REPUBLIC OF CYPRUS

NATIONAL CHANGEOVER PLAN
FROM THE POUND TO THE EURO

(Revised)

August 2007

MINISTRY OF FINANCE CENTRAL BANK OF CYPRUS

Contents

1. INTRODUCTION

2. BASIC CHARACTERISTICS OF THE CYPRUS ECONOMY

3. CYPRUS'S ROAD TO THE EURO AREA

4. BASIC AIMS OF THE NATIONAL ACTION PLAN

5. TIMETABLE OF THE CHANGEOVER TO THE EURO

6. INSTITUTIONAL FRAMEWORK AND ORGANIZATIONAL STRUCTURE

7. PROGRESS IN THE IMPLEMENTATION OF THE NATIONAL PLAN

8. COMMUNICATION POLICY PLAN

9. OPINION SURVEYS WITH RESPECT TO THE EURO

10. PRIORITIES OVER THE FOLLOWING MONTHS

10.1 INFORMATION CAMPAIGN

10.2 LEGISLATIVE FRAMEWORK

10.3 PUBLIC SECTOR

10.4 BUSINESS SECTOR

10.5 CONSUMERS – POLICY FRAMEWORK WITH RESPECT TO PRICES

10.6 THE VULNERABLE GROUPS OF THE POPULATION

10.7 INFORMING THE TURKISH CYPRIOTS

10.8 FINANCIAL SECTOR

10.9 CO-OPERATION WITH THE EUROPEAN COMMISSION AND THE EUROPEAN CENTRAL BANK

11. BENEFITS AND CHALLENGES

12. CONCLUSIONS

Appendix I - Preconditions for the adoption of the euro: Convergence criteria.

Appendix II - Main features of the Exchange Rate Mechanism II (ERM II).

Appendix III - Composition of Committees.

Appendix IV - Organization Chart Euro Coordinating Group, Ministry of Finance.

Appendix V - Introduction of the euro, rounding up and inflation.

1. INTRODUCTION

The adoption of the euro constitutes a comprehensive undertaking, requiring vision, planning and much preparation by the public sector, financial and business sectors, as well as the other socioeconomic groups. At the same time, it requires that all citizens and residents in Cyprus are informed, in plain language, in a systematic, timely and sound manner.

The National Changeover Plan was formulated jointly by the Ministry of Finance and the Central Bank of Cyprus, based on the relevant decision of the Council of Ministers of 29 December 2004, which provides for the establishment of the appropriate institutional framework and mechanisms for implementing the strategy of the entry of Cyprus into the euro area. By another related decision dated 2 November 2005, the Ministerial Council set 1 January 2008 as the target date for the adoption of the euro.

The National Changeover Plan for the changeover from the pound to the euro was submitted to the competent Committees, the National Changeover Board and the Political Committee for the changeover, on 29 March 2006, for comments and final formulation and thereafter it was submitted to and approved by the Council of Ministers on 13 July 2006.

Taking account of experiences to date, a revised National Changeover Plan was prepared for the changeover from the Cyprus pound to the euro, and was adopted by the Minister of Finance and the Governor of the Central Bank of Cyprus in June 2007. The revised Plan gives emphasis to confronting the concerns of unjustified price increases, through the formulation of a comprehensive policy framework. It gives emphasis also to the supply of information to small enterprises and the vulnerable groups of the population.

The National Plan takes into account the experiences of the countries which have already adopted the euro, including the recent successful adoption of the euro by Slovenia. It draws also on close cooperation with Malta, which, like Cyprus, intends to adopt the euro on 1 January 2008. Furthermore, substantial assistance was provided by the European Commission and the European Central Bank, within the context of the EU institutional framework.

The National Changeover Plan aims at the analysis of the fundamental parameters of the strategic design. First it sets out the basic characteristics of the Cyprus economy and then

describes the course of Cyprus towards the euro area and the anticipated time schedules involved. It then analyses the basic aims of the Plan, the institutional framework and organization structure which has been set up, as well as the actions that have already been taken for the implementation of the Plan. Following this, it describes the approach taken as regards to the formulation of the appropriate legislative framework. It continues by referring to the Communications Policy Strategic Programme, which covers the vital aspect dealing with informing the public. Following the above, the programme for the preparation of the wider public sector, the business sector, matters relating to consumers, the financial sector, as well as the introduction of euro bank notes and coins, are analysed.

The Ministry of Finance and the Central Bank of Cyprus, in close cooperation with the European Commission and the European Central Bank, will continue to work methodically for the introduction of the euro.

The close and harmonious cooperation between the competent authorities of the Republic, the political parties, the employers and trade union organizations, the consumers associations and the mass media, which has already been established and that will be strengthened further, constitutes a guarantee for the successful adoption of the euro.

The competent authorities of the Republic support and will continue to support the work aiming at preparing the economy and the members of the public for the successful adoption of the euro, through the formulation of the appropriate institutional and legislative framework, the setting up of appropriate mechanisms for implementing the National Plan, but foremost through the supply of data and information. The business community and the citizens of the Republic are called upon to contribute by actively participating in the implementation of the National Plan. The universal cooperation and mobilization of all parties cannot but ensure the successful changeover from the pound to the euro.

The successful adoption of the euro is in our hands.

The authorities of the Republic wish to express their warm thanks to the authorities of Greece, Ireland, Slovenia and Malta for their invaluable contribution in the formulation, refinement and implementation of the National Changeover Plan. Special thanks are also

due to the European Commission and the European Central Bank for their valuable cooperation.

2. BASIC CHARACTERISTICS OF THE CYPRUS ECONOMY

Cyprus is a small open and dynamic economy, with tourism and other services sectors constituting the engine powering the economy. It is characterized by a high level of real and nominal convergence with the EU, with its per capita GDP standing at around 94% of the average for the EU27 in 2006.

The course of the Cyprus economy shows a satisfactory picture with the average rate of growth reaching 3.8% in real terms in 2006, compared with the average for the EU25 of around 3%. The satisfactory expansion of economic activity is reflected in the labour market, exhibiting a relatively high level of employment, as indicated by the Labour Force Survey, showing a rate of unemployment for 2006 of 4.5%.

"Underlying" inflation, which excludes transitory effects, including the impact of changes in the price of crude oil (and which reflects more accurately the picture regarding the determinants of the general level of prices), has over the last few years oscillated around a low level of about 2%, indicating that conditions of price stability have been achieved.

In addition, over the last years a substantial improvement in the public finances has taken place. The fiscal deficit for 2006 was reduced to 1.5% of GDP compared to 2.4% of GDP for 2005, reflecting continued implementation of the measures included in the Revised Convergence Programme. These measures (are structural in nature and) aim, amongst other things, in increasing public revenues through mainly the improvement in the tax collection ability of the competent departments/services of the state and the elimination of tax evasion, as well as through the restraining of the growth of public expenditure, particularly of consumption expenditure, to levels below that of the increase in nominal GDP. The public debt, as a percentage of GDP, entered a downward course and is estimated at around 65% in 2006.

The formal establishment of the practice of setting a Medium Term Budgetary Framework of three year duration serves the strategic goal of reducing the fiscal deficit

and the public debt on a sustainable basis, permitting, in parallel, a reallocation of public expenditures in favour of developmental and social expenditures.

The phased implementation from 2007 of the Medium Term Budgetary Framework will enable the linking of the medium term fiscal and structural objectives, included in the Convergence Programmes and the Lisbon Strategy, with the yearly budget preparation process.

The first medium term budgetary framework covers the period 2007 – 2009. This framework will permit:

- The estimation of government expenditures on a three yearly basis, taking into account the revenue of the Cyprus economy.
- The determination of priorities and reallocation of expenditures for the benefit of development and social cohesion.
- The curbing of wasteful expenditure and the phased termination of the use of supplementary budgeting.

The policy of fiscal consolidation which the government is applying successfully will be continued and strengthened, given that it constitutes a substantive prerequisite for the economic and social development of Cyprus and it forms strong foundations for the successful adoption of the euro.

3. CYPRUS'S ROAD TO THE EURO ZONE

(a) Accession of the Republic of Cyprus to the European Union – 1 May 2004

From the time of the accession negotiations and having in mind the benefits from the adoption of the euro, the authorities of the Republic set as a strategic objective the entry of Cyprus into the euro area the soonest possible. In accordance with the Accession Treaty, Cyprus and the other nine countries that acceded to the EU on 1 May 2004 participate in the Economic and Monetary Union (EMU) as "member state with derogation". That is, with its accession to the EU, Cyprus undertook a conventional commitment to adopt the euro, within a reasonable period of time, after fulfilling the necessary preconditions, namely the convergence criteria, known as the Maastricht criteria, which are described in **Appendix I.**

(b) Entry of the Cyprus pound in (ERM II) - 2 May 2005

The entry of the Cyprus pound in ERM II on 2 May 2005 was a milestone in Cyprus's path towards the euro area, since the criterion of exchange rate stability requires the participation of the national currency in ERM II for at least two years. The main features of the ERM II are described in **Appendix II**.

The central rate in ERM II was set on 29 April 2005 as 1 euro = 0.585274 pounds – the same central rate which had been adopted unilaterally by Cyprus since 1992 – with a standard fluctuation band of ±15%. The pound's entry in ERM II sealed the stability of the national currency until the time of its substitution by the euro. Since joining ERM II the pound has remained close and slightly above its central parity, and has not experienced tensions or problems.

(c) Reports on fulfilment of the convergence criteria – 16 May 2007

On 5 November 2005 the Ministerial Council adopted 1 January 2008 as the target date for the adoption of the euro. On 13 February 2007 Cyprus requested from the European Commission and the European Central Bank to assess the fulfilment of the convergence criteria so that Cyprus could adopt the euro on 1 January 2008.

On 15 March 2007 the House of Representatives enacted the required amendments to the legislation on the Central Bank of Cyprus, and hence, legal convergence was achieved. With respect to economic convergence, Cyprus has already fulfilled the inflation and interest rate criteria since 2005, and the fiscal criterion since 2006, while the exchange rate criterion was satisfied on 2 May 2007, when the required two-year participation in ERM II was completed.

On 16 May 2007 the European Commission and the European Central Bank published their convergence reports. The reports concluded that Cyprus has achieved a high degree of sustainable convergence, satisfying all the criteria, economic and legal, to adopt the euro. On the basis of this positive conclusion, the European Commission proposed to the Council of the EU to decide that Cyprus adopts the euro on 1 January 2008.

On 5 June 2007, in the context of the Economic and Financial Affairs Council (ECOFIN) meeting, the Council of the EU shared the European Commission's assessment that Cyprus fulfils the necessary conditions for the adoption of the euro and forwarded this positive assessment to the European Council (which comprises of the heads of state or

government of EU member countries). The European Council at its meeting of 21 June 2007 welcomed the proposal that Cyprus should adopt the euro on 1 January 2008. The ECOFIN Council took the final decision on 10 July 2007, after taking into consideration the opinion of the European Parliament and the outcome of the discussion in the European Council. With the positive decision of the ECOFIN Council, the course towards the actual adoption of the euro has entered its last and most intense phase.

4. BASIC AIMS OF THE NATIONAL ACTION PLAN

The basic aims of the National Changeover Plan concentrate on the timely and complete preparation of the public, the financial – banking and the private – business sectors, as well as of all the citizens living in Cyprus.

Within this context the specific aims are the following:

- The preparation of the Cyprus economy to take advantage of the opportunities and successfully face the challenges which the foreseeable entry of Cyprus to the euro area entails. Consistent with the above, it is the basic objective of the Government to take effective measures to counter the unjustifiable increase in prices during the period surrounding the changeover from the Cyprus pound to the euro.
- The continuation and strengthening of the policy aiming at macroeconomic stability and the continued satisfaction of the convergence criteria, as well as of the provisions of the revised Stability and Growth Pact.
- The promotion of the technical preparations for the adoption of the euro, including the adjustment of the accounting and software systems in the private and public sectors and the formulation of the appropriate legal framework.
- A smooth cash changeover, which includes the timely acquisition of euro banknotes and coins, the safe distribution of adequate quantities into the economy, the facilitation of the public and enterprises on the exchange of cash, and the rapid withdrawal of the Cyprus pound.
- The systematic, timely and correct supply of information to all citizens living in Cyprus. Particular emphasis is given to the information conveyed to vulnerable groups, aliens and the Turkish Cypriots.
- The close cooperation with the competent organs of the EU.

