Estonia adopts the euro

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At the start of the year, Estonia became the 17th country to adopt the euro. After Slovenia and Slovakia, Estonia is now the third eastern European country and the first former Soviet republic to join the eurozone.

Representatives of the European Union have sought to portray the country's entry into the crisis-ridden eurozone as a vote of confidence in the joint currency. "The entry of Estonia into the euro area sends a strong message about the attractiveness of the euro and the stability that this brings to the member states of the European Union," said José Manuel Barroso, the president of the European Commission.

In fact, the introduction of the euro is bound up with huge social sacrifices for Estonia's 1.3 million inhabitants. On closer inspection, the country's reputation for financial stability is also suspect.

Thanks to double-digit economic growth, the country gained the reputation of the "Baltic Tiger". This was mainly because of high direct investments from the Nordic and Central European countries, attracted by low taxes and wages. The country had already made an attempt to introduce the euro in 2007 but postponed the process because of fears of growing inflation.

The outbreak of the economic and financial crisis ended the boom. In 2009, economic output fell by over 14 percent. Unemployment shot up above 15 percent.

The government in Tallinn introduced a rigid austerity programme, comprising 8 percent of GDP to meet the targets set by Brussels. The wages of state employees were cut by about 30 percent and massive cuts in social benefits introduced. In this way, the budget deficit could be pushed down to just 1.5 percent of gross domestic product at the expense of the general population. With just 7.2 percent of GDP, the total debt of the state reached a low level in comparison to other EU countries.

The austerity measures have led to widespread poverty, and in many regions social infrastructure barely exists. Estonia is now the poorest country in the euro community. More than 100,000 people currently live below the poverty line, and unemployment is officially almost 20 percent. Thousands of people have emigrated. According to a recent survey, they will be followed in the spring by a further 77,000.

The impact of the austerity measures was heightened by a devaluation of the kroon, which led to falling wages and higher prices. This trend will continue in the new year.

Estonian Finance Minister Jurgen Ligi, who was responsible for the recent austerity measures, had announced earlier that the government would be continuing that course. In an interview with the *Frankfurter Allgemeine Zeitung*, he said the government would be "promoting entrepreneurship" and making "work affordable"—in other words, there will be further wage cuts.

Experts agree that the changeover to the new currency will bring drastic price increases. The latest consumer price index confirms this. Day-to-day products have never been as expensive as now.

Few people in this Baltic state still harbour illusions in an improvement in their living standards after accession to the euro area. A survey published just before the beginning of the year by the Estonian Institute of Economics (EKI) showed that only a quarter of Estonians supported the change to the single currency.

Under conservative Andrus Ansip, the Estonian government and senior EU leaders celebrated the country's entry into the single currency. But such statements cannot hide the fact that Estonia's accession to the eurozone will exacerbate the difficulties of the European currency.

The government hopes that adopting the euro will attract more foreign investors and strengthen trade. Estonian Minister of Economic Affairs Juhan Parts speculated recently that the euro would bring the country up to 1 percent growth per year. He was citing estimates by the International Monetary Fund.

But many economists are already predicting that Estonia's accession will not lead to economic expansion for the EU and that Estonia will not be able to keep up the formerly favourable economic data. Although Estonia's gross domestic product will contribute just 0.2 percent of the eurozone's total €8.9 trillion, any economic deterioration there could have implications for the entire euro area.

Although in Brussels everyone is saying that Estonia has done its "homework", even the European Central Bank had to warn that a low inflation rate cannot be maintained and that it can rise dramatically at any time.

The chief economist of the UN Conference on Trade and Economy (UNCTAD), Heiner Flassbeck, sees great risks ahead. "The country has become a member of a community that is being shaken to its core", he said.

He pointed to the huge boom in 2007, which had led to a current account deficit of 17.2 percent of gross domestic product. In comparison, Greece in 2008 managed only 16.4 and Spain 10 percent. This development was only slowed by the collapse of the economy and the subsequent collapse of imports by more than 30 percent in 2009.

Even the often-praised low budget deficit is not very stable. Things are only so good at the moment because the share of government revenues as a part of total product has skyrocketed, despite the "mega-recession and rising government spending". But even that is not permanent.

The enormous scale of private debt is also seen as a problem. The Institute for Macroeconomic Research (IMK) at the Hans-Böckler Foundation has warned of potentially drastic problems due to Estonia's excessive private debt. "The national debt is extremely low in Estonia, which is celebrated everywhere as a contribution to stability", said the scientific director of the trade-related institute, Gustav A. Horn, at a press conference in Berlin. "If you look closely at the numbers, however, one sees that private debt is relatively high", he emphasised.

There are the examples of Ireland and Spain, warned Horn, where it had already been seen how quickly a private debt crisis can become public. The recent problems in the crisis countries were caused not only by government debt, but by private debt as well.