

In February, 1946, a new attempt was made to stabilize the drachma. The program included two main measures: (a) free sale to the public of sovereigns by the Bank of Greece at a fixed rate, and (b) more liberal allocation of foreign exchange to private individuals for import purposes.

The inflationary pressure created by the extension of credits by the Bank to the Government, agriculture, industry, and trade was thus relaxed, though at the cost of the dissipation of a large part of the gold and foreign exchange holdings of the Bank of Greece. The sale of sovereigns absorbed part of the surplus purchasing power, and for the first time since liberation there was a considerable volume of imports other than those for which UNRRA was responsible; this helped to keep internal prices, on the whole, steady, although the internal price level was still out of line with the world level.

Premiums paid for foreign currencies on the black market remained high; receipts in foreign exchange (such as emigrants' remittances and shipping receipts) were therefore diverted, to a considerable extent, to illegal channels. Moreover, export trade was hampered by high internal prices, and current foreign exchange receipts were still quite inadequate to meet even the most urgent import requirements of the country.

The comparatively stable monetary conditions provided the basis for a marked improvement in public finance. The largest part of governmental receipts still, however, consisted of extraordinary revenue such as receipts from sales of UNRRA supplies; though there was some improvement in tax yields, there were still certain sectors in the economy upon which the burden of taxation fell very lightly.

Agricultural production was more satisfactory in 1946 than in 1944 and 1945. Food conditions, however, were not improved to the extent that might have been expected, because the Government failed to collect from producers a sufficient part of the cereal crop to be utilized for bread rationing. In 1947 cereal crops

are expected to be about 40 per cent less than in 1946, but the output of olive-oil, vegetables, and fruit will be larger. Industrial production, especially in the industries essential for reconstruction or the satisfaction of basic consumers' needs, has continued to lag far behind the prewar levels. In physical reconstruction of railroads, roads, and ports, almost nothing has been done.

Under such conditions, distrust of the drachma continues; voluntary savings remain at an insufficient level; and the need for foreign exchange and gold not only for imports but also to counteract the inflationary pressure and to prevent large fluctuations in prices does not diminish. The monetary stability of 1946-47 has been based on three factors: sales of gold to the public, extraordinary receipts from the sale of UNRRA goods, and increased imports paid for by drawing on foreign exchange resources which are now exhausted. The influence of each of these factors is necessarily temporary, and with the withdrawal of these supports the stability of the currency is again endangered.

Meanwhile, Greece is in need of outside aid, not only for reconstruction and production purposes, but also for current food requirements. As long as the civil war continues and political stability is not restored, no substantial improvement in economic conditions can be expected.

Economic reconstruction is at a complete standstill partly on account of the unsettled political situation and the resulting civil strife, and partly because so far no workable plan of recovery and stabilization has been applied. The rehabilitation of the economy is impossible without administrative, financial, and fiscal reforms carried out by an Administration with broad political support by the population.

1. Agricultural Production

Agricultural production improved substantially in 1946, largely because of good weather conditions, UNRRA supplies of seeds, fertilizers, and agricultural machinery, the hard work of the Greek peasants, and some credit facilities granted them through the Agricultural Bank of Greece. With the assistance of UNRRA food supplies, and government and private imports, the food situation on the whole was better than in the early post-liberation period, although some deterioration was evident in the late months of the year.

It is reported that the cultivated area averaged approximately 80 per cent of the prewar level and that output was about 70-80 per cent of that in prewar years. The gap between wheat production and the country's requirements, however, was even greater than before the war, when average annual consumption exceeded 1,300,000 metric tons, which meant that substantial imports were always necessary. Production in 1938 and 1946 is indicated by the following estimates for the principal crops, which--especially for wheat--may be somewhat exaggerated:

| | <u>1938</u> | <u>1946</u> |
|------------------------------|-------------------------------|-------------|
| | (in thousands of metric tons) | |
| 1. Wheat | 980.3 | 700.0 |
| 2. Rye, barley, oats, meslin | 463.6 | 330.0 |
| 3. Maize | 217.4 | 190.0 |
| 4. Rice | 9. | 4. |
| 5. Pulses | 78.9 | 50.1 |
| 6. Cotton | 45.3 | 31.6 |
| 7. Tobacco | 48.1 | 32. |
| 8. Currants | 150.1 | 57. |
| 9. Raisins | 37.3 | 18-20 |
| 10. Olive-oil | 102.8 | 90. |

Although in 1947 the cultivated area is reported to have reached 81 per cent of the prewar level for wheat and 88 per cent for other cereals, unfavorable weather conditions and the civil war have exerted a disastrous influence on cereal production. The 1947 cereal crop will probably be about 40 per cent less than that of 1946.

Production of other crops, such as cotton, tobacco, currants, and raisins, is expected to be near the 1946 level, while the output of olive-oil, vegetables, and fruit may show considerable improvement.

In the absence of adequate supplies of other foodstuffs, bread is the basic food for most of the people of Greece. Since the middle of 1946, however, when UNRRA imports began to decline, the bread ration has been reduced in quantity and has deteriorated in quality. As a result of inadequate organization, the government did not succeed in collecting sufficient quantities of wheat from the 1946 crop to maintain the bread ration at the level established when UNRRA was supplying a large quantity of this grain.

UNRRA imports of cereals and foodstuffs decreased quite sharply in the third quarter of the year; later, the exhaustion of the U.S. dollar holdings of the Bank of Greece made it necessary to restrict the import of food by both the government and private importers. As a result and in the absence of government stocks, nominal rations were reduced from month to month, and there was increasing difficulty in supplying them. In recent months, food rations in the metropolitan area, which in this respect is the most favored, corresponded to an average of only about 800 calories per day, including 256 grams of bread, equivalent to 664 calories.