5. TIME SCHEDULE FOR THE CHANGEOVER TO THE EURO

The present section sets out the time schedule of the course that Cyprus has taken towards the adoption of the euro.

- **Council of Ministers decision for the establishment of the National Advisory Board (National Changeover Board) and on the institutional framework for the adoption of the euro – December 2004**
- **Entry in ERM II – 2 May 2005**
- **Council of Ministers decision setting 1 January 2008 as the target date for the adoption of the euro – November 2005**
- **The implementation of the Twinning Programme with Ireland and Malta, with a view to assisting the authorities of the Republic of Cyprus in the preparation of its Strategic Communications Policy Plan – 6 month period, 22 June-22 December 2005**
- **The Central Bank of Cyprus draws on the experience of Greece with respect to the technical, legal and communication aspects of the preparation for the introduction of the euro. In this context, a twinning programme between the Central Bank of Cyprus and the Bank of Greece was implemented in the period July 2005-June 2006. This programme was financed by the European Commission and covered technical assistance.**
- **Formal beginning of the Communication Campaign – May 2005**
- **Adoption of the National Changeover Plan by the National Advisory Board – March 2006**
- **Adoption by the Council of Ministers of the National Changeover Plan – July 2006**
- **Signing of the agreement for the purchase of public relations and promotional services from the private sector (Mediacom) – 27 February 2007**
- **Formal application by the Minister of Finance and the Governor of the Central Bank of Cyprus to the European Commission and the European Central Bank for an assessment of whether Cyprus meets the criteria for entry into the euro area – 13 February 2007**

- **Positive assessment of the application of Cyprus for entry to the euro area by the European Commission and the European Central Bank – 16 May 2007**
- **Positive outcome of the discussion in the European Council of the EU for the adoption of the euro by Cyprus – 21 June 2007**
- **The establishment of a toll free telephone line to serve and inform the public with respect to the euro - 11 June 2007**
- **Adoption of the irrevocable fixing of the exchange rate at which the euro will be substituted for the Cyprus pound – 10 July 2007**

  The conversion rate between the Cyprus pound and the euro was adopted by the Council of the EU, with the unanimity of the countries in the euro area and Cyprus, on 10 July 2007, together with the decision on the abrogation of the derogation.
- **Fair Pricing Code – 10 July 2007 - 10 July 2008**

  With a view to meeting effectively the concerns of the public, regarding unjustifiable price increases, a multifaceted comprehensive policy framework has been established. This policy framework includes the Fair Pricing Code, which aims at committing enterprises, which choose voluntarily to participate, not to apply unjustified increases to their prices during the period of the introduction of the euro. At the same time the enterprises that adopt the Code shall be committed to increased transparency in respect of the pricing policies regarding their products and services.
- **Dual display of prices – 1 September 2007 – 30 September 2008**

  Dual display (in pounds and euro) of the prices of goods and services is expected to begin on 1 September 2007 and to continue for a period of nine months after the adoption of the euro (that is until 30 September 2008). The dual display of prices will be obligatory for all suppliers of goods and services, with but a few exceptions which are specified in the Law.
- **Frontloading of euro banknotes and coins – October-December 2007**

  - Commencement of frontloading (prior supply) of euro coins to banks and (subsequently) sub-frontloading to enterprises – 22 October 2007.

  - Commencement of frontloading of euro bank notes to banks and sub-frontloading to enterprises - 19 November 2007.

- Commencement of distribution of euro coin starter packs to the public and to enterprises – 3 December 2007.

- **Operation of a Euro bus – October-December 2007**

  The Euro bus will operate in all Districts informing the public about the euro.

- **Distribution of converters to all households – November 2007**

- **Adoption of the euro – 1 January 2008**

  - On 1 January 2008 the euro is expected to become the official currency of the Republic of Cyprus, replacing the Cyprus pound. Euro banknotes and coins will be put into circulation and will become legal tender in the Republic.

  - On the euro adoption date (1 January 2008) all accounts denominated in Cyprus pounds with banks and cooperative credit institutions will be converted automatically into accounts denominated in euro, without any charge to the account holder.

- **Period of parallel circulation of the Cyprus pound and the euro – 1-31 January 2008**

  - Cash in pounds will circulate in parallel with the euro and will be accepted for payments for a period of one month after the adoption of the euro.

  - However, payments made by cheques, credit cards or other non-cash means will be made exclusively in euro.

  - Enterprises should give change only in euro.

  - Banks and cooperative credit institutions will exchange cash in Cyprus pounds for euro banknotes and coins, free of charge, up to £1,000 for each transaction in banknotes and £50 in coins from 1 January 2008 for a period of six months. In addition they will accept deposits of any amount of banknotes and coins in Cyprus pounds, free of charge.

- **Celebration of the adoption of the euro – 18 January 2008**

- **Exchanging Cyprus pounds after 31 January 2008**

  - Banks and cooperative credit institutions will continue to accept deposits or exchange cash in pounds for euro (free of charge subject to the ceilings referred to above) up to 30 June 2008 (that is six months after the adoption of the euro).

- The Central Bank of Cyprus will continue to exchange pounds for euro, free of charge, in the case of banknotes for a period of 10 years (up to 31 December 2017), and in the case of coins for a period of 2 years (up to 31 December 2009).

- **Completion of the changeover to the euro – 1 February 2008**

  From 1 February 2008 cash in Cyprus pounds will cease to be legal tender and shall not be accepted for payments. All payments shall be made henceforth in euro.

6. INSTITUTIONAL FRAMEWORK AND ORGANIZATIONAL STRUCTURE

On 29 December 2004, the Council of Ministers adopted the institutional framework and the organizational structure which would regulate the implementation of the National Changeover Plan.

Structure

The basic arrangement of the institutional structure for the implementation of the strategy for the entry of Cyprus to the euro area is the following:

- National Advisory Board (National Changeover Board)
- Political Committee for the changeover of the pound to euro
- Coordinating Committee
- Joint Communications Committee
- Technical committees of the Ministry of Finance/ and the Pubic Service sector
- Technical committees of the Central Bank of Cyprus

Details with respect to the make up of the above committees are set out in **Appendix III.**

The organizational mechanism of implementation of the part of the Plan which falls under the responsibility of the Ministry of Finance is presented in **Appendix IV.**

7. PROGRESS IN THE IMPLEMENTATION OF THE CHANGEOVER PLAN

The implementation of the National Changeover Plan is proceeding at a satisfactory rate. Particular progress has been made in the creation of the institutional and legislative framework and in preparing the public and banking sectors. Noteworthy progress has been noted also in preparing the large and medium-sized enterprises. Based on the results of various opinion surveys the most significant challenges faced, in the period to the changeover to the euro, refer to the preparation of small sized enterprises, in informing

the population residing in rural areas, as well as certain vulnerable groups, such as the retired. In this context, special emphasis will be given to meeting effectively the concerns of the public with respect to unjustified price increases during the period of the changeover from Cyprus pounds to euro, as indeed recent opinion surveys confirm the high levels of this concern (about 83% of respondents in May 2007).

(a) Communication Policy

To activate the Joint Communication Policy, a Strategic Communication Policy Plan was prepared, with partial funding from the European Commission and is being implemented. This strategic Plan is being implemented in close cooperation with all interested parties both in the public and private sector, as well as with the private public relations and promotion firm (Mediacom).

In the context of preparations for successful entry of Cyprus to the euro area, a Twinning Programme was instigated and completed in the period 22 June-22 December 2005, between the Ministries of Finance and the Central Banks of Cyprus and Malta on the one hand and of Ireland on the other. The main objective of the Twinning Program was the utilization of the experiences of Ireland for the formulation of the Communication Policy Plan for the adoption of the euro by Cyprus.

In parallel a twinning programme between the Central Bank of Cyprus and the Central Bank of Greece was implemented in the period from July 2005-June 2006 for the extension of technical assistance on the preparation of the information campaign of the Central Bank of Cyprus and for other matters on the technical preparation of the Central Bank for the adoption of the euro.

Other activities undertaken by the Ministry of Finance and the Central Bank of Cyprus include:

- The distribution of information material to enterprises and the general public, prepared by the authorities in Cyprus, employers and professional organizations, the European Commission and the European Central Bank. The publications covered the preparation of the enterprises for the adoption of the euro, including the crucial retail enterprises sector and the consumers. The publications are distributed through the various business associations, with large membership, which act as Europartners in implementing the Plan for the conversion to the euro and through functions, seminars,

presentations, as well as through the joint euro internet site of the Ministry of Finance and the Central Bank of Cyprus.

- The organization of two large events (31 May and 30 November 2006) with wide participation of European Commission and European Central Bank officials, as well as internationally acclaimed experts and researchers, with a view to transmitting their international experiences regarding the adoption of the euro to the general public in Cyprus. Turkish Cypriots were invited and, indeed, participated in both of the above events.
- The organization of a large number of presentations and seminars on matters relating to the euro, given by the Minister of Finance and Officers of the Ministry, as well as by the Governor of the Central Bank of Cyprus and senior officers of the Bank to the mass media. During the first phase of this information campaign emphasis was given to analysing the benefits to be obtained and the challenges to be faced, as well as in explaining, in general terms, basic matters related to the adoption of the euro, such as the dual display of prices, the Fair Pricing Code, the arrangements for the frontloading of euro banknotes and coins, the exchanging of Cyprus pounds into euro, the period of parallel circulation, etc. Emphasis was given also to encouraging enterprises to make timely preparations.
- The arrangement of special presentations dealing in depth with the experiences of Greece given by Officials from Greece. This was considered necessary having in mind the results of various opinion polls which confirmed that the public in Cyprus is concerned that the adoption of the euro would lead to unjustifiable price increases. This opinion owed mainly to the mistaken perceptions and information on the experiences in Greece.
- The organization of a special seminar, regarding the experiences in price developments in the member countries of the EU, during the changeover from national currencies to the euro in 2002. For this subject an expert was called in from the European Central Bank. Within this context a study was prepared by the economic studies Centre of the University of Cyprus, entitled "Introduction of the Euro, Rounding and Inflation: Myths and Reality", **Appendix V**. The aim of the

above actions was the dissemination of impartial information on the subject of price developments which is of particular concern to the public in Cyprus.

- The arrangement of educational lectures at secondary schools, the National Guard, in the districts and communities in Cyprus. The lectures at secondary schools and the National Guard aim at informing the youth of Cyprus and through them the older generations. The lectures in the districts and communities target the rural population, which according to various surveys still exhibits a lack of knowledge on the subject.
- Exhibitions entitled "From the pound to the euro" and "Euro coins genesis". These two exhibitions were inaugurated on 11 October 2006 at the premises of the Central Bank of Cyprus. Several thousand primary and secondary school pupils have visited the exhibitions with their teachers. The touring exhibition of the European Commission "Euro coins genesis" completed its presentation in Cyprus in January 2007 while visits of pupils and organized groups to the exhibition "From the pound to the euro" will continue until the end of 2007.
- Seminars for the financial sector. During 2006 the Central Bank of Cyprus held seminars on the basic aspects of euro adoption, which were attended by more than three thousand persons employed in the financial sector (banks, insurance companies, capital market institutions).
- Seminars for teachers. After the successful seminar of November 2006 on the introduction of the euro, which was attended by almost all secondary school teachers of economics and commerce, the Central Bank of Cyprus held seminars in March 2007 which were attended by more than 1,500 other primary and secondary school teachers.
- The organization of specialized seminars for the press with funding from and in close cooperation with the European Commission. Two such seminars were undertaken in Brussels and Frankfurt, one in Nicosia and others in Slovenia where its experiences were presented. It should be noted that these seminars were attended by Turkish Cypriot reporters with a view to enable them to inform the Turkish Cypriots.
- The activation of interested parties from the private sector through the creation of specialized bodies, such as Europartners and the Euroteam, which were set up on the initiative of the European Commission.

