

Lars Calmfors: Estonia could get euro and Latvia could devalue

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Stockholm University professor Lars Calmfors says that he would not be surprised if Estonia gets the euro and Latvia devalues. "This is a competitive situation."

He said that the only reason for Estonia to postpone switching to euro is if the country wants to devalue its currency.

"I think the most important factor here is not economy, but Estonia's geopolitical location that was the key driving force also behind Finland's decision to adopt the euro. The country whose neighbour is Russia needs as close ties with Western Europe as possible," said Calmfors to Äripäev.

Calmfors said that since Estonia seems to want to keep its fixed peg, joining the eurozone would be the natural thing. "Sweden with its floating exchange rate is benefiting from staying away from the eurozone," he said.

He said that Estonia's accession to eurozone would be justified also by the large share of trade Estonia does with eurozone countries. "I would also mentioned the risk of political instability since populist parties are more likely to dominate in new member states than old ones. This populism could be used to force a devaluation. Estonia is balancing the fixed exchange rate with its flexible approach to salaries and prices. Also Estonia's workforce seems to be flexible and willing to seek job abroad when the domestic economy is in crisis. These are important adjustment mechanisms."

"Keeping your national currency would enable you to change the exchange rate. On the other hand, own currency means higher interest rates - this is the price of having it."

Speaking of devaluation, Calmfors said that Latvia and Estonia would overcome the crisis faster if they decided to devalue. "Now the crisis will last longer."

Calmfors said that he believed that the euro would bring more foreign investments into Estonia. "The risk of devaluation would disappear," he explained.



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