The civil war, which since the middle of 1946 has extended over a wide area, in certain provinces renders the farmers' job difficult if not impossible. The expansion of production has also been hampered by the absence of adequate incentives for the farmers. Throughout the period there has been a wide disparity between the internal and world price levels. The successive rates fixed for the foreign exchange value of the drachma have always been based on a view, which subsequent events failed to justify, of the speed at which increased production would improve the supply situation, and the speed of the revival of confidence in the currency would destroy the basis for speculative transactions. Since the disparity between internal and world prices has made the export of tobacco, currants, and raisins unprofitable, the output of these crops remains far below

the prewar level. The wide margin between high industrial prices and the much lower prices received by agricultural producers, even though it has narrowed since the third quarter of 1946, is a further discouragement to farming activity.

At present, free market prices are well above the regulated prices of rationed goods. During the most recent period some basic foodstuffs such as sugar, cheese, etc. have, from time to time, entirely disappeared from the market, partly because of the concealment of food by producers and traders in the expectation of more stringent shortages and larger profits.

Without sufficient imports of foodstuffs in the immediate future, the food situation will deteriorate even more.

2. Industrial Production

Currency instability, political disturbances, and other factors have prevented the full use of the available industrial capacity. Some Greek manufacturers have preferred to hoard gold sovereigns and raw materials instead of using their funds for the renewal of factory equipment and for more intensive production.

Industrial raw materials imported by UNRRA could probably have provided a basis for increased industrial production had production and the marketing of industrial products been supervised by the Government. Considerable quantities of raw materials, especially cotton, were sold to various industries at prices well below the internal market level, but the Government imposed no controls on the subsequent processes of manufacture. Industrialists were thus able to neglect the requirements of the low income groups, and instead converted much of these raw materials into products which they could sell at abnormally high prices.

By the middle of 1946, therefore, while production of expensive consumer goods and luxury items showed an improvement, the output of other industries of vital importance for reconstruction (such as metal working and cement industries) or of industries supplying the needs of low income groups remained far below the prewar level. The rehabilitation of the bauxite and other mining industries whose output might have been exported was scarcely even begun.

Reliable data concerning industrial development are not available. The imperfect index of industrial production shown below was compiled by the Research Department of the Bank of Greece on the basis of information furnished by the Federation of Greek Industries:

| <u>Index of Industrial Production in Greece</u> * | | | |
|---|--------------|-------------|------|
| <u>1946</u> | (1939 = 100) | <u>1947</u> | |
| January | 38.3 | January | 62.2 |
| February | 42.9 | February | 59.3 |
| March | 43.5 | March | 59.7 |
| April | 48.1 | April | 66.4 |
| May | 52.6 | May | 68.7 |
| June | 55.0 | June | ... |
| July | 57.3 | July | 67.2 |
| August | 57.6 | | |
| September | 59.3 | | |
| October | 62.5 | | |
| November | 66.7 | | |
| December | 61.1 | | |
| Average 1946 | 53.7 | | |

* In the construction of the total index, each industry included has been weighted according to the value of its output in 1939.

No reliable data concerning the movement of wages and salaries are available. In February, 1946, wages and salaries were raised in exactly the same proportion as official foreign exchange rates, i.e., to 10 times the wage level established in June, 1945, when wages had been fixed at approximately 5 times the prewar level. Additional increases were granted to some categories of workers and employees. The salary level of civil servants - the largest category of employees - is not likely to exceed 75-80 times the prewar level; this would mean since the cost of living has increased to more than 150 times the prewar level, that in real terms their salaries now correspond to about 50 per cent of the inadequate prewar level.

3. Financial Developments

Attempts to Stabilize the Drachma:

The unprecedented monetary inflation and shortage of goods during the enemy occupation of the country (May, 1941-October, 1944) led to a general flight from the currency, and gold became almost the exclusive basis of all calculations. The price of the gold sovereign became the most important indicator for price movements in general, fluctuations in the circulation of bank notes and in the price level reacting continuously upon each other, and producing conditions of abnormal instability. Large numbers of gold sovereigns passed into the hands of private investors, as assistance was given in this form to the resistance movement by the Allied Governments or sales were made to the public by the German authorities.

Throughout the whole post-liberation period up to January, 1946, with the exception of two months, June and July, 1945, economic and monetary conditions were characterized by almost the same instability as during the occupation. Internal political disturbances, shortages of goods and inflationary pressure intensified by budgetary deficits, advances to British troops and expansion of credit for agriculture, trade, and industry, prevented the restoration of confidence in the drachma. There was a strong tendency to convert cash balances into sovereigns, and movements in their price had the same relationship with the price level as during the occupation.

In November, 1944, the currency then existing was virtually cancelled, and a new currency was issued, with its value fixed at 150 drachmae to 1 U.S. dollar. Prices, however, again rose rapidly, and in June, 1945, the drachma was revalued, at the rate of 500 to 1 U.S. dollar. In February, 1946, following the Greek-British economic agreement of January 24, 1946, another attempt was made to establish monetary stability by making the drachma convertible into gold or foreign currencies for import purposes. A new exchange rate was established, 5,000 drachmae per 1 U.S. Dollar and 20,000 drachmae per 1 £ sterling, and gold sovereigns were sold freely to the public at a fixed price of about 135,000 drachmae. At the same time, heavy allocations of foreign exchange for imports were made from the foreign exchange and gold holdings of the Bank of Greece.

Both measures were designed to absorb some of the surplus purchasing power in the hands of private individuals and thus to counteract inflationary pressures. Furthermore, it was expected that governmental and private imports, in addition to those of UNRRA, would diminish or eliminate the existing shortage of commodities; it was hoped that domestic prices would thus be stabilized near the

world price level which at that time was far below the level of free market prices in Greece.^{1/}

These measures continued in operation until the end of November, 1946, when foreign exchange assets - especially U.S. Dollars - were almost entirely exhausted, and the Government was compelled to restrict import licenses. The free sale of sovereigns was still continued.