- The dissemination of information to the public, on the adoption of the euro, through the Cyprus International State Fair held between 10-20 May 2007 and Europe Day on 9 May 2007. These two events drew a significant number of visitors, in excess of 200,000.
- Close cooperation with Malta, which, like Cyprus intends to adopt the euro on 1 January 2008. In this respect a mission from Cyprus consisting of Government and Central Bank representatives visited Malta on 16 May 2007 to exchange experiences. Within the context of this visit particular emphasis was given to the matters of the operation of the Euro-Observatories Fair Pricing Code and the dual display of prices.
- Utilization of the successful experience of Slovenia in the adoption of the euro. In relation to this, a visit by a mission from the Cyprus Republic was undertaken on 6 June 2007, with the basic aim of drawing on the experiences, particularly those relating to the policy measures implemented in Slovenia to address effectively the concerns of the public regarding unjustifiable price increases.
- The operation of a "Toll Free Telephone Line 80002008 for the euro" on 11 June 2007. Up to now the response of the public is very encouraging.
- The upgrading of the national euro website (www.euro.cy), which is supported both by the Ministry of Finance and the Central Bank of Cyprus. It is estimated that the web page is visited daily by about 100 persons, which is considered satisfactory.

(b) Legislative Framework

The Committee dealing with the legislative framework prepared (end 2005 - beginning 2006) a complete action plan, with a specific time schedule, aiming at the timely formulation of the appropriate legislative framework, so that the required time for the preparation of the public and private sectors is made available.

Within this same context, a legislative drafting committee was set up, under the chairmanship of the Attorney Generals Office and the cooperation of the Ministry of Finance and the Central Bank of Cyprus, which prepared the enabling law for the adoption of the euro.[1] This Enabling Law is complementary to the relevant Community Regulations and constitutes the regulatory framework which will assist in the successful adoption of the euro.

[1] The Law Adopting the Euro of 2007 (Law N. 33(I)/2007).

The preparation of the Law for the adoption of the euro involved more than eighty services and bodies from the public and private sectors.

The final draft was submitted to the European Central Bank on 27 November 2006 for its opinion, in the context of the established practice of consultation with the European Central Bank. The final draft Law was the result of the incorporation of the amendments suggested by the European Central Bank into the third draft of the law.

Reference to the main contents of the Enabling Law

Law N. 33(I)/2007 which was enacted and came into force on 15 March 2007, regulates matters relating to the adoption of the euro and aims at facilitating the smooth transition from the Cyprus pound to the euro. The main provisions of the Law, among others, refer to:

- The dual display of prices, which is obligatory for suppliers and which is required for reasons of clarity and certainty for the public.
- The establishment of the Euro-Observatories which aim at protecting the consumers and the public, with respect to the introduction of the euro, by monitoring the legality of transactions, pointing the public to all sources of relevant information and investigating any possible infringement of the provisions of the Law.
- Other provisions are included which refer to the period of parallel circulation, the conversion and rounding up of prices, e.g. the share capital of companies, the change in interest rate denomination, etc.

Reference to the main provisions of the amending Law

The submission of the amending Law to the House of Representatives on 23 May 2007, which was enacted into law on 21 June 2007, aimed at the further improvement of the Enabling Law and its more effective and smoother application. Specifically, amongst other things, the power of the Euro-Observatories is expanded to enable a more effective operation and the publication of the names of the persons who are administratively fined for infringement of the Law is made obligatory.

(c) The Public Sector

For preparing the public sector a special Public Sector Committee was established which meets regularly on a monthly basis. All the Ministries prepared and are implementing

specific action plans for the adoption of the euro, which cover, amongst other things, the appropriate amendment of laws, regulations, Government directives, etc.
In addition the Municipalities and the Local Communities Association have become very active, as they play a leading role in the preparation and implementation of the Strategic Plan for the adoption of the euro by the municipalities and communities.

Each Ministry/Service has appointed a liaison officer, who is responsible for the organization of the work of their Ministry/Service relating to the adoption of the euro and they work in close cooperation with the competent Public Sector Committee.
In parallel, the Ministry of Finance prepared and sent to all the Ministries/Services a model table for monitoring the progress in their preparation for the adoption of the euro.

Computerization (Data Processing)

The adjustment of the data processing and software systems in the civil service for the adoption of the euro is being promoted by the competent Department of Data Processing Services of the Ministry of Finance. The basic principle in their approach to this matter is the maintenance of the historic data in Cyprus pounds (£), mainly for reasons of dealing with taxation declarations, retroactive calculations, salary statements, audit trail availability for payments in foreign currencies, as well as for possible requirements arising from legal or technical matters, which may arise as a result of the changeover from the pound to the euro. In all cases where the historical data is required for reasons of information or execution of transactions by the public sector, such historical data as well as the amounts which will result from their use in calculations shall be presented/converted into euro on the basis of the fixed exchange rate parity of the pound.
However, in the cases where the Ministries/Departments/ Services themselves consider that for the smooth operation of their services it is imperative that the conversion of the historic data be made into euro, then , where it is necessary for reasons of information the data can be presented in Cyprus pounds at its fixed exchange rate parity.

(a) Description of the Action Plan

(i) Cataloguing and Categorizing the Data Processing Systems

From the cataloguing and categorizing of the data processing systems it was found

that:

- 32 data processing systems were not affected by the introduction of the euro.
- 51 data processing systems are affected by the introduction of the euro and their adjustment can be undertaken by the department of data processing services.
- 28 data processing systems are affected by the introduction of the euro and their adjustment will be undertaken by outsourcing to the private sector.
- 7 data processing systems are affected by the introduction of the euro and they will need to be replaced by the development of new systems, given that they were developed on the basis of software and other tools which are no longer in use. For some systems the tendering procedures for the new systems have already been activated.

(ii) Analysis of the factors affecting the data processing systems

In looking at the matter of the substitution of the national currency by the euro, the following factors were found to influence the data processing systems:

- Changes in the legislation and/or regulations to harmonize them with the euro.
- Policy decisions regarding the processes which will be followed during the period prior to and after the introduction of the euro, which relates to the cases where the retroactivity of transactions will apply.
- Changes in forms/documents.
- The presentation of accounting and fiscal statements (printing and computer screens).
- Interaction with other data processing systems.

(iii) Meeting with Departments and Services utilizing data processing systems

During the period June to September 2005 the department of data processing services had contacts with the departments and services that possessed and utilized data processing systems, at which:

- They were informed in general terms about the matters regarding the introduction of the euro.
- The action plan of the department of data processing services was analysed for them.

- They were given a chance to analyse and discuss the factors which would affect their data processing systems.

(iv) The preparation of user requirements lists

At the meetings held by the department of data processing services with the other departments and services, the latter were asked to prepare user requirement lists of the changes which they required to be made to their data processing systems, so as to enable the adjustments to be made taking into consideration the factors which had been analysed and discussed. The categorization of the changes was completed in February 2006.

(v) Analysis of the changes required

Based on the lists of user requirements, prepared by the Ministries, departments and services, the department of data processing services proceeded with an analysis of the changes and the formulation of technical specifications, costings and time schedules for their implementation.

(vi) Requests for tenders, their evaluation, award and signature of contracts

For the systems whose changes required to be outsourced to the private sector the process begun in May of 2006 and for most was completed by December 2006. Priority was given to the taxation systems and the payments systems. For the remainder the process was completed by May 2007. For these systems the changes required were limited in number.

(vii) Implementation of the changes

The implementation of the changes begun in January 2007 and they will be completed in September 2007. Already the adjustment and testing of many systems has been completed.

(viii) The changeover of the systems

During the period June to August 2007 the department of data processing services will prepare detailed action plans for the changeover of the systems, which will include the following;

- The closing of accounts using the existing currency.
- The changeover, where this is considered necessary, of the monetary amounts in the data base into euro.

- Installing and testing the new or adjusted systems.

The changeover of the systems will be done in December 2007.

(b) The Business Sector

The committee dealing with the business sector took action with a view to:

- Encourage the business sector to proceed with the following:-

  * The distribution of various publications with useful information to help the preparation of enterprises.

  * The organization of educational seminars for professionals active in providing accounting and informatics services to enterprises, who by virtue of their professional relations with enterprises are able to play a multiplier role in the distribution of information to enterprises.

  * The strengthening of initiatives of the private sector (employers' federations, banks, professional associations) for informing and educating enterprises. It is worth noting, at this point, that the private sector organizations have been to a very satisfactory extent active in this respect and have contributed significantly to the work of the authorities of the Republic of Cyprus.

- Urge enterprises to prepare appropriately for the correct implementation of the dual display of prices and to participate in the adoption of the Fair Pricing Code, by which they commit themselves to avoid unjustified increases in their prices as a result of the adoption of the euro.
- Undertake meetings and consultations with particular sub groups of enterprises to identify and solve the special problems they face. Already, meetings have been undertaken with groups representing the tourism sector, the newspaper distribution agents, the petrol station operators, the political parties, etc.

(c) The Vulnerable Groups.

The communications strategy gives emphasis to informing the vulnerable groups, e.g. the blind, the deaf, etc. Particular attention is given to the retired and the housewives.

Within the context of the preparatory actions taken, meetings were held with the organizations representing the said groups, where their special needs were identified and a specific action programme was formulated to meet their needs effectively. More detailed analysis of the action programme is to be found in the following chapter.

Additionally, a PanCyprian one day meeting was organized for the blind and the deaf at which presentations were made by specialist advisors and the Minister of Finance.

(d) Informing Turkish Cypriots and Aliens

The strategic communications plan aimed at covering the information needs of the Turkish Cypriots, as well as those aliens who live and work in Cyprus. It also covers the information needs of the population living in the British Sovereign Bases.

Under the preparatory activities, information material in English and Turkish was distributed and a number of specifically targeted meetings, in English, were organized.

In addition, Turkish Cypriot reporters were invited to participate in an educational seminar which was organized by the authorities of the Republic of Cyprus, in collaboration with the European Commission, in Nicosia and Brussels/Frankfurt on 13 March 2007.

(e) The Central Bank of Cyprus

The Central Bank of Cyprus prepared and is executing an internal action plan regarding the technical matters relating to the adoption of the euro.

(f) Cooperation with the European Commission and the European Central Bank

The formulation of the strategic design for the changeover to the euro, is supported by the institutional bodies of the EU, particularly the European Commission and the European Central Bank.

With respect to the Strategic Communication Policy Plan, a partnership agreement was signed on 5 May 2006 between the Commissioner for Economic Matters, Mr. Almunia, on behalf of the European Commission and the Minister of Finance Mr. Sarris, on behalf of the Government of Cyprus. The agreement provides for the support and the extension of funding by the European Commission for certain specific activities. These activities include amongst others:

- The holding of two international seminars, with the participation of officials of the European Commission and the European Central Bank, with the object of transferring international experiences gained in this respect. It should be noted that at these seminars which were held in May and November 2006, Turkish Cypriot citizens of the Republic of Cyprus were both invited to and participated in the seminars.

- The undertaking of surveys to ascertain the level of preparedness of enterprises. The first such survey was completed in January 2007.
- The preparation by the European Commission and the European Central Bank, of printed information and other advertising material, which was distributed to enterprises and to the general public.
- The undertaking of seminars in Slovenia, Frankfurt and Brussels in April and June 2007 for reporters, to inform them of the experiences of other countries which had already adopted the euro.
- The presentation of the European Commission's touring exhibition "euro coins genesis" from 12 October 2006 to 19 January 2007, at the premises of the Central Bank of Cyprus.

The cooperation between the authorities of the Republic of Cyprus and the European Commission and European Central Bank will continue and intensify in the coming months with the actions noted in the following chapter.

The total funding from the European Commission in 2006 amounted to 287,000 euro.

(g) The Operation of the National Web Page

The distribution of information material to the general public is also supplied through the National Web Page for the euro, which was created jointly by the Ministry of Finance and the Central Bank of Cyprus, www.euro.cy .

8. COMMUNICATIONS POLICY PLAN

With the object of formulating and implementing the Communications Policy Plan, a Joint Communications Committee was established, which is chaired by the Director of the Ministry of Finance responsible for matters relating to the euro and consists of the Officers from the Communications Committees of the Ministry of Finance, the Central Bank of Cyprus, representatives of the Public Information Office, the Ministry of Commerce, Industry and Tourism, as well as the Head of Mission of the European Commission in Cyprus. The Committee constitutes the "point of contact" with the competent directorate of the European Commission for communication matters.

