EUROPEAN CENTRAL BANK

EUROSYSTEM

Press release

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ECB reports on progress towards euro adoption

- Biennial report assesses progress towards euro adoption in Bulgaria, Czech Republic, Hungary, Poland, Romania and Sweden
- Inflation above reference value seen as key economic obstacle in central and eastern European countries under review
- Legislation in five of six countries under review not fully compatible with legal requirements for euro adoption
- Economic activity expected to strengthen in 2024, but outlook clouded by geopolitical uncertainty

Limited progress has been made by non-euro area Member States of the European Union (EU) on economic convergence with the euro area since 2022, according to the 2024 Convergence Report of the European Central Bank (ECB) [link]. This is mainly due to challenging economic conditions.

Over the past two years, the countries under review have been hit by the fallout from Russia's invasion of Ukraine, which led to a significant weakening of economic activity and soaring inflation. Countries with a history of higher energy dependence on and stronger trade links with Russia were the most affected. Looking ahead, economic activity is expected to strengthen in all of the countries under review, but geopolitical tensions and risks are clouding economic prospects.

As regards the **price stability criterion**, five of the countries under review – Bulgaria, the Czech Republic, Hungary, Poland and Romania – recorded average inflation rates well above the reference value of 3.3%, while inflation was slightly above the reference value in Sweden (Chart 1). The reference value is based on the three best-performing Member States over the past 12 months, i.e. Denmark (1.1%), Belgium (1.9%) and the Netherlands (2.5%), taking their average inflation rates over the past 12 months and adding 1½ percentage points. One outlier, Finland, was excluded from this calculation.

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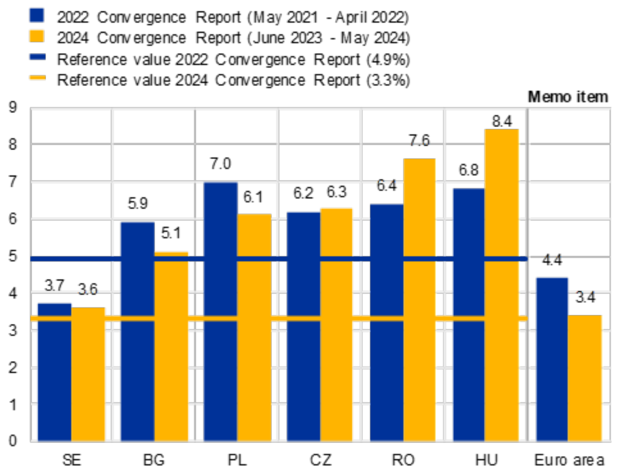
Chart 1

HICP inflation

(average annual percentage changes)

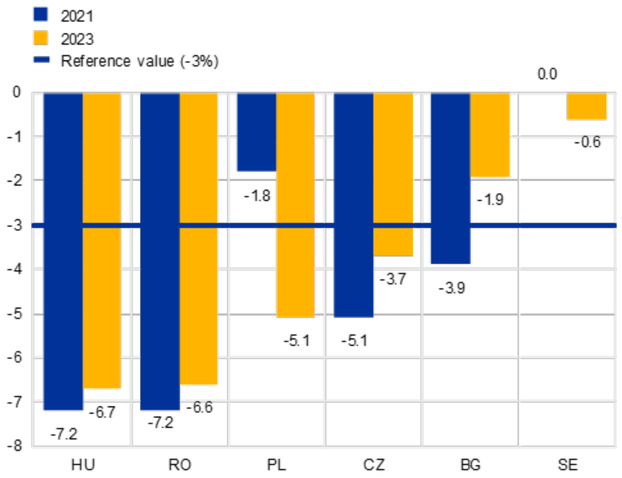


Source: Eurostat.

Chart 2

General government surplus (+) or deficit (-)

(percentages of GDP)



Source: Eurostat.

The **fiscal deficit** in 2023 improved compared with its 2021 level in four of the countries covered in this report, owing to the post-pandemic economic recovery and the phasing-out of fiscal support measures. However, this improvement was in part curbed by the economic impact of Russia's war against Ukraine, including weaker economic activity, and fiscal policy measures taken in response to high energy prices. In 2023 the Czech Republic, Hungary, Poland and Romania exceeded the deficit

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reference value of 3% of GDP (Chart 2). The **government debt-to-GDP ratio** in 2023 was below the reference value of 60% in all of the countries under review except Hungary. In 2024 and 2025 the budget balance is expected to continue to exceed the reference value in Hungary, Poland and Romania.

Romania continues to be subject to an **excessive deficit procedure**, which was opened in 2020. On 19 June 2024 the European Commission found that Romania had not taken effective action to end its excessive deficit. The Commission recently also concluded that Hungary and Poland did not fulfil the government deficit criterion under the Stability and Growth Pact. The Commission will recommend to the EU Council to open excessive deficit procedures for these countries.

As regards the **exchange rate criterion**, only the Bulgarian lev is participating in the exchange rate mechanism (ERM II). Bulgaria joined ERM II with its existing currency board in place as a unilateral commitment in July 2020. This agreement on participation in ERM II was based on a number of policy commitments made by the Bulgarian authorities. Bulgaria is currently working towards completing these policy commitments, including by strengthening its anti-money laundering framework.

With regard to the **convergence of long-term interest rates**, three of the six countries under review (Poland, Romania and Hungary) recorded long-term interest rates above the reference value of 4.8%.

The **strength of public and economic institutions** is an important factor in the sustainability of convergence over time. With the exception of Sweden, indicators published by international organisations suggest that the quality of institutions and governance in the countries under review remains weaker than elsewhere in the EU.

As for the **compatibility of national legislation** with the Treaties and the Statute of the ESCB and of the ECB, five of the six countries under review were not fully compatible with the requirements for the adoption of the euro. With regard to Bulgaria's legislation, the report concludes that its national legislation is consistent with the Treaty and the Statute, subject to conditions and interpretations set out in the relevant country assessment.

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Notes

- The European Commission's Convergence Report [link]
- The ECB's Convergence Report reviews the economic and legal convergence of non-euro area EU Member States with a derogation every two years or at the request of a specific country. It assesses the degree of sustainable economic

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convergence with the euro area, whether the national legislation is compatible with the EU legal framework, and whether the statutory requirements are fulfilled for the respective national central banks. Given its “opt-out” clause, Denmark is not included in the assessment unless it so requests.

- The cut-off date for the statistics included in this Convergence Report was 19 June 2024. The reference period for both the price stability criterion and the long-term interest rate criterion is from June 2023 to May 2024. For exchange rates, the reference period is from 20 June 2022 to 19 June 2024. Historical data on fiscal positions cover the period up to 2023. Forecasts are based on the European Commission’s Spring 2024 Economic Forecast and the most recent convergence programmes of the countries concerned, as well as other information relevant to a forward-looking examination of the sustainability of convergence.

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