The following figures show the factors affecting the note circulation before and after the measures of February, 1946:

| | <u>January 31, 1946</u> | <u>June 30, 1947</u> |
|--|-------------------------|----------------------|
| | (billions of drachmae) | |
| <u>Sources of increase</u> | | |
| Advances to the State, less receipts effected by the Bank on State account | 98.8 | 678.8 |
| Loans, advances and other credits to agriculture, industry, trade | 37.6 | 860.9 |
| Net purchases of foreign exchange including advances to British troops | 33.9 | --- |
| Various accounts | <u>---</u> | <u>39.7</u> |
| | <u>170.3</u> | <u>1,579.4</u> |
| <u>Sources of decrease</u> | | |
| Deposits and current accounts of the State | 12.3 | 82.4 |
| Other deposits and current accounts | 25 | 148.7 |
| Net proceeds of sale of gold | 0.1 | 323.4 |
| Net proceeds of sale of foreign exchange | --- | 334.5 ^{2/} |
| Various accounts | <u>1.5</u> | <u>---</u> |
| | <u>38.9</u> | <u>889.</u> |
| Note circulation | <u>131.4</u> | <u>690.4</u> |

^{1/} In the postwar period world prices have not increased by more than 100 per cent; in Greece, the official dollar exchange rate was fixed in February, 1946, at a level about 40 times higher than prewar. This would correspond to a domestic price level approximately 80 times as high as the prewar level. Free market prices in Greece have in fact increased approximately 200 times compared with 1939 level.

^{2/} Purchases of £ sterling by the Bank of Greece for advances to the British Forces are not shown separately but together with other foreign exchange transactions. These purchases are placed in a special account, and cannot be used, pending a settlement between the two governments. Of a total of about £ 18.9 million, corresponding to advances of about 154 billion drachmae up to June 30, 1947, only £ 5,000,000 were freed and transferred to the monetary reserve account of the Bank of Greece in February, 1947.

These figures indicate that until January, 1946, apart from budgetary deficits and credits granted to the various sectors of the economy, the proceeds from net purchases of foreign remittances by the Bank of Greece also exerted inflationary pressure. After January, 1946, net purchases were replaced by net sales of foreign exchange, and this together with the sale of gold sovereigns had a deflationary effect on the monetary circulation. In all, the volume of purchasing power withdrawn by this policy amounted to about 778 billion drachmae,^{1/} a figure which indicates the extent to which the inflationary pressure was checked.

Despite the almost continuous increase in the volume of bank notes generated by further credit expansion throughout this period, the new deflationary policy achieved a considerable degree of monetary stability and the additional imports caused a sharp fall in the prices of some commodities, e.g., leather, coffee, and sugar.

The upward trend in the price level has, however, now been resumed; the decrease in the prices of imported goods was more than offset by the increase in the prices of domestic food and other agricultural products, particularly because there was a serious reduction of UNRRA food imports which home production was unable to replace. Later on, the exhaustion of foreign exchange holdings and restrictions on imports also led to a rise in the prices of imported goods. (See Table A, showing movements in the cost of living index, in free market prices in Athens, in the gold sovereign rate, and in the circulation of bank notes.)

Permanent monetary stability, however, was not assured. The stabilization efforts had some effect in decreasing the velocity of circulation. The willingness of the public to hold drachma cash balances was slightly increased by the knowledge that drachmae could be easily converted at fixed rates into gold sovereigns or foreign exchange for import purposes. But confidence in the currency was far from being fully restored, and savings deposits in banks and other institutions were still considerably below the level of bank notes in circulation.

Evidence of the present abnormal monetary situation in Greece is the high ratio of credits granted by the Bank of Greece to the Government, agriculture, industry and trade, to the total amount of bank notes in circulation. Although Government overdrafts upon the Bank of Greece have, as a rule, been smaller since the middle of 1946, there still persists a budgetary deficit. According to the accounts of the Bank of Greece, the Government overdrafts totalled 580 billion drachmae during the period February, 1946 - June, 1947. The expansion of credits, granted mainly to agriculture, during the same period amounted to another 823.3 billion. The greater part of the new issues which resulted from the total amount of credits (1,403.3 billion) has been absorbed through the net sales of foreign exchange (approximately 522.4 billion) and the sales of gold sovereigns (nearly 323.3 billion); the remainder, excluding deposits with the Bank of Greece, caused an increase of bank notes in circulation from 131.4 billion on January 31, 1946, to 690.4 billion drachmae on June 30, 1947. The net effect of these developments is an increase of credits outstanding with the Bank of Greece to more than twice the amount of the note circulation.

During 1946, sales of gold sovereigns by the Bank of Greece to the public averaged 200,000 sovereigns per month. It is estimated that in all 5 - 5.5 million gold sovereigns (equal to 675 - 742 billion drachmae at the rate of 135,000 drachmae per sovereign, or \$140 million at the rate of 5,000 drachmae per dollar) have, during the enemy occupation and the post-liberation period,

^{1/} 323.3 billion from gold plus 334.5 from foreign exchange plus 154 from sterling advances minus 33.9 from foreign exchange purchases before January 31, 1946.

passed into private hands. Some sovereigns, perhaps 10 - 15 per cent of the total amount, are being used as a medium of exchange for current transactions. The remainder is hoarded, either in the form of individual savings or as business reserves of which for the time being no use is being made.

It might have been expected that the rapid decline in the Bank of Greece's holdings of foreign exchange, and especially of U.S. dollars, and the reduction of imports, since the early months of 1947, would have increased the demand for gold by the public and completely exhausted the remaining official gold holdings within a few months. Actually, sales of gold sovereigns declined to about 6,000 in March, 1947, and then rose in April to about 7,000, in May to about 47,000 and in June to about 100,000. On June 30, 1947, the assets in gold of the Bank of Greece totalled some \$15,000,000, of which \$10,800,000 were kept as collateral against a loan granted to Greece by the Federal Reserve Bank of New York, and part consisted of gold coins other than British gold sovereigns.

The maintenance of a relatively stable monetary situation since the spring of 1947 has been partly the result of the favorable psychological atmosphere created by the announcement of the "Truman Doctrine." No data on the sales of gold sovereigns since July are available, but recent reports of movements in the price of sovereigns suggest that the gold sovereign assets of the Bank of Greece have by now been exhausted. The gold sovereign rate was reported early in August to have risen from about 135,000 drachmae to a record price of 170,000 drachmae. It dropped subsequently, and on August 13 was reported at 150,000. Some imported goods such as coffee, sugar, rice, and flour are difficult to obtain as merchants are hoarding their most negotiable goods and trying to exchange others for gold sovereigns. It is also reported that internal prices are rising.