Matters of strategic concern and importance for the Communications Strategy:

Considering the facts, one draws the conclusion that the average Cypriot today:

- Has already experienced a number of "metric" changes over the last 25 years.
- Is already familiar with the euro.
- Does not easily change his habits.
- Is interested in the euro, but is afraid of its adoption.
- Is influenced by what happened in Greece, and his impressions regarding the adoption of the euro in Greece are negatively tainted, mainly in respect to the matter of prices.

The basic aims of the Strategic Communication Policy Plan are the following:

- To gain the confidence of the public in the euro and its support for entry into the euro area.
- To give information on the processes of entry into the euro area and the preconditions for the successful adjustment of the Cyprus economy to the euro area.
- To inform and promote consultation about the benefits and the challenges for the Cyprus economy (growth, employment, inflation, public finances, macroeconomic policy).
- To inform the general public of the impact on their daily life.
- To face effectively the possibility of unjustified increases in prices during the changeover to the euro.
- To achieve the timely preparation of the public sector, the business sector, including the retail sector, as well as the financial sector.
- To identify and effectively deal with the special needs of the vulnerable groups (low income groups, uneducated persons, persons with impairments, retirees), the Turkish Cypriots and aliens.
- To familiarize the public with the euro (bank notes and coins).
- To explain the practical aspects of the changeover to the euro.

To achieve the above aims the following measures were adopted:

- A multi – media campaign, including television and printed matter.
- The preparation of informational and advertising material for enterprises and the public, including CD ROMs.
- The use of press conferences, meetings, lectures, etc.

- The operation of the national web page, as from 31 May 2006, dealing solely with the adoption of the euro in Cyprus, which gives all the necessary information to the public about the euro (www.euro.cy).
- Other activities (measures), such as, establishing the Euro-Observatories, distributing currency converters, setting up a toll free telephone line.

The communications strategy will utilize the Europartners (employer and trade union organizations, professional associations, consumer associations, the financial sector, local authorities) and the multipliers (the media, politicians, academics, teachers and pupils).

The communications strategy is based on the following:

- On the timeliness of the information it gives.
- On the simplicity and consistency of such information.
- On the ease of accessibility to the information.
- On the repetition of the messages sent out.
- On the dissemination of the feeling of confidence and security about the euro.
- On the intensification of the information campaign during the last months prior to the introduction of the euro.

The communications strategy has been formulated according to the characteristics and realities of the Cyprus economy. It will have a Cypriot character, but at the same time a parallel European one.

The campaign begun in phases and will be intensified in the second half of 2007 and at the beginning of 2008. During the first phases of the communication campaign, emphasis was placed on matters of general interest. Subsequently, towards the end of the campaign, the emphasis will be shifted to specific and practical matters.

The communications strategy will help the Cypriot citizens to feel stronger by ensuring the dissemination of the necessary information, building up his feeling of confidence and transmitting the principle that the successful adoption of the euro depends on him.

The fundamental messages of the communications campaign are the following:

- One currency – many opportunities.
- The euro becomes our currency also – a common European future.
- We are changing our currency, not our way of life.
- A successful changeover of the pound to euro is expected.

- Adoption of the euro strengthens the position and prospects of our country in Europe.
- Appropriate preparation is needed.
- The competent authorities are preparing in a timely manner.
- It is up to each individual to prepare for the change.

The logo used for the campaign is a heart with the symbol of the euro, because this expresses, positively, simply and directly, warm and human feelings. The slogan of the campaign is *"The euro: It's in your hands!"* The euro states that it is our new currency as from 1 January 2008. The expression "It's in your hands!" is based on the fact that the euro will indeed be in "Your" hands, but in order to be in "Your" hand, the successful adoption of the euro depends on "You".

The communication campaign has been divided into four phases:

Strategic action plan:
4 Phases

Introductory Phase. 2005 – 2007 *Preparation, contacts, issue of directions and direct information to vulnerable groups and public, articles and interviews.	**Intensification of campaign** **Phase 1.** March to May 2007. **General public:** *Information to create positive interest. **Europartners:** *Obtaining their commitment to spread messages. **Business sector:** * Encourage timely preparation.	**Phase 2.** June 2007 to locking of the exchange rate. **General public:** * Information on important dates. * Explanation of locking of the exchange rate. **Europartners /business sector:** * Encourage fair and correct behaviour and dual display of prices.	**Phase 3.** Locking of exchange rate – 1 January 2008 Euro day. **General public:** * Information on the exchange rate. * Creation of expectations and presentation of the benefits. * Explanation of process of change. **Europartners /business sector:** * Encourage fair and correct behaviour and dual display of prices. * Explanation of process of change. **Vulnerable Groups** **Exchange rate adoption of and date of the euro**	**Phase 4.** 1 January 2008 Euro day to mid 2008. **General public:** * Information on date of ending of parallel circulation. * Encourage the change from the pound to the euro. * Urging for care and checking of transactions. **Europartners /business sector:** * Encourage fair and correct behaviour – transactions.

9. SURVEYS OF PUBLIC OPINION

Euro-barometer Survey May 2007

The recent Euro-barometer survey on public opinion in Cyprus, with regard to the introduction of the euro in the new member states of the European Union (European Commission May 2007), shows more positive results relative to previous surveys.

More specifically, the results of the said survey indicate a relative increase in the acceptance of the euro in Cyprus.

- The proportion of respondents against the introduction of the euro has declined from 59% in September 2006, to 53% in April 2007.
- In parallel, 40% of Cypriots felt more comfortable with the substitution of the Cyprus pound by the euro in April 2007, compared to 32% in September 2006.
- With respect to the information on the euro, in April 2007 53% stated that they were very well informed about the euro, whereas in September 2006 only 39% made this statement, a fact which shows a significant increase in awareness, amounting to 14% points.
- With respect to the impact of the introduction of the euro, in April 2007, 38% declared that it would have positive effects at the national level (compared with 29% in September 2006), 44% declared that the euro would impact positively people at the personal level (compared to 33% in September 2006) and 43% believes that the introduction of the euro will strengthen and restore the public finances of Cyprus (compared to 35% last year).
- As regards to the familiarization and use of the euro, 84% responded that they were familiar with the euro bank notes and 72% that they have used such euro bank notes.

  In spite of this, public opinion still reflects a strong concern about the possibility of unjustified price increases as a result of the introduction of the euro, given that 83% declared this as a concern in April 2007.
- In April 2007, on the question to what extent the introduction of the euro would assure the stability of prices, 47% responded YES and 34% NO.

The opinion surveys constitute a very valuable tool for the authorities and assist towards the appropriate adjustment of the communications strategy.

10. PRIORITIES OVER THE FOLLOWING MONTHS

The implementation of the Strategic Plan for the changeover from the pound to the euro has entered its intensified phase.

Having in mind the strategic aims which have been set and the course of the development of public opinion in Cyprus, the basic priorities in the following months are facing, in a convincing manner, the concerns of the public of unjustified price increases during the changeover to euro. With respect to this matter the main policy measures consist of (i) the establishment and operation of the Euro-Observatories, (ii) the promotion of the Fair Pricing Code, (iii) the implementation of the dual display of prices and (iv) the systematic monitoring and the creation of conditions of transparency as regards price determination.

Other priorities refer to:

- promoting the timely preparation of the small enterprises which, according to the various opinion surveys, require to speed up their preparedness
- informing adequately the population living in rural areas, the retirees, as well as the vulnerable groups
- informing adequately the Turkish Cypriots

10.1 INFORMATION CAMPAIGN

Within the context of the general aims and priorities which have been set, the most crucial activities which have been programmed for the next months, under the communication strategy, are the following:

- Implementation of the 2nd, 3rd and 4th phases of the campaign through the medium of television. In this framework, emphasis will be shifted from the dissemination of information of a general character, to information of a more practical nature (the conversion rate, the design of the banknotes and coins, dehoarding, etc.), as well as the advancement of the various initiatives, which aim at confronting convincingly the concerns of the public about price increases (dual price display, Fair Pricing Code, etc.).
- Continuation of the distribution of printed material for enterprises and the general public. As in the case of the television campaign, the priorities will centre on the matter of prices and information of a practical nature.

- Continuation of the lectures and educational seminars, concentrating on the small enterprises and the population living in rural areas. In this respect some of the activities programmed are as follows:

  * Lecture by the previous Governor of the Slovenian Central Bank (12 July 2007), outlining the successful adoption of the euro in Slovenia.

  * Lectures for special categories of goods and services with emphasis on those categories which, on the basis of the experiences of other countries that have already adopted the euro, have exhibited a trend for excessive price increases during the transition period of the changeover to the euro (e.g. coffee shops, restaurants, hairdressers, etc.).

  * Intensification of the lectures in the districts, in cooperation with local authorities, utilizing the Euro Teams (speakers from the private sector).

  * Organization of a special seminar, in collaboration with the University of Cyprus, on the adoption of the euro and its impact on the Cyprus economy, at which officials of the European Commission and the European Central Bank, as well as other experts on the euro, will attend. This seminar is programmed for next November.

  * The placing of advertisement signs and banners regarding the euro, on and around the Ministry of Finance and the Central Bank of Cyprus.
- The celebration of the final approval of the adoption of the euro and the determination of the conversion rate between the Cyprus pound and the euro – 10 July 2007 in Brussels and Cyprus.
- Organizing monthly meetings of the Minister and Officers of the Ministry of Finance with reporters, for the dissemination of information to them on a systematic basis.
- Utilization of the infrastructure of the Cyprus Telecommunications Authority to disseminate information material to the general public. A Memorandum of Cooperation between the Ministry of Finance and the Cyprus Telecommunications Authority was signed – 26 March 2007.
- Placing web banners on highly visited web sites.
- Encouraging the use of the toll free telephone line for the euro, which has, already been in operation since 11 June 2007.

- Undertaking a Pan-Cyprian competition on the subject of the euro, for secondary education pupils.

  The informing of secondary education pupils of the benefits of the introduction of the euro, the correct use of the euro and its role in our lives, is encompassed within the aims of the information campaign for the public, with respect to the euro in Cyprus. Towards this aim, the Ministry of Finance and the Ministry of Education and Culture, decided to conduct a Pan-Cyprian competition on the euro, open to all pupils of secondary education level, which will be funded by the European Commission.

  The competition will involve the creation of a calendar (be it pocket sized, or for hanging on the wall or an electronic one) for 2008. The best design for each type of calendar will be issued in copies and be given, not only to all the secondary schools, but also to the general public. The object of the competition would be that, through the work undertaken for the creation of the calendar, the knowledge of the pupils would be enhanced, both with regard to the history of the Economic and Monetary Union (EMU) and of the benefits and changes that the euro will bring to our lives. At the same time, the pupils will obtain other benefits, such as organizational and planning skills, group cooperation and work, responsibility, etc.

  The competition will be completed prior to the end of 2007, so that the calendars can be published and disseminated to the public at the beginning of 2008. The time schedule of the competition is as follows:

Activity	**Time Period**
Appointment of General Coordinator	June 2007
Preparation of Guidelines	July – August 2007
Distribution of Circulars and Applications to Schools	1 - 10 September 2007
Submission of Applications	Up to 28 September 2007
Creation of Calendars by Competitors	October - 5 November 2007
Evaluation of the Groups' Work	5 - 25 November 2007
Awards Ceremony for the Best Groups	End November – Beginning December 2007
Issue of Copies of Calendars	December 2007
Dissemination of Calendars	From January 2008

- Making and setting up of portable stands for the euro, which will be positioned at places the public tends to congregate – September 2007.
- Organization of "Euro exhibition" in Limassol – 26 October to 5 November 2007.
- Distribution of information and other promotional material by the Euro Bus. The Euro Bus is programmed to circulate in October and November and will mainly cover the districts of Cyprus and the rural areas which, according to various surveys, are not as well informed.
- Dissemination of converters to each household – November 2007.
- Celebrations for the adoption of the euro – 18 January 2008.
- Evaluation of the course of the communications campaign at regular periods of time.

