CONVERGENCE CRITERIA

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Glossary*
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Convergence criteria or, as they are also known, the Maastricht criteria, are the criteria that member states of the EU have to meet in order to enter into third stage of the Economic and Monetary Union, the EMU, and so adopt the euro. These criteria have been framed on the basis of the provisions of Article 121 (1) of the Treaty establishing European Union (Treaty). Those countries, then, that are preparing to introduce the euro must meet the following four criteria.

1 Price stability

The Treaty states: "The achievement of a high degree of price stability… will be apparent from a rate of inflation which is close to that of, at most, the three best performing Member States in terms of price stability,"

In practice, the rate of inflation of a given member state must not be greater than 1.5 percentage points of the average rate of inflation of the three EU countries with the lowest inflation in the year preceding the examination in the EMU candidate country. The rate of inflation is measured by the consumer price index.

2 Government finances

The Treaty states: "The sustainability of the government financial position … [is] defined by a government budgetary position without a deficit that is excessive".

In practice, the European Commission, when it draws up the annual recommendations it sends to the

Council of Finance Ministers examines budgetary discipline pursuant to the following two criteria.

• Government deficit: general government budgetary deficit must not exceed 3% of GDP at the end of the previous financial year. If this is not the case, the deficit can be allowed to be temporarily over the 3% level, but still within reach of it.

• Government debt: the gross general government debt must not exceed 60% of GDP at the end of the precious financial year. If this is not the case, the percentage must nevertheless show a tendency towards a signification reduction, and must be converging on the reference value with a satisfactory dynamic.

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3 The exchange rate

The Treaty stipulates: “The observance of the normal fluctuation margins provided for by the exchange rate mechanism of the European Monetary System, for at least two years, without devaluing against the currency of any other Member State”.

A member state has to take part in the Exchange-rate mechanism, or ERM of the European Monetary System, EMS, uninterruptedly during the two years preceding the examination of the situation. This means that fluctuations of exchange rate between the euro and the currencies of the members must move within agreed-on limits. Apart from that, in the same period, a member state is not allowed to devalue its currency. After transition into the third stage of the EMU and after accepting the euro, the EMS was replaced by the new exchange mechanism (ERM II).

This last could well be clarified. The European Monetary System was established in 1979 as an agreement with which member states linked their currencies in order to stop their large fluctuations, to create monetary stability and to prepare for the introduction of a common currency. In 1999, the EMS was replaced by ERM II, and the euro became an anchor for the countries taking part in it. These were EU member states that had not yet accepted the euro, and that two years before joining the Eurozone had to participate in ERM II.

4 Long-term interest rates

The Treaty states: “The durability of convergence achieved by the Member State … [is] reflected in the long-term interest-rate levels”.

The nominal long-term interest rate (on government bonds or similar securities) must not in practice exceed by more than two percentage points the corresponding interest rate in the (at most) three member states with the lowest rate of inflation (the same countries mentioned in the price stability criterion). The consideration period is a year before the beginning of the examination of the situation in a particular member state that is a candidate for the EMU.

In order to facilitate and maintain the Economic and Monetary Union in the part concerning managing fiscal policies, since January 1999, the Stability and Growth Pact has been in place. The objective of this Pact is to maintain budgetary discipline in the member states after the introduction of the euro. The chief principle that binds all the member states is the maintenance of a balanced budget. The dual anchor with which this principle is implemented comprises the two convergence criteria related to government finances: the budgetary deficit must not exceed 3% of GDP and government debt must not be greater than 60% of GDP. If the existence of an excessive deficit is established, the Commission and the Council of Europe will instruct the member state to take appropriate measures to reduce the excessive deficit. The Pact provides for certain sanctions to be applied to a member state that has not stabilised its public finances. They range from the interest-free deposit that a member state has to make in the Union to its transformation into a non-returnable penalty if the deficit is not adjusted in a period of two years. But there is no ultimate rule concerning the implementation of these penalties – they are the subject of assessment by the Council based on an evaluation of the circumstances in which the given country is situated.

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