If the gold sovereign rate could not be kept relatively steady, a new collapse of the Greek economy will follow. A considerable rise in the gold sovereign rate will be reflected in a further general upward movement of prices. For various reasons, the Government is not in a position directly to influence internal prices. Domestic production is quite insufficient to cover consumption needs, and the efficient collection and distribution of domestic food presents the most formidable difficulties. There has been no serious attempt to control the selling prices of imports, and in the early months of 1947, the imports which were still available were often either hoarded by their owners or sold only for gold sovereigns at higher prices. The Civil War and the international political situation also inevitably aggravate the Greek economic problem. It is still too early to judge how far the United States Mission in Greece will succeed in helping the Government give to the people of Greece financial stability, economic recovery and the political peace on which the first two objectives so much depend.

Commercial Banks and Credit Expansion

Under present economic and monetary conditions the Greek commercial banks^{1/} face very serious difficulties. The greatly reduced economic activity of the country, the elimination of prewar deposits by the monetary inflation, and the general lack of confidence in the currency make it almost impossible for the

^{1/} In addition to the Bank of Greece (the Central Bank) and the Agricultural Bank of Greece (a government institution granting credits to farmers), there are 15-17 commercial banks. The largest, the National Bank of Greece, carries out 50-60 of all banking transactions; and four other banks carry out 35-45 per cent. The remaining 10-12 smaller local banks are established mostly in the provinces.

banks to earn sufficient to cover their expenses.

Current account and savings deposits are at such a low level that the banks' resources are insufficient to provide credits for the various branches of the economy. Before the war deposits in commercial banks and other savings institutions amounted to twice or three times the note circulation. In spite of some improvement in recent months, deposits on June 30, 1947, still amounted to only about 35 per cent of the note circulation. Moreover, nearly one-half of these deposits are compulsory deposits of public institutions.

At present, therefore, expansion of credit is possible only by the issue of currency provided by the Bank of Greece. Credits granted by other banks from their own resources are estimated to be not more than 10 to 12 per cent of total credits.

The volume of credit, as well as its distribution among the various sectors of the economy, is regulated by the Currency Committee established under the Greek-British Economic Agreement of January 24, 1946, which however has little effective control over the credit granted from their own resources by the commercial banks.

The amount of loans and credits outstanding on June 30, 1947, financed by the Bank of Greece, are shown in the following table:

| | (In millions of drachmae) | Percentage |
|---------------------------------|---------------------------|-------------|
| <u>Credits to:</u> | | |
| Industry | 42,389.3 | 4.9 |
| Agriculture | 581,220.1 | 67.5 |
| Tobacco trade | 147,726.5 | 17.2 |
| Import, export & internal trade | 26,142.6 | 3. |
| Banks (for payroll purposes) | 39,980.5 | 4.7 |
| Miscellaneous | <u>23,398.8</u> | <u>2.7</u> |
| | <u>860,857.8</u> | <u>100.</u> |

Of the total amount, 151,901.8 million drachmae were granted directly by the Bank of Greece, 553,622.1 million drachmae through the Agricultural Bank of Greece, and the remainder 155,333.9 million drachmae through the commercial banks.

On August 21, 1946, the official discount rate of the Bank of Greece and the legal maximum rate of interest were both fixed at 10 per cent per annum, including commissions but excluding other expenses. The Bank of Greece charges interest at 3 to $3\frac{1}{2}$ per cent on approved loans granted to other banks for re-lending purposes. The interest rates paid by the banks on deposits vary from $1\frac{1}{2}$ to 3 per cent.

The net rate of interest gained by the commercial banks therefore amounts to $6\frac{1}{2}$ to 7 per cent for credits granted with funds of the Bank of Greece and 7 to $8\frac{1}{2}$ per cent for those granted from their own sources. However, in view of the relatively small activity in the field of financing and of the fact that the

volume of miscellaneous banking transactions, which in normal times were a significant source of bank commissions, is in present circumstances greatly reduced, the profits of the commercial banks are not, as a rule, sufficient to cover their expenses, consisting mainly of payroll payments.

4. Government Finance

In the fiscal year 1946-47 (April 1, 1946 to March 31, 1947) there was some improvement in public finance, compared with previous post-liberation periods. The improvement is attributable to the comparatively stable monetary conditions of 1946-47, and to the extraordinary revenue from the sales of UNRRA supplies. The movement of receipts and payments in the Government accounts with the Bank of Greece is shown below:

| | 11/11/44 to 3/31/45 | 4/1/45 to 3/31/46 | 4/1/46 to 3/31/47 |
|--------------------------------------|---------------------------|----------------------|----------------------|
| | (in billions of drachmae) | | |
| Payments by the Bank to the State | 11.5 | 477.2 | 2,051.7 |
| Receipts on account of the State | <u>1.9</u> | <u>188.2</u> | <u>1,680.3</u> |
| Overdraft at Bank of Greece | 9.6 | 289.0 | 371.4 |

While in 1944/45, 83.5 per cent of Government expenditure was covered by overdraft with the Bank of Greece, in 1945/46 this percentage dropped to 60.6 per cent and in 1946/47 to 18.1 per cent. The monthly movement of the State account with the Bank of Greece during the period February, 1946 - May, 1947, gives further indication of the improvement of the budgetary situation. (See Table B).

Until May, 1946, deficit spending by the Government contributed substantially to the increase of inflationary pressure. Since June, 1946, Government overdrafts have been, as a rule, smaller, and for the first time since liberation there has been in some months a surplus of receipts over expenditure.