Further within the context of its specialized responsibilities and specifically as a member of the European System of Central Banks, the Central Bank of Cyprus deals with all matters relating to the communications campaign which relate to the introduction of euro bank notes and coins and the withdrawal of Cyprus pounds.

The communications campaign of the Central Bank of Cyprus was designed in cooperation with the European Central Bank. At the beginning of July 2007 a Memorandum of Cooperation was signed between the Central Bank of Cyprus and the European Central Bank which, amongst other things, covers the following:

- The production of informative material developed and produced by the European Central Bank and distributed by the Central Bank of Cyprus.
- Campaign for the dehoarding of accumulated Cypriot coins.
- The organization of seminars for financial editors in Cyprus.
- Training of tellers on the security features of the euro banknotes and coins.

More information is given in the "Information Campaign Plan of the Central Bank of Cyprus for the adoption of the euro", which is to be found on the Central Bank of Cyprus web page.

10.2 LEGAL FRAMEWORK

(a) Community Legal Framework

Community Regulations

In order to ensure the successful adoption of the euro, the EU has passed regulations which are automatically applicable in the member states participating in the euro area. These regulations regulate the basic aspects of the introduction of the euro.

A description of the main regulations is given below.

The continuity of contracts and the conversion of amounts therein.

Regulation (EC) 1103/97 (as amended by Regulation (EC) 2595/2000) includes important provisions for the continuation of contracts and rules regarding the conversion of amounts from the national currency to the euro. According to this Regulation, existing contracts (pacts, agreements) whose amounts are expressed in Cyprus pounds, shall continue to be valid as regards their conditions and the payment or imputation of such amounts expressed in Cyprus pounds shall, however, be made in and calculated in euro and rounded up to the nearest cent, based on the fixed exchange rate parity.

The euro as legal tender – banknotes and coins.

Regulation (EC) 974/98 (as amended by Regulations (EC) 2596/2000 and 2169/2005) provides for the introduction of euro banknotes and coins. It delineates the euro as the currency of the "participating member states", meaning the states participating in the euro area, and determines that the euro banknotes and coins are the only legal tender in these states, except for the period during which parallel circulation of the euro and the state's national currency is permitted. Regulation (EC)974/98 also provides that any references to the national currency in existing national legislation, administrative decisions, court decisions, agreements or payment systems (excluding cash systems) shall be considered to be references to the euro, in accordance to the conversion rate and the rules for rounding provided for by Regulation(EC) 1103/97.

At present, Regulation (EC) 974/98 specifies the states participating in the euro area as being the following twelve countries: Austria, Belgium, France, Germany, Greece, Ireland, Spain, Italy, Luxemburg, The Netherlands, Portugal and Finland. It is expected that the EU Council will amend Regulation (EC) 974/98, at the appropriate time, so as to

include Cyprus, and presumably Malta to adopt the euro at the same time, in the above list of the countries participating in the euro area.

Regulation (EC) 2866/98 (as amended by Regulation1 (EC) 478/2000 on the adoption of the euro by Greece and Regulation (EC) 1086/2006 on its adoption by Slovenia) specifies the exchange rate parity between the euro and the currency of each of the member states adopting the euro.

Regulation (EC) 975/98 (as amended by Regulation (EC) 423/1999) determines the nominal value and the technical specifications of the euro coins which are intended for circulation.

(b) National Legislation

Legislative amendments to harmonize existing national legislation with Community euro area legislation.

Certain laws of the Republic of Cyprus contained provisions which were considered not to be in line with, or were indeed contrary to, the provisions of EU legislation applicable to the euro area, thus they required amendment or abrogation. The main legislation which required significant amendment is the Central Bank of Cyprus Laws of 2002 and 2003. The Central Bank of Cyprus prepared an amending bill for the full harmonization of the Central Bank legislation with that applicable for the euro area, which was voted into Law on 15 March 2007.[2]

New legislation regarding the changeover from the pound to the euro – Adjustment of monetary amounts.

In many laws of the Republic of Cyprus there are provisions for amounts expressed in Cyprus pounds such as monetary fines, administrative fines, monetary limits, and other monetary reference amounts, as well as references to the meaning of the "Cypriot currency". With the automatic application to Cyprus of the previously mentioned Community Regulations, the said amounts are automatically converted into euro, in accordance with the conversion rate which shall be determined. For example if the conversion rate is set at 1 euro = £0,585274, the amount of £10.000, which is foreseen in certain laws as the highest fine, will be converted to 17.086,01 euro.

More specifically, the new law provides, amongst other things, for the following matters:

[2] The Central Bank of Cyprus (Amending) Law of 2007 [N.34(I)/2007], EU pg.357.

- The conversion of prices and monetary amounts into euro and their rounding
- The dual display of prices
- Interest rates
- The adjustment of administrative fines/ monetary penalties, other liens, etc
- The exchanging of bank notes and coins from pounds to euro
- The conversion of other balances in bank and other accounts
- The treatment of post-dated cheques
- The establishment of Euro-Observatories
- The conversion to euro of company share capital
- The conversion of fees and charges

Process of preparation of the bill with respect to the Enabling Law for the introduction of the euro.

- The preparation of a bill with general provisions (umbrella provisions) with a view to covering as much as possible that which required legislative regulation.
- The inclusion in the bill of the amendments suggested by the Ministries, Departments and Organizations.
- The inclusion in the bill of the suggestions made by the interested parties of the private sector.
- The submission of the revised draft bill to the European Central Bank and the European Commission for consultation purposes.
- Approval of the draft bill by the Ministerial Council – 7 February 2007.
- Submission of the draft bill to the House of Representatives – 8 February 2007.
- Discussion of the draft bill by the House of Representatives – 22 February and 8 March 2007.
- Voting into effect the Enabling Law for the introduction of the euro - 15 March 2007.
- Preparation of amending bill, ministerial administrative regulatory orders, official notices, etc.

The legal framework regulating the adoption of the euro, was made known to the general public, by way of seminars, the distribution of printed material, articles in newspapers, etc., with particular emphasis being given to enterprises and to certain professional

organizations, such as the Accountants Associations, the Association of Informatics Companies and the Cyprus Informatics Company, etc.

Future priorities

The main work, with respect to the putting in place of the legislative framework required has been completed. During the following months the process of informing people of the legislative framework will continue and be intensified, with emphasis being given to the matter of the dual display of prices and the operation of the Euro-Observatories.

10.3 THE PUBLIC SECTOR

The preparation of the public sector is proceeding satisfactorily, in accordance with the strategic plans drawn up by the Ministries.

The priorities over the next months relate to informing of the public on practical matters, such as taxation matters, pensions, allowances, fees imposed by the public sector for services rendered, changes to the income limit preconditions set for programmes and schemes offered by the public sector, etc.

More specifically the following actions are envisaged:

- Consultations between the Ministries, the Ministry of Finance in its capacity as coordinator and the private firm Mediacom – June 2007
- Finalization of the information programme for each Ministry – July and August 2007
- Implementation of the information programme for each Ministry – September 2007 to February 2008
- The work on the adjustment of the data processing systems in the civil service is being implemented in accordance with the action plan shown in the following table:

A/A	Work Description	Completion Date	Comments
1.	Preparation of action plan	31/05/2005	Completed
2.	Cataloguing and categorizing the data processing systems.	15/06/2005	Completed
3.	Analysis of factors affecting the data processing systems.	30/06/2005	Completed
4.	Contacts with departments and services to discuss factors effecting their data processing systems	31/09/2005	Completed
5.	Listing of user requirements	30/03/2006	Completed
6.	• Analysis of changes	30/04/2006	Completed

	• Preparation of specifications • Costing of changes • Preparation of budgets for changes • Preparation of analytical time schedules.		
7.	Preparation of tender documents and calls for tenders.	31/07/2006	Completed
8.	Evaluation, awarding and contract signatures.	31/12/2006	Completed
9.	Implementation of changes and testing of systems.	30/09/2007	For many systems completed. For remainder proceeding according to time schedule.
10.	Changeover to the new or adjusted systems.	31/12/2007	

Until the adoption of the euro, priority will be given to the following:

- The completion of the implementation of the changes
- The testing of the systems
- Preparation of detailed action plans for change over to new or adjusted systems, to be done end 2007
- Implementation of action plans for change over to new or adjusted systems

10.4 <u>BUSINESS SECTOR</u>

The successful adoption of the euro presupposes the timely and complete preparedness of business units. Towards this objective, the competent authorities supply the required guidance and all possible assistance.

Indicatively, the business sector should include in its programming the following adjustments and policies:

- The establishment of the necessary structures for the programming and implementation of the action plan for adoption of the euro. In this context it is suggested that the responsibility for the preparation and implementation of the action plan be given to a senior officer of the enterprise.
- The carrying out of a study to analyse the impact of the adoption of the euro on the enterprise
- Identification of the necessary operational changes that would be entailed

- Adjustment of the computer programmes of the accounting department, the cash machines and generally all computer programme systems of the enterprise
- Adjustment of price lists, taking into account the period of dual display of prices, which will apply a few months prior and a few months after the adoption of the euro
- Inform customers of changes
- Educate staff with regard to the changes

The competent authorities contribute actively to the preparation of the manufacturing and commercial enterprises, particularly through the preparation and publication of manuals for the guidance of enterprises, which describes the various matters which an enterprise needs to take into consideration, if it is to be ready to take advantage of the prospects and face, successfully, the challenges which will be created by the foreseeable introduction of the euro on 1 January 2008. Already, relevant issues of manuals have been circulated, which offer guidance on the preparation of enterprises for the adoption of the euro in Cyprus.

The course of the preparation of the business sector is being monitored on a systematic basis, in close cooperation with the employers' federations. In addition, special surveys are carried out addressed to the entrepreneurs and funded by the European Commission. The next survey is programmed for September 2007.

Commerce

The sector of retail and wholesale commerce, which is made up mainly of small family enterprises, faces significant challenges at the stage of preparation for the adoption of the euro.

The competent authorities support actively the attempts of the commercial enterprises to adjust to the conditions that will be created by the adoption of the euro, thus ensuring at the same time, the effective protection of the consumer.

In this context the establishment of appropriate mechanisms was pursued, as was the taking of appropriate measures to face effectively the possibility of unjustifiable price increases, during the changeover to the euro. This matter is of crucial importance, as is verified by the various opinion surveys and constitutes a fundamental priority of the National Changeover Plan for the adoption of the euro.

The policy framework for assuring the stability of prices during the changeover from Cyprus pounds to euro is described in great detail in the chapter on consumers.

Tourism enterprises

The adoption of the euro is expected to benefit substantially the tourism sector, given that a significant part of the tourists visiting Cyprus are drawn from the member states of the euro area. After the adoption of the euro, tourists coming from the countries of the euro area will not have to be burdened with the cost of exchanging currencies.

At the same time, the tourism industry is expected to face stronger competition, due to the greater transparency of prices affecting potential tourists. As a result, the matter of competitiveness will become an even more important factor, with respect to the further development of this vital sector for Cyprus.

10.5 CONSUMERS – POLICY FRAMEWORK FOR STABILITY OF PRICES

The adoption of the euro is expected to bring significant benefits for the consumers, which are expected to counterbalance the transitional difficulties that will arise from the necessary adjustments to a new currency.

The various opinion surveys show that a significant proportion of the population living in Cyprus, expects that the foreseeable entry of Cyprus to the euro area on 1 January 2008, will lead to excessive price increases, with the result that inflationary tendencies will be exacerbated.

Taking seriously into account these concerns of the public, the competent authorities of the Republic of Cyprus formulated a complete policy framework, which is being implemented and which aims at stabilizing prices and the limiting, to the greatest possible extent, possible unjustified increases in prices during the changeover from the pound to the euro.

It should be noted that, in contrast to the opinion held in Cyprus, the euro area is an area of low inflation and of price stability, with an average yearly increase in prices of just 2%.

In view of this, the concerns of the Cypriot public are not justified.

The experience of the member countries in the euro area has shown that the price increases which did result from their rounding was limited. In the case of certain products

of wide consumption, with a low purchasing value, their selling prices did increase. Despite the fact that the impact of the increase on inflation was on average just 0,3 percentage points, these isolated increases in certain products created the mistaken impression, to the general public, of the existence of unfair profiteering in the market and high inflationary pressures during the transition to the euro.

The authorities in the Republic of Cyprus believe that they are in a position to face the specific problem through the appropriate communications strategy and at the same time, to counter effectively attempts at profiteering by the market during the changeover period to the euro.

More specifically the policy framework includes the following measures:

- Voluntary Fair Pricing Code.

  The Fair Pricing Code aims at encouraging the entrepreneurial unit to commit themselves not to implement unjustified increases in their prices during the changeover of these prices from Cyprus pounds to euro. In addition, the enterprises, which voluntarily participate in implementing the Code, will commit themselves to increased transparency in the pricing of their products. Also, they will commit themselves to appoint an officer of the enterprise to be responsible for giving information to the public and for customer services assistance in respect of, matters related to the adoption of the euro.

  The participants in the implementation of the Code will have the right to use the Logo, which will inform consumers that the enterprise agrees with and is applying the Code provisions.

  Given that the participation in applying the Code is voluntary, it is expected that the participants will comply fully with the provisions of the Code. In the case where the competent authorities judge that a participant does not comply with the Code provisions, they will inform the participant accordingly. Where the participant does not take corrective measures, as proposed by the authorities, then the authorities may withdraw the right of the participant to use the logo and publish their decision in any manner they consider appropriate.

  The Ministry of Finance, so as to inform consumers, will publish a list of the enterprises that will adopt the above Code. Additionally, with the setting up of

appropriate monitoring mechanisms (Euro-Observatories), the conformity of the enterprises to the provisions of the Code to which they have voluntary committed themselves, will be assured.

The Code will apply from 10 July 2007 to 10 July 2008.

Preliminary indications, regarding the adoption of the Code are encouraging. Already two large groups of companies have declared publicly their intention to adopt the Code, committing, themselves, to reducing the prices of the goods and services they offer. The employer's federations have also declared that they will encourage their members to embrace the Government's initiative and to adopt the Code.

- The obligatory, by law, dual display of prices in Cyprus pounds and in euro.

  The obligatory dual display of prices in Cyprus pounds and in euro will be applied for a substantial period before and after the physical adoption of the euro. The objective will be to familiarize the consumers with the prices in euro.

  The dual display of prices will begin on 1 September 2007 and continue until 30 September 2008.

- Establishment of Euro-Observatories.

  The Government has established the "institution" of Euro-Observatories, which will deal with the complaints from the public, undertake sample audits/checks to ensure the correct application of the provisions of the Enabling Law, for the adoption of the euro and will propose to the Minister of Finance the imposition of penalties in cases where there is infringement of the Law.

  It is understood that in cases where the above proposal of the Euro-Observatory applies to a bank or a cooperative credit institution, then that proposal shall be addressed to the Governor of the Central Bank of Cyprus, or to the Director of the Cooperative Societies Supervision and Development Service.

- Monitoring of prices.

  The Ministry of Finance along with the Statistical Services and in cooperation with the Pan-Cyprian Consumers Association will proceed with the systematic monitoring and publication of price developments, particularly as regards the so called sensitive products, in order to present information and transparency on prices to the public, during the period of the changeover to the euro.

The monitoring policy for prices is based on three axes:

* The frequent publication of indices of changes in prices, by the Statistic Services and regular monitoring of certain chosen sensitive product/categories, which are considered to be "high risk" as candidates for unjustified price increases.

* The monitoring of certain sensitive products[3] of enterprises and shops which will be participants in the application of the Fair Pricing Code. The monitoring will be undertaken by the Pan-Cyprian Consumers Association. The prices and the variation of the prices will be published by the Pan-Cyprian Consumers Association on web pages, in newspapers, periodicals or other printed matter of the Association.

* The monitoring of the same list of certain sensitive products as noted above, of enterprises and shops which will not be participants in the application of the Fair Pricing Code. The monitoring will be undertaken by the Pan-Cyprian Consumers Association.

10.6 VULNERABLE GROUPS OF THE POPULATION

Within the context of the strategy to inform the public about the introduction of the euro, the Government gives particular emphasis on taking into consideration the needs of and informing appropriately the vulnerable groups of the population (the blind, deaf, disabled).

The Government's objective is the full, valid and timely provision of information to the vulnerable groups, so that they can properly prepare themselves to handle the introduction of the euro into Cyprus. With this in mind, the Government has undertaken meetings with representatives of vulnerable groups, in order to identify methods of support and assistance of such groups, according to each groups needs.

The above meetings resulted in the formulation and implementation of the following measures:

- The sponsoring and organization of functions on the euro, for the vulnerable groups, in all the districts of Cyprus. Already the first such function was organized, with the

[3] The specific products to be monitored by the consumers association are different from those that are referred to in the above first axis.

assistance of the Pan-Cyprian Association for the Blind and Deaf, with great success in Nicosia.

- Translation into brail of information material on the euro, as well as preparing voice recorded information material on the euro on cassettes, CDs, DAISY or MP3 forms and its free dissemination to the blind.
- The covering of the cost for the purchase of a special converter of Cyprus pounds to euro and vice versa, with a Greek language voice function, offering in this way practical assistance to the blind to enable them to familiarize themselves with the euro exchange rate.
- Utilization of the television medium to its greatest extent, through the presentation of programmes in sign language for the deaf.

10.7 INFORMING THE TURKISH CYPRIOTS

The information campaign for the Turkish Cypriots will be intensified in the following months. The specific actions programmed are the following:

- Preparation of a two page leaflet in Turkish
- Translation of certain basic publications on the changeover to the euro in Turkish
- Placement of articles in Turkish on the web page for the euro
- Inviting Turkish Cypriot reporters to the monthly information meetings with the Minister of Finance
- Participation in the state television programmes (CyBC) in Turkish
- Preparation of an information guide for Turkish Cypriots, which will be distributed at the Green Line crossover points

10.8. FINANCIAL SECTOR

10.8.1. Cash Changeover Plan

The Central Bank of Cyprus (CBC), having the exclusive responsibility and accountability for the introduction of the euro in physical form and for the withdrawal of the Cyprus pound from circulation, has published the "Cash Changeover Plan". The plan presents the decisions and the action plans adopted by the CBC for the acquisition of euro

banknotes and coins, their distribution into the economy, the exchange of cash and the withdrawal of the Cyprus pound.

The detailed plan is published as a separate document (www.centralbank.gov.cy , www.euro.cy) and is summarised as follows:

Acquisition of euro banknotes and coins

The CBC will acquire adequate quantities of euro banknotes from the Eurosystem, through the Bank of Greece. For the required quantities of coins, the CBC will mint Cypriot euro coins in co-operation with the Finnish Mint.

Distribution of euro banknotes and coins

The CBC will frontload all banks with euro banknotes and coins before the introduction of the euro in Cyprus, and, in turn, banks will sub-frontload businesses. The objective is to facilitate the settlement of transactions in euro, from the first day, especially in the retail sector. At the same time, banks will convert their Automated Teller Machines so that the public can be provided with euro banknotes as of the first hours of 2008.

Exchange of Cyprus pounds

As specified in the Euro Adoption Law (N. 33(I)/2007), banks will exchange Cyprus pounds, without any charges, starting from 1 January 2008 for a period of 6 months, with defined limits per transaction. The CBC will continue to exchange, without any charges or limits, banknotes for 10 years and coins for 2 years after the introduction of the euro.

Withdrawal of the Cyprus pound

Banks will deposit Cyprus pound banknotes and coins that will accumulate at their cash tills to the CBC for authenticity checking and destruction, following existing procedures.

Security measures

The CBC, adhering to European Central Bank regulations and in co-operation with the competent authorities of the Republic, will assume all necessary measures in order to deter criminal acts. At the same time, the CBC will organise extensive training on the security features of the euro for persons who professionally handle cash.

Banking services during the changeover period 31/12/2007 to 2/1/2008

The following services will be provided by banks during the changeover period:

- On 31 December 2007, bank branches will only accept deposits from enterprises and the public. Recorded transactions with value date 31/12/2007 will be processed without any expenses or loss of interest for the customers.
- Banks' Automated Teller Machines will provide Cyprus pounds to the public until 17:00 on 31 December 2007. During the first hour of 1 January 2008, at least 70% of each bank's ATMs will dispense only euro banknotes of €10 and €20 denominations. The remaining 30% of ATMs will be made operational, providing only euro, the latest by noon of 1 January 2008.
- On 1/1/2008, an established bank holiday, bank branches will open in each District only for the exchange of Cyprus pounds into euro.
- Banks will resume normal banking operations on 2/1/2008.

10.8.2. Central Bank of Cyprus

(a) The role of the Central Bank of Cyprus

The CBC, being the monetary authority of the country, has key role in the changeover to the euro. In the context of its legally assigned functions, the CBC's preparatory work for the smooth introduction of the euro on 1 January 2008 focuses on the following areas:

- Smooth introduction of euro banknotes and coins and withdrawal of the Cyprus pound (see chapter 10.8.1)
- Contribution to the lasting fulfilment of the economic convergence criteria, through prudent monetary and exchange rate policies
- Adjustment of the CBC's legal framework. Legal convergence, which is an essential prerequisite for euro adoption, was achieved with the enactment of the Central Bank of Cyprus (Amending) Law on 15 March 2007.
- Timely preparation of the financial sector, particularly the banks, for the changeover to euro

- Timely dissemination of information about the denominations, visual appearance and security features of euro banknotes and coins, as well as the modalities of the cash changeover
- Contribution to the broader information campaign
- Adjustment of the CBC's activities in accordance with the euro area rules, particularly in the areas of monetary policy, payment and settlement systems, and statistics.

(b) Technical preparation for euro adoption

(i) Payment and settlement systems

Large value payment systems – TARGET2 (Trans-European Automated Real-Time Gross Settlement Express Transfer system)

Since 1999 the Eurosystem (i.e. the European Central Bank and the central banks of the euro area countries) has been using TARGET for the settlement of operations implementing the single monetary policy and other large-value euro payments. TARGET is expected to be replaced by the new improved system TARGET2. Cyprus has been included in the first wave of countries to be connected to TARGET2 by 19 November 2007 and will, therefore, be a participant in this system at the time of euro adoption (1 January 2008). Henceforth, transactions currently carried out and settled through the CBC's Large Value Credit Transfer System will be handled and settled through TARGET2. The testing for the migration to TARGET2 has entered its final phase since May 2007. The CBC has also made contingency plans for a fallback solution in case TARGET2 is not ready when Cyprus adopts the euro. Specifically, since 4 December 2006 the CBC and 15 commercial banks operating in Cyprus have been connected to the current TARGET system through the national real-time payments system of Germany, known as RTGSplus.

Cyprus Clearing House – Adjustment of the cheque clearing system

As from the euro adoption date (1 January 2008) cheques will no longer be issued in Cyprus pounds, but in euro, and the cheque clearing system will be adjusted accordingly. On 9 February 2007 the Committee of the Cyprus Clearing House announced that any

cheques in pounds issued before the euro adoption date (1 January 2008) and presented after the euro adoption date will be payable in the corresponding euro amount for a period up to six months after the date they become payable, in line with normal banking practices. For example, a cheque in pounds dated 20 December 2007 may be paid until 19 June 2008, in euro.

In view of these changes, the Cyprus Clearing House has selected a technical solution for handling cheques both in euro (dated on or after 1 January 2008) and in pounds (dated before 1 January 2008), for a six-month period.

(ii) <u>Monetary policy operations</u>

Following euro adoption, the CBC will no longer design an autonomous monetary policy, but will participate in the design and implementation of the single monetary policy of the European Central Bank. More specifically, the Governor of the CBC will participate in the Governing Council of the European Central Bank, which makes monetary policy decisions (e.g. setting official interest rates). In parallel, the CBC will participate in the implementation of the single monetary policy, mainly by conducting open market operations through tenders aiming at the provision (or absorption) of liquidity to the banking system. The CBC's counterparties for such transactions will be credit institutions fulfilling the relevant criteria. As regards the collateral required for credit operations, the CBC has selected the pledge technique, with collateral pooling. The CBC is currently drafting the national legal documents, on the basis of the European Central Bank's General Documentation on Eurosystem Monetary Policy Instruments and Procedures, and preparing the technical infrastructure (IT systems) for monetary policy operations.