The Government account with the Bank of Greece shows only global items and does not indicate the sources of receipts or the nature of payments. Moreover, some items passing through the Government account do not represent real government receipts or expenditures, e.g., in connection with loan operations. "Accountancy entries" have also been included on both sides of the account. This explains the discrepancies between the receipts and payments shown in the Government account with the Bank of Greece and the data of the budget prepared by the Ministry of Finance. The discrepancy in the final deficit is, however, quite small.

According to a report submitted by the Ministry of Finance to Parliament on the execution of the budget for the fiscal year April 1, 1946 to March 31, 1947, total government receipts amounted to 1,553.3 million drachmae and expenditure to 1,938.9 million, the deficit being 385.6 million drachmae. Of the total receipts, 605 million were derived from the sale of UNRRA supplies and 36 million

from the sale of tobacco recovered from Bulgaria. Thus, more than 40 per cent of budget receipts consisted of extraordinary revenue which did not reflect a permanent improvement in the economic situation of the country. The revival of private import trade in 1946 did not go far enough to prevent import duties, which in the prewar period constituted nearly 30 per cent of total revenue, from dropping to only 5 per cent in 1946-47.

More detailed data concerning the sources of government receipts were presented in a statement of the Greek Ministry of Finance on the government financial position during the first eleven months (April 1946 - February 1947) of the past fiscal year. This reveals both the importance of extraordinary revenue, already mentioned, and the large proportion of taxation revenue derived from indirect taxes (including tobacco tax and import duties).

I. Revenues
(in millions of drachmae)

A. Ordinary Revenues

| | | |
|----------------|----------------|---------|
| Direct taxes | 145,626 | |
| Indirect taxes | 302,633 | |
| Monopolies | 31,507 | |
| Other revenues | <u>165,632</u> | |
| Total | | 645,398 |

B. Extraordinary Revenues

| | | |
|---|---------------|---------|
| Proceeds of sale of foreign supplies | 546,488* | |
| Proceeds of sale of UNRRA cars | 1,439 | |
| Proceeds of sale of State-owned tobacco of Macedonian-Thrace | 36,000 | |
| Other extraordinary revenues | <u>46,818</u> | |
| Total | | 630,745 |

C. Revenues from past years

| | | |
|----------------|---------------|------------------|
| Total Revenues | <u>30,475</u> | |
| | | <u>1,306,618</u> |

II. Expenditure

Total expenditure (Analysis has been given by Ministries, without any specification of the nature of expenses.)

1,487,611

* Includes the proceeds from sales of UNRRA's supplies and, to an unknown extent, proceeds from sales of supplies imported from abroad by the Government.

No analysis of Government expenditures during the past fiscal year is available. In the budget submitted for approval by Parliament in the summer of 1946, provision was made almost exclusively for expenses connected with maintenance of the State administration. Salaries and pensions of civil servants and military officers constituted about 50 per cent of total expenditures. This percentage was further raised by increases of 25 per cent in salaries and pensions in June, 1946, and by additional monthly allowances from February, 1947, of 100,000 drachmae per civil servant and 50,000 drachmae per pensioner.

Budget expenditure for reconstruction and social welfare purposes has been extremely low. Only 45,681 million drachmae, or 2.9 per cent of total expenditure, were allocated for the execution of public works, and for reconstruction purposes 100,000 million drachmae, or 6.3 per cent of total expenditure.

A large proportion of Government expenditure is absorbed directly by the War Ministries and the Public Security Ministry, even though war material has been delivered to Greece by the British Government without payment.

The absence of an efficient and flexible system of income taxation allows large amounts of industrial, commercial and other profits to escape taxation. A re-organization of the fiscal services of the Government is urgently needed in order to secure larger amounts of ordinary revenue, especially from income taxation. Such reforms would not only contribute to greater financial stability but would also lead to a more equitable distribution of the national income. On the expenditure side, apart from military expenses, the cost of the civil service presents serious difficulties for which no obvious solution is in sight. Even after the recent increases, the salaries and pensions of civil servants still fail to ensure an adequate standard of living. Their number is probably excessive, but a sudden contraction in the volume of civil service employment would create serious social difficulties.

5. Foreign Exchange Control

According to the laws established for the protection of the national currency, all foreign exchange transactions, including payments for imports and exports, are carried out exclusively by the Bank of Greece and other authorized banks which have to report to it. The law provides that foreign exchange derived from exports or other sources must be offered for sale to the Bank of Greece or other authorized banks, and payments in foreign exchange are permitted only in cases specified by the law, e.g., for imports, travel expenses, and remittances abroad, for which a permit by the competent authorities has been issued.

The procedure applied after February, 1946, for regulating imports was as follows: All commodities were divided into two classes. For Class A, which included foodstuffs, clothing, and other essential goods no import license was required and foreign exchange was freely allocated by the Bank of Greece. For imports of goods in Class B, which included all other commodities, an import license was required, issued by the Ministry of National Economy, after consultation with a special committee consisting of civil servants and employees of the Bank of Greece. In practice, however, licenses for any kind of import were freely given to importers who already had legally in their possession abroad the foreign exchange necessary to pay for imports.

At the end of November, 1946, the almost complete exhaustion of the foreign exchange and especially of the dollar holdings of the Bank of Greece made a

tightening of import restrictions inevitable. Certain commodities were transferred from Class A to Class B; even for imports in Class A, as well as for Class B imports, for which licenses had been granted, confirmed credits could not be opened without an assurance that the foreign exchange necessary for their purchase was actually available. Importers possessing private foreign exchange assets abroad were also no longer given priority over other importers, while the legality of these private foreign exchange holdings was to be more strictly controlled. These measures were clearly designed to discourage importers and others from acquiring foreign exchange in the free market in which the strong demand for foreign exchange was partly the result of the import privileges previously enjoyed by owners of foreign exchange.^{1/}

The whole question of import restrictions is now under consideration by the Greek Government and the U.S. Mission in Athens with a view to formulating a new foreign trade and exchange policy.

All foreign exchange transactions carried out through legal channels are calculated on the basis of the official rates of the Bank of Greece, as established by Law 879 of January 25, 1946. These rates are 5,000 drachmae for the U.S. Dollar and 20,000 drachmae for sterling with selling and buying rates 0.4 per cent above or below the official par value. Exchange rates for other currencies are fixed on the basis of the corresponding cross rates.