From the euro adoption date, the CBC will also implement Regulation ECB/2003/9 on the minimum reserves of credit institutions. In the context of its preparation for the implementation of this regulation, the CBC issued the Directive on the maintenance of minimum reserves with the CBC (Κ.Δ.Π. 510/2005), which entered into force on 1 January 2006, adopting to a large extent the provisions of Regulation ECB/2003/9. The CBC is planning to fully align its minimum reserve system with Regulation ECB/2003/9 around the end of 2007.

(iii) Statistics

Participation in the euro area will expand the obligations of the CBC to report statistical data to the European Central Bank. In the connection, in August 2005 the CBC issued the Directive on the monthly balance sheet of monetary financial institutions, which incorporates the provisions of Regulation ECB/2001/13. The CBC has also prepared a draft directive on a new direct reporting system for balance of payments statistics, which will facilitate the compilation of Cyprus's balance of payments and international investment position, fully in line with Guideline ECB/2004/15. Furthermore, responding to the requirements of the European Central Bank, the CBC is preparing for a change in the residency criterion for all statistics compiled by Cyprus, so that enterprises registered in Cyprus but having no physical presence in the country will be treated as residents of Cyprus for statistical purposes.

10.8.3. Banking sector

The banking sector will naturally play a major role in the introduction of the euro. Upon the recommendation of the CBC, each bank has established a special committee to coordinate the necessary preparations for the changeover to the euro. Each bank has also appointed a "euro-coordinator". In the context of the ongoing cooperation of the CBC and all the parties involved, the Coordinators Committee was set up with representatives of the banks, the Cooperative Societies Supervision and Development Authority, the Ministry of Finance, the Association of Cyprus Commercial Banks, and the clearing company JCC. In the meetings of the Euro-Coordinators Committee, the basic parameters of the frontloading of euro banknotes and coins were agreed. Special emphasis was also given to issues related to the banking services that will be provided to the public.

(a) Banks

The adoption of the euro affects the entire spectrum of banking operations and requires, inter alia, the adaptation of the accounting and information technology systems of each bank. Moreover, banks will face a loss of income from the conversion of national currency to euro and vice versa. The timely preparation of banks is vital for the smooth changeover to the euro. At the same time, with the appropriate preparation, banks as

enterprises will be able not only to reduce the cost of adjustment, but also to better face the competitive challenges ensuing from the adoption of the euro and to exploit opportunities in the vast market of the euro area.

The banks' role in the changeover from the pound to the euro comprises mainly the following tasks:

- **Contribution to the cash changeover** (see chapter 10.8.1)
- **Conversion to euro of bank accounts and loans denominated in pounds and replacement of interest rates**

  On the euro adoption date (1 January 2008) banks (as well as cooperative credit institutions) will convert into euro all balances on customers' accounts and loans denominated in pounds, in accordance with the conversion rate (which is expected to be adopted by the Council of the EU on 10 July 2007). For example, if a conversion rate of €1 = £0,585274 is adopted, an account balance of £10.000,00 will be automatically converted to a balance of €17.086,01 (i.e. 10.000/0,585274). The Euro Adoption Law (N. 33(I)/2007), which was enacted by the Parliament on 15 March 2007, ensures that the conversion will be carried out without any direct or indirect charge for the customer.

  Interest rates on deposits as well as loans will be replaced by the corresponding interest rates for the euro, pursuant to the Euro Adoption Law. However, in the case of deposits and loans for which a fixed interest rate was agreed, the interest rate will remain unchanged (unless the bank and the customer agree to a change).

- **Adaptation of means of payment other than cash**

  <u>Cheques</u>

  From the euro adoption date (1 January 2008) the issue of cheques in Cyprus pounds will not be legally possible. In accordance with the relevant legislation, cheques denominated in pounds with a date on or after the euro adoption date will not be valid as cheques. Therefore, to safeguard their interests, the public should not accept cheques in pounds with a date after 31 December 2007. In the last months of 2007, banks will supply their customers with cheque books in euro.

Electronic cards

All transactions by electronic cards will be conducted in euro as from the euro adoption date (1 January 2008).

Payment orders using transfers

All payment systems using transfers will be processing transfers only in euro as from the euro adoption date (1 January 2008).

Standing orders and direct debits

In accordance with the principle of the continuity of contracts, standing orders will continue to be valid (unless they are explicitly amended or revoked by the ordering customer). The amounts of the standing orders will be automatically converted into euro, in accordance with the conversion rate (which is expected to be adopted by the Council of the EU on 10 July 2007).

(b) Cooperative credit institutions

The abovementioned information generally applies to cooperative credit institutions as well. Moreover, for the cooperative credit institutions in Cyprus, the euro adoption date coincides with the entry into force of the requirements of the EU banking directive (2006/48/EC – recast directive 2000/12/EC), which mainly concern capital adequacy. To successfully meet the challenges of harmonisation with the banking directive, the cooperative movement has promoted a series of structural and organisational reforms, including mergers on a geographic and/or functional basis, technological upgrading, and enhancement of the efficiency of cooperative credit institutions. Strengthened by these reforms, cooperative credit institutions will further contribute to the smooth introduction of the euro in Cyprus.

10.9 COOPERATION WITH THE EUROPEAN COMMISSION AND THE EUROPEAN CENTRAL BANK.

The implementation of the last phase of the Plan for the changeover from the Cyprus pound to the euro will be assisted by the continuation of the Partnership Agreement with the European Commission and by a memorandum of understanding between the

European Central Bank and the CBC. The main activities covered under this cooperation with the European Commission are:

- The carrying out of a survey on the extent of preparedness of enterprises - October 2007
- The making and situating of portable stands – July 2007
- The euro-celebration of the setting of the conversion rate between the Cyprus pound and the euro – 10 July 2007
- The euro calendar competition for schools – September 2007
- Formal celebrations for the euro - 18 January 2008
- The carrying out of a survey to evaluate the communication campaign – April 2008

In parallel, the CBC's information campaign was designed in cooperation with the European Central Bank. Amemorandum of understanding (MoU) is expected to be signed by the European Central Bank and the CBC in July 2007. The MoU will cover, inter alia, the following:

- Production of creative materials, that will be developed and produced centrally by the European Central Bank and whose distribution will be done by the CBC
- Hoarded coin campaign
- Seminars for financial journalists in Cyprus
- Training of cashiers on the security features of the euro banknotes and coins

More information is given in the "Central Bank of Cyprus Euro Information Campaign Plan" which is available on the CBC's website (www.centralbank.gov.cy).

11. BENEFITS AND CHALLENGES.

With the adoption of the euro, Cyprus will become a member of the Eurogroup. It is noted that countries that have adopted the euro, have continually attained increased power and influence in the decision-making process on various EU policies. In addition the entry of the Central Bank of Cyprus to the Eurosystem, is expected to upgrade the role of Cyprus with respect to the economic and monetary developments in the EU.

The smooth adoption of the euro will constitute an achievement with positive impact on the status and economic robustness of our country.

The benefits are:

- The convergence of the interest rates in Cyprus with those in the euro area and the consequent adjustment of the cost of borrowing will benefit the consumers, enterprises, the public sector and generally economic expansion.
- The elimination of the foreign exchange risk for transactions in euro and the consequent reduction of exchange costs and uncertainty will have favourable effects on investment.
- Greater transparency in prices will strengthen competitive conditions, giving substantive benefits, particularly to consumers. Cypriot consumers will be able to henceforth take decisions which are in their best interest, as they will now be able to compare directly the prices in Cyprus with those corresponding overseas. Cypriot businessmen will be able to evaluate better the opportunities of the single European market.
- Easier access to the capital markets of the euro zone will open up the spectrum of choices for investing and borrowing, particularly for households and enterprises.
- The strengthening of investment activity and the reinforcing of a stable business environment, as a result of the securing of conditions of price stability, as well as the securing of the confidence of international markets and investors in the Cyprus economy, with positive effects on the balance of payments, constitute indirectly, very important and crucial benefits for the Cyprus economy.
- Participation in the euro zone reinforces the incentives for advancing the necessary structural reforms, improving further fiscal consolidation (which will facilitate the implementation of a more substantive social policy, during periods of difficult economic conditions) and taking greater advantage of the EU objectives and programmes.
- The adoption of the euro supports the preconditions for the further development of the Cyprus economy with high rates of growth and employment under conditions of social cohesion.

The challenges are;

- The loss of the power to exercise an independent monetary and exchange policy. Although, it should be noted that Cyprus had never used the exchange rate

(devaluation of the pound) as a tool to obtain or strengthen its competitiveness, even in difficult economic periods (e.g. after the Turkish invasion of Cyprus and the Gulf War). Nevertheless, with the loss of independence in exercising monetary and exchange policy, the emphasis of policy actions will centre more on fiscal policy.

- The change in currency constitutes a very important and multifaceted exercise, in which are involved, in one way or another, the public and the professional and social bodies of the country. Substantial preparation is required for the introduction of the euro banknotes and coins, for the adjustment of the accounting and data processing programmes of enterprises and the public sector and for the necessary communications campaign. This preparation presumes an economic cost also. Despite this, it must be noted with emphasis that, the successful adoption of the euro makes the above cost insignificant, in view of the tremendous benefits from the prospects which will open up, both over the medium and long term, for the Cyprus economy.
- With the adoption of the euro, the possible inability of Cyprus to conform to the conditions of the Stability and Growth Pact will, from now on, continue to place Cyprus in the process of excessive deficits, which involves the imposition of penalties in the event of not responding to the recommendations of the EU Council for the correction of the deficit. Nevertheless, it should be noted that the obligation to conform to the provisions of the Stability and Growth Pact, and the danger of entering the process of excessive fiscal deficits, exists irrespective of whether we enter or not the euro area. Furthermore, in the case where there is inability to conform with the recommendations of the EU Council, in the context of the process of excessive fiscal deficit, particularly for countries not participating in the euro zone (in which case the imposition of monetary penalties is not provided for), there is the possibility that the cost may be more onerous for the country, as a result of political pressures, than the imposition of monetary sanctions. In addition, the fixed exchange rate policy which traditionally has been followed by Cyprus, in an environment permitting the free movement of capital, implies the implementation of fiscal discipline, irrespective of the requirements of the EU. Otherwise the stability of the pound would have been endangered.

- The effects on the general level of prices which may be attributable to the transition to the new currency are likely to be negligible. The adoption of the euro by the present twelve member countries of the euro zone had an insignificant increase in the rate of inflation in the euro area. Specifically, the effect as estimated by Eurostat is put at between 0.1% and 0.3%. The experience of the member countries which have adopted the euro has, nevertheless, shown that a certain problem did exist with respect to excessive price increases, during the conversion of the values of certain products of daily use, particularly in those countries where the appropriate deterrent measures were not taken. Because of this problem the mistaken impression was formed by the public of substantive increases occurring in the general level of prices. In the case of Cyprus, this danger is significantly ameliorated by the fact that the value of the Cyprus pound is higher than that of the euro (£1 = 1.7086 euro). Also the fact that the Cypriot public is familiar with the euro constitutes a deterrent to the emergence of this problem. In addition, the Cyprus authorities, having in mind the experience of other countries, are now preparing measures for the minimization of the danger of prices increases. In these measures are included the dual display of prices for a number of months prior to and after the introduction of the euro, the establishment of a committee to monitor the changeover of prices, as well as the implementation of a Fair Pricing Code.

12. CONCLUSIONS.

- The positive perception of the public regarding the introduction of the euro will increase.
- The results of the changeover that took place in Slovenia are not expected to occur in the case of Cyprus, as conditions here are different.
- One should be certain that the changeover from the pound to the euro will be successful.