The black market in foreign exchange is very extensive and its rates are far above official quotations. The average "free" market rate of the U.S. dollar was 6,500 drachmae in 1946 and 7,800 drachmae in the first five months of 1947, corresponding to premiums of 30 and 56 per cent, respectively. According to recent information from Greece the rate had risen in early August to 9,300 - 9,400 drachmae corresponding to a premium of about 86 per cent. The black market rates reflect not only distrust of the currency but also the risk involved in illegal transactions.

6. Foreign Trade

Imports

In both 1945 and 1946 UNRRA deliveries constituted the greater portion of Greek imports, but in 1946, imports effected by the Greek Government and private individuals showed a considerable increase. The value of UNRRA imports in 1946 has been estimated at \$210 million, compared with \$176 million in 1945. No detailed or complete data are available concerning other imports or exports; the foreign exchange control records of the Bank of Greece are the main source of information.

According to these records foreign exchange sold in 1946 for imports amounted to \$146.6 million, a figure however which does not correspond either with the value of imports during the year, or with the total amount of confirmed

^{1/} For details of the foreign exchange policy announced in October, 1947, see R.D. Memorandum 392.

credits abroad for Greek imports.^{1/} The purposes for which exchange was sold are as follows:

| <u>Imports</u> | <u>Dollars</u> | <u>Sterling</u> | <u>Total</u> (in million dollars) |
|---|----------------------|---------------------|--------------------------------------|
| Coal | \$ 4,073,639 | £ 988,032 | \$ 8.0 |
| Petroleum products | 3,312,647 | 1,647,239 | 9.9 |
| Machines, spare parts & metal products | 3,353,526 | 1,445,187 | 9.1 |
| Drugs & chemical pro- ducts | 3,671,033 | 699,741 | 6.4 |
| Foodstuffs | 14,335,250 | 13,155,814 | 66.9 |
| Paper & paper products | 865,431 | 46,498 | 1.0 |
| Industrial raw materials | 7,654,714 | 1,855,303 | 15.0 |
| Automobiles & parts | 1,137,397 | 104,879 | 1.5 |
| Clothing | 5,483,145 | 466,053 | 7.3 |
| Leather & leather articles | 3,969,504 | 376,021 | 5.5 |
| Timber | 1,698,230 | 153,227 | 2.3 |
| Miscellaneous | <u>8,123,405</u> | <u>1,387,871</u> | <u>13.7</u> |
| | \$ <u>57,677,921</u> | £ <u>22,325,865</u> | \$ <u>146.6</u> |

A second estimate of the value of imports, based on Bank of Greece records of actual payments and transfers to the accounts of its foreign correspondents for import purposes, gives a total of more than \$200 million, of which approximately \$150 million were paid for imports by private importers and the rest for imports by the Government. These figures include an unknown amount of confirmed credits still outstanding on December 31, 1946, some of which were utilized in 1947, while others were cancelled.

Figures recently presented by Greek officials in Athens newspapers give a third indication of the total value of Greek imports in 1946. According to these sources, the total amount of confirmed credits opened abroad for the import of goods, on account of both the Government and private importers, totalled an equivalent of U.S. \$178.5m; of this amount, credits of \$30.5 million were subsequently cancelled, reducing effective credits to \$148.0 million. In execution of these credits, goods valued at \$112.6 million were actually imported into the country up to December 31, 1946. It may be assumed that goods not delivered by the end of 1946 were imported during the first six months of 1947, but additional cancellations of confirmed credits may also have taken place. It is claimed that of the total amount of imports (\$112.6), 41.1 per cent consisted of foodstuffs, 18.7 per cent of raw materials, 6.4 per cent of footwear, 5.2 per cent of clothing, 6.2 per cent of petroleum products, and the remaining 22.4 per cent of various other items, figures which correspond roughly to the breakdown of the first estimate.

^{1/} When a confirmed credit for imports is opened, the Bank of Greece debits the foreign exchange account with only that percentage of the whole amount of the credit, which importers must pay in drachmae at the time of confirmation of credit (20-60 per cent); an entry for the remaining part is made only when the importer settles the balance, i.e., at the time of the actual importation of the commodities.

Whichever of the three estimates presented above is accepted, Greek imports in 1946 (including those of UNRRA) amounted to at least \$300 million. In the prewar period (1936-39) average annual imports amounted to only about \$120 million, equivalent to approximately \$240 million at postwar prices if it is assumed that prices have risen by 100 per cent. It would therefore appear that Greek imports in 1946 were well above the prewar level, a fact to be explained by the very low level of domestic production and the inclusion in UNRRA imports of certain items, such as agricultural machinery, which were not normally imported before the war.

According to the above-mentioned statement of Greek officials, imports of foodstuffs, clothing, footwear, raw materials, and petroleum products absorbed about 77.6 per cent of the total foreign exchange expenditure. This, however, does not mean that luxury foodstuffs, clothing, etc. have not been imported. Both official foreign exchange holdings and foreign exchange in the hands of individuals derived from illegal transactions have been used to a considerable extent for non-essential imports. Private importers moreover have in fact been free to sell imported goods on the free market at high prices or to hoard them in the expectation of further price increases. It is also reported that the lack of strict and efficient control of the inflated declared values of imported goods permitted to some extent flight of capital from the country.

Exports

The value of exports during 1946 may be estimated from the following table showing the foreign exchange proceeds acquired by the Bank of Greece:

| <u>Exports</u> | <u>Dollars</u> | <u>Sterling</u> | <u>Total</u> (in million dollars) |
|----------------|----------------------|-------------------|--------------------------------------|
| Tobacco | \$ 23,984,413 | £ 724,537 | \$ 26.7 |
| Currants | 422,679 | 529,785 | 2.5 |
| Figs | 148,955 | 41,398 | 0.3 |
| Olives | 742,924 | 204,334 | 1.6 |
| Olive-oil | 40,557 | 5,556 | 0.1 |
| Leather | 456,548 | 85,161 | 0.8 |
| Other items | <u>1,656,898</u> | <u>761,377</u> | <u>4.7</u> |
| Total | <u>\$ 27,452,984</u> | <u>£2,352,148</u> | <u>\$ 36.7</u> |

The average annual prewar value of exports was approximately \$79.3 million. On the assumption of a price increase of 100 per cent, the volume of Greek exports in 1946 may therefore be estimated at about 23 per cent of the prewar level.

Greek exports have been handicapped by the disparity between high domestic costs and the world price level. Devaluation of the drachma would involve the risk of a further rise in the cost of living; nevertheless, many Greek economists, though with great hesitation, believe that it is the only measure by which exports might be expanded. It is, however, questionable whether devaluation would solve the problem of finding new export markets to replace Germany, which in the prewar period was Greece's chief trading partner for both imports and exports. Trade relations with most central and eastern European countries have not yet been resumed. Commercial agreements concluded with certain countries (Austria, France, Switzerland, Czechoslovakia) have so far produced negligible results.

7. Balance of Payments and Foreign Exchange Resources

In the last prewar years the value of Greek exports amounted to 60-75 per cent of the value of imports; the deficit in the trade balance was covered mainly by emigrants' remittances, shipping receipts and tourist expenditure. After the war exports dropped to a very low level while import requirements were much greater because of the devastation of the country and the exhaustion of commodity stocks. In 1946, the value of exports corresponded to no more than 10 per cent of the total value of imports. It has always been difficult to prevent a large part of Greek shipping earnings from being held abroad, and the fraction of those earnings which now becomes available to the exchange control authorities is quite negligible. Emigrants' remittances increased above prewar levels in 1945 and the early months of 1946, but since September, 1946, a large part of these remittances has escaped the control of the Government, conversion into drachmae on the black market being a much more profitable operation for their recipients. Receipts from tourist expenditure have entirely disappeared.

Import requirements have so far been met mainly with the aid of UNRRA and from prewar official holdings of foreign exchange. No official estimates of the balance of payments of Greece have been published. Rough estimates for 1945 and 1946, based on foreign exchange control records, are given in Table C.

Unless drastic monetary and economic measures are taken, there is little hope that Greece's foreign exchange receipts will be larger in 1947 than they were in 1946. On the basis of last year's experience, it may be estimated that foreign aid to the amount of \$300 million will be required in 1947 in order to cover the most urgent current needs.

The serious reduction of Greek foreign exchange resources, which is a measure of the cost of the stabilization policy applied since February, 1946, is shown in the records of the net gold and foreign exchange position of the Bank of Greece on January 31, 1946, and June 30, 1947.

Net Gold and Foreign Exchange Position of the Bank of Greece

| | Gold (ounces) | U.S. Dollars | Sterling | Total U.S. \$ Equivalent |
|------------------------------|------------------------|----------------------------|------------|-----------------------------|
| January 31, 1946 | 800,670 | 42,403,060 | 30,596,691 | 193,497,690 |
| June 30, 1947 ^(a) | 428,143 ^(b) | - 7,670,000 ^(c) | 23,053,794 | 100,096,940 |

(a) This statement includes (1) the monetary reserve account representing balances of £ 19,000,000 and \$3,030,000, (2) some \$1,200,000 advances in drachmae to American Forces in Greece, pending definite settlement on the part of the U.S. Government. Foreign Exchange earmarked for confirmed credits opened abroad for imports is excluded even when the goods have not yet been imported.

(b) Includes gold used as collateral for a loan of \$10,800,000 granted by the Federal Reserve Bank of New York.

(c) Excludes a loan of \$10,800,000 granted by Federal Reserve Bank of New York which covers the deficit in dollars shown above.

The decrease in the gold and foreign exchange net position during the whole period is \$93 million. Without the extraordinary foreign exchange receipts of £ 15 million (£ 10 million from the British stabilization loan plus £ 5 million on account of advances to British Forces released in February, 1947), the total decrease would have reached about \$153 million. For practical purposes, the foreign exchange holdings of the Bank of Greece had by the end of June, 1947, fallen to a negligible figure. The most important item was a balance of about £ 23,000,000 including £ 19,000,000 in the stabilization account. These sterling holdings are not freely convertible and the use of the British stabilization loan of £ 10 million would probably not be permitted, even for sterling area imports.

TABLE A. - Price and Monetary Data, Greece

| | Cost of Living Index ^{1/} | Athens Market Retail Price Index ^{2/} | Free Market Gold <u>Sovereign Rate</u> Monthly Average | Index | Note Circulation (In millions of drachmae) ^{3/} | Index |
|-----------------------|--|--|---|--------|--|-------|
| Average: year 1938 | 100 | -- | -- | -- | -- | -- |
| October 1940 | -- | 100 | 1,168.6 | 100 | 11,801 | 100 |
| <u>1946</u> | | | | | | |
| January | 15,586 | 21,109.7 | 148,346. | 12,694 | 131,472 | 1114 |
| February | 13,456 | 18,409.7 | 141,708 | 12,126 | 218,645 | 1853 |
| March | 13,734 | 18,337.8 | 135,875 | 11,627 | 278,743 | 2363 |
| April | 14,038 | 17,576.6 | 136,000 | 11,638 | 363,533 | 3081 |
| May | 14,210 | 17,523.4 | 134,750 | 11,531 | 389,414 | 3300 |
| June | 14,246 | 16,224.2 | 136,982 | 11,722 | 411,994 | 3492 |
| July | 14,217 | 14,951.6 | 134,585 | 11,517 | 444,129 | 3763 |
| August | 13,775 | 15,038.7 | 134,962 | 11,549 | 495,850 | 4193 |
| September | 14,224 | 15,509.7 | 135,587 | 11,603 | 511,669 | 4337 |
| October | 14,661 | 16,029.8 | 135,696 | 11,612 | 505,320 | 4282 |
| November | 15,197 | 16,016.9 | 136,264 | 11,660 | 468,041 | 3966 |
| December | 14,337 | 15,885.5 | 136,212 | 11,656 | 537,463 | 4554 |
| <u>1947</u> | | | | | | |
| January | 15,405 | 16,221.0 | 139,116 | 11,905 | 499,325 | 4231 |
| February | 15,605 | 16,343.5 | 138,583 | 11,859 | 523,540 | 4436 |
| March | 15,883 | 15,701.6 | 134,980 | 11,551 | 559,371 | 4740 |
| April | 16,020 | 16,035.5 | 128,275 | 10,977 | 656,984 | 5567 |
| May | 16,511 | 16,651.6 | 132,012 | 11,297 | 676,158 | 5730 |
| June | 16,587 | 16,646.0 | 135,217 | 11,571 | 690,452 | 5851 |

^{1/} The cost of living index is compiled by the Research Department of the Bank of Greece on the basis of the expenditure of a family of about six persons, food expenditure representing nearly 3100 calories per person per day. The prices of rationed food used in this index are usually far below free market prices. The index also includes housing rents and utility rates, e.g., electric current, gas, streetcar fares, which are controlled by the Government. There is therefore a considerable discrepancy between the two series of figures quoted above, which would be still wider if the cost of living index could be recalculated on the base October, 1940, when prices were already higher than in 1938.

^{2/} The Athens Market Retail Price Index is the monthly average of daily price indices, which result from a calculation of the arithmetic mean of price relatives, based on free market prices of 21 basic commodities: bread, meat (calf), olive-oil, fish (marides), eggs, sugar, olives, macaroni, rice, white cheese, 3 kinds of vegetables, varying according to the season, potatoes, soap, charcoal, wood, drill cloth, calico, leather for soles, and wine. The index was originally compiled by the Research Department of the Bank of Greece with 1938 as base, and has been adjusted to the new base of October, 1940. The table above shows the latest available revised figures, which are not identical with those quoted in R.D. 221.

^{3/} End of month figures; for October, 1940, average of the note circulation on 7, 15, 23 and 31 October, 1940.

TABLE B

Government Payments and Receipts.
as Recorded in the Concentration Receipts and Payments Account of
the Government with the Bank of Greece
(in millions of drachmae)

| | <u>Payments</u> | <u>Receipts</u> | <u>Surplus of Receipts (+) or Payments (-)</u> |
|---------------------------------------|-----------------|-----------------|--|
| November 11, 1944 - January 31, 1946. | 181,193 | 82,411 | - 98,782 |
| <u>1946</u> | | | |
| February | 114,467 | 41,802 | - 72,665 |
| March | 192,986 | 65,864 | - 127,122 |
| April | 150,954 | 69,981 | - 80,973 |
| May | 214,764 | 94,822 | - 119,942 |
| June | 76,774 | 91,842 | + 15,068 |
| July | 142,615 | 129,035 | - 13,580 |
| August | 139,175 | 117,843 | - 21,332 |
| September | 133,456 | 153,780 | + 20,324 |
| October | 140,901 | 169,449 | + 28,548 |
| November | 182,687 | 155,252 | - 27,435 |
| December | 265,001 | 165,002 | - 99,999 |
| <u>1947</u> | | | |
| January | 136,626 | 164,700 | + 28,074 |
| February | 254,970 | 169,662 | - 85,308 |
| March | 213,792 | 198,922 | - 14,870 |
| April | 225,124 | 268,576 | + 43,452 |
| May | 329,494 | 311,069 | - 18,425 |
| June | 268,923 | 235,075 | - 33,848 |

TABLE C - Balance of Payments Estimates for Greece, 1945 and 1946 ^{1/}
(in millions of U.S. dollars)

CONFIDENTIAL

| | 1945 ^{2/} | 1946 | Debits | 1945 ^{2/} | 1946 |
|--|--------------------|-------|---|--------------------|---------------------|
| Credits | | | | | |
| I. <u>Movement of Goods and Services</u> | | | | | |
| 1. Exports | 0.3 | 36.7 | 7. Imports | 5.9 | 146.6 ^{3/} |
| 2. Emigrants' remittances and shipping | 24.6 | 37.6 | Private and Government | 176.0 | 210.0 |
| 3. Miscellaneous receipts | 3.7 | 16.7 | UNRRA | 6.3 | 6.3 |
| | | | 8. Government expenses abroad | -- | 3.8 |
| | | | 9. Expenses of Greeks traveling abroad, subsistence etc. | -- | 0.5 |
| | | | 10. Insurance premiums | 1.9 | 5.5 |
| | | | 11. Other expenses abroad | -- | -- |
| | | | 12. Foreign exchange sold through branches of the Bank of Greece and other banks for payments abroad, not yet accounted for (net) | -- | 6.6 |
| II. <u>Unilateral Transactions</u> | | | | | |
| 4. UNRRA assistance | 176 | 210 | | | |
| III. <u>Capital Movements</u> | | | | | |
| 5. British Government stabilization loan | -- | 40.3 | 13. Increase in foreign exchange and gold assets of the Bank of Greece | 14.0 | -- |
| 6. Decrease in foreign exchange and gold assets of the Bank of Greece | 204.6 | 297.6 | 14. Internal sales of gold | 0.5 | 18.3 |
| | | | | 204.6 | 397.6 |
| <p>^{1/} The advances in drachmae made by the Bank of Greece to the British and American Forces are not presented above in the credit side as foreign exchange receipts, because accounts with the two Governments have not yet been settled. In regard to the advances to British Forces in particular, it is not known what part of these will finally constitute a charge against the Greek Government for expenses incurred on Greek account. No information is available on (a) expenses incurred by the British Government for the Greek Army, (b) utilization of the Export-Import Bank credit of \$25 million, (c) utilization of the American loan of \$55 million for the purchase of American surplus army stocks.</p> <p>^{2/} For the period October, 1944 - December 31, 1945</p> <p>^{3/} The nature and reliability of this estimate has been discussed earlier in the paper, see pages 13 and 14.</p> | | | | | |