APPENDIX I

Conditions for the adoption of the euro: Maastricht convergence criteria

The EU has specified certain criteria that a member state must fulfil to adopt the euro and become a full member of the Economic and Monetary Union (EMU). These criteria (known as the Maastricht criteria) are laid down in the Treaty establishing the European Community and focus on the "achievement of a high degree of sustainable convergence" as follows:

- **Inflation**. The average rate of inflation, observed over a 12-month period before the examination (on the basis of the harmonised consumer price index) should not exceed by more than 1½ percentage points the average rate of inflation of the three best performing EU countries in terms of price stability.
- **Government budgetary position**
  - **Fiscal deficit**. There should not be an excessive deficit, i.e. the fiscal deficit should not exceed the reference value of 3% of the Gross Domestic Product (GDP).
  - **Public debt**. The public debt should not exceed 60% of GDP, unless the ratio is sufficiently diminishing and approaching the reference value at a satisfactory pace.
- **Exchange rate stability**. There should be observance of the normal fluctuation margins provided for by the exchange rate mechanism for at least two years without severe tensions, in particular without an own-initiative devaluation against the currency of any other EU member state. That is, the national currency must successfully participate in ERM II for at least two years.
- **Long-term interest rate**. The average long-term interest rate (i.e. the yield of the ten-year government bond) over a 12-month period should not exceed by more than two percentage points the average rate of the three best performing EU countries in terms of price stability.

In addition to the above nominal criteria, the assessment also takes into account several other factors, including the situation of the current account, the development of unit labour costs and other price indices.

- **Legal convergence**. National legislation should be compatible with the Treaty establishing the European Community and the Statute of the European System of Central Banks and of the European Central Bank.

APPENDIX II

Main features of the Exchange Rate Mechanism (ERM II)

ERM II is a multilateral arrangement linking the currencies of non-euro area EU countries to the euro. It aims at ensuring the relative stability of the currencies of non-euro area EU countries, in the context of economic policies fostering macroeconomic stability and convergence. For the currency of each non-euro area country participating in ERM II, a central rate against the euro is specified by mutual agreement between the country concerned, the other countries participating in ERM II, the euro area countries and the European Central Bank. Exchange rates may fluctuate within a standard fluctuation band of ±15% around the central rate, and the parties intervene, if necessary, to prevent fluctuations outside the agreed band.

Thus ERM II promotes exchange rate stability. At the same time, the participation of national currencies in ERM II is a testing phase for the sustainability of the exchange rate, so that the conversion rate at which the euro shall be substituted for the national currency (which will be decided irrevocably by the Council of the EU, when all the conditions for euro adoption are fulfilled) will be appropriate.

Currently, the currencies of the following seven countries participate in ERM II: Denmark, Estonia, Lithuania, Cyprus, Latvia, Malta and Slovakia. Estonia and Lithuania (as well as Slovenia) joined ERM II on 28 June 2004, Cyprus, Latvia and Malta joined on 2 May 2005, and Slovakia on 28 November 2005.

APPENDIX III (a)

National Advisory Board (National Changeover Board).

Composition:

- Minister of Finance, Chairman.
- Minister of Commerce, Industry and Tourism.
- Governor of the Central Bank of Cyprus.
- 2 members from the Central Bank of Cyprus:
    - Governor's Advisor.
    - Officer responsible for EU matters.
- 2 members from the Ministry of Finance:
    - Director General of the Ministry of Finance.
    - Finance Director responsible for EU matters.
- Other bodies – House of Representatives Finance Committee; Attorney Generals Office; Commercial Bankers Association; Accountants, Lawyers and Consumers Associations; Department of Cooperative Development; Cyprus Chamber of Commerce; Employers and Industrialists Federation; Labour Organizations; Farmers Organizations; Local Authorities; Semi-government Organizations.

Objective/Responsibilities:

- National strategy – Information– Suggestions.
- Monitoring the progress in the implementation of the Strategic Plan
- Formulation of suggestions for changes in the Strategic Plan.

Organization/ Operation:

- Meets twice yearly.

APPENDIX III (b)

Political Committee for the changeover from the pound to euro.

Composition:

- Minister of Finance, Chairman.
- Minister of Commerce, Industry and Tourism.
- Governor of the Central Bank of Cyprus.
- 2 members from the Central Bank of Cyprus:
    - Governor's Advisor.
    - Officer responsible for EU matters.
- 2 members from the Ministry of Finance:
    - Director General of the Ministry of Finance.
    - Finance Director responsible for EU matters.
- Other bodies – Heads or representatives of political parties.

Objectives/Responsibilities:

- Information - suggestions
- Monitoring the progress in the implementation of the Strategic Plan
- Formulation of suggestions for changes in the Strategic Plan.

Organization/Operation:

- Meets twice yearly.

APPENDIX III (c)

Coordinating Committee.

Composition:

- Governor Central Bank of Cyprus, Chairman.
- Four members from the Central Bank of Cyprus :
  - Governor's Advisor.
  - The two chairmen of the Central Bank Committees (technical and Communications.
  - Officer responsible for EU matters.
- Five members from the Ministry of Finance:
  - Director General of the Ministry of Finance.
  - Accountant General.
  - The two Chairmen of the competent Committees of the Ministry of Finance, corresponding to the Committees of the Central Bank.
  - Finance Director responsible for EU matters.
- One member from the Ministry of Commerce, Industry and Tourism (MCI&T)
  - Director General of (MCI&T).

Responsibilities:

- Detailed drafting of the National Action Plan.
- Submission of reports informing the National Changeover Board on the progress of implementation of the National Action Plan.
- Monitoring and guiding the work of the technical committees and setting priorities.
- Coordination and cooperation between Ministry of Finance and Central Bank of Cyprus.
- Contact with European Commission, European Central Bank and member states in euro zone.

Organization/Operation:

- Meets once a month or more frequently, when considered necessary.

APPENDIX III (d)

Common Communications Committee.

Composition:

- Finance Director Ministry of Finance responsible for EU matters, Chairman.
- Three members of Ministry of Finance, One member of Public Information Office, and one member from Ministry of Commerce, Industry and Tourism..
- Four members of the Central Bank of Cyprus.
- Head of the Representation of the European Commission, in Cyprus.

Responsibilities:

- Formulation and implementation of the communications policy strategy.
- Coordination and cooperation between the Ministry of Finance and the Central Bank of Cyprus, according to the responsibility of each organ.

Organization/operation:

- Meets once a month or more frequently, when considered necessary.

APPENDIX III (e)

Technical Committees - Ministry of Finance/Civil Service.

- Committee for the analysis of the impact on the economy, of the introduction of the euro and the preparation of suggestions for the successful adjustment of the economy.
- Committee for the Communications Policy – informing enterprises and consumers (in close cooperation with the Public Information Office).
- Legislative Framework Committee, (in close cooperation with the Attorney Generals Office and the Central bank of Cyprus).
- Committee for the preparation of the wider public sector, including the semi-government organizations and local authorities.
- Committee for the preparation of the business sector – encouragement and guidance for timely preparation of enterprises and the facing of the problem of unjustified price increases (in conjunction with the Central Bank of Cyprus and in close cooperation with the Ministry of Commerce, Industry and Tourism).
- Committee for the vulnerable groups of the population, aliens and Turkish Cypriots (in conjunction with the Central Bank of Cyprus and in close cooperation with the Ministry of Labour and Social Insurance)

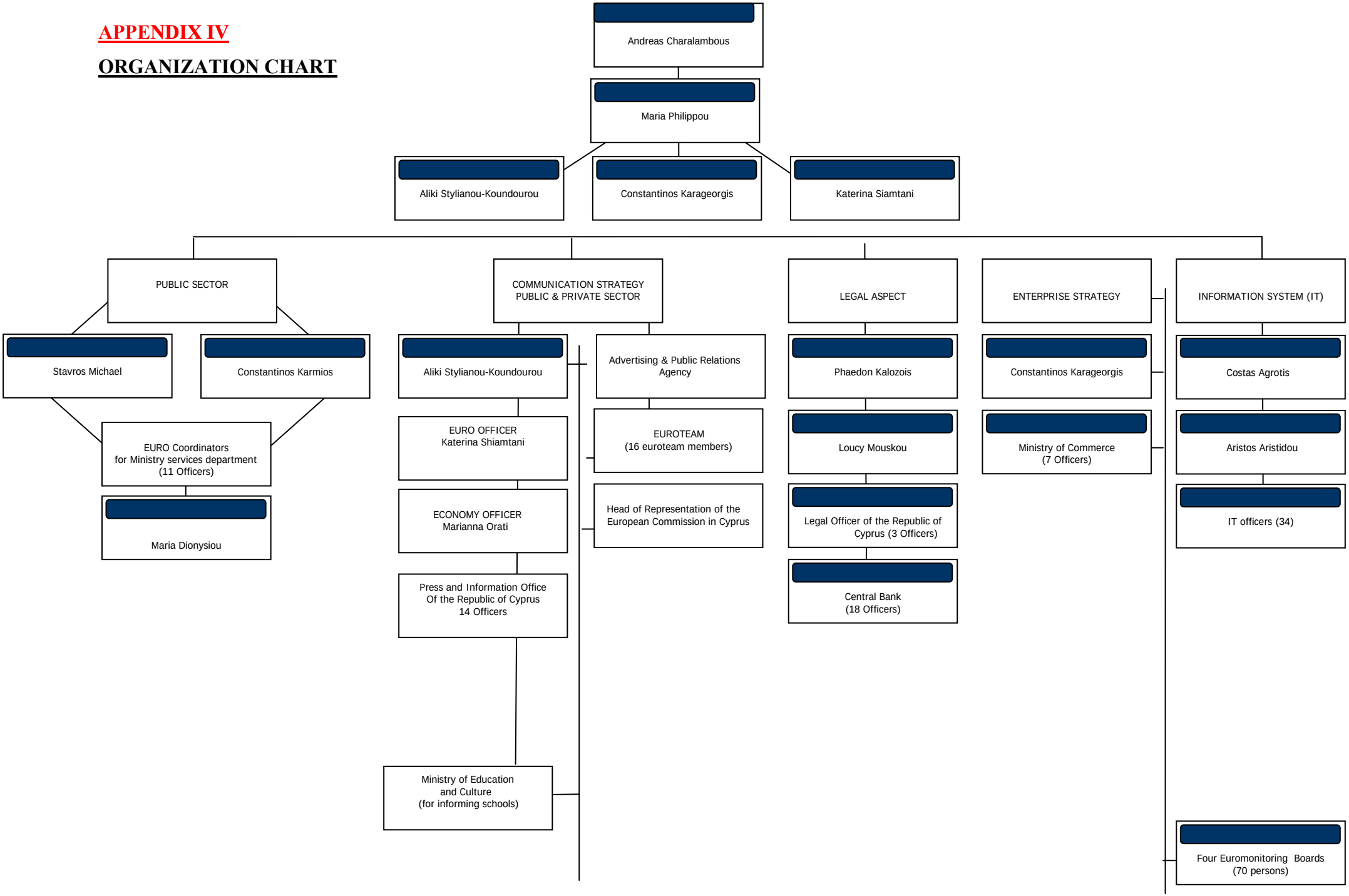
APPENDIX III (f)

Technical Committees - Central Bank of Cyprus.

- Coordinating Committee of the Central Bank of Cyprus.
- Communications Committee – in cooperation with the Common Communications Policy Committee.
- Technical Committee – responsible for the introduction of the euro in its physical form and the preparation of the financial sector.

APPENDIX IV

ORGANIZATION CHART



APPENDIX V

THE INTRODUCTION OF THE EURO, ROUNDING AND INFLATION: MYTHS AND REALITIES.

by Zenon G.Kontolemis and Panos Pasiardis.
An economic policy commentary of the Economic Research Centre of the University of Cyprus[*].

The entry into the euro zone is one more major step which will bring Cyprus, not just closer, but into the core of the European Union. This, naturally, implies the loss of monetary independence for Cyprus, a small price to pay compared to the many economic and political benefits which our country is expected to have, particularly if it takes advantage of the opportunities which will open up in the new economic environment. Despite this, discussion has often centered not on the advantages of entry into the Eurozone and the efforts which must be made for the Cyprus economy to confront the new challenges, but that on the introduction of the euro the cost of living will increase as a result of the "rounding" up of prices. This concern is fuelled by articles on significant price increases in countries which had entered the Eurozone recently, specifically, Greece, Portugal and Italy.

The rounding of prices is of course unavoidable. The conversion of prices from pounds to euro is unlikely to result in "convenient"[•] prices for most products, particularly for those of small value, which are frequently purchased and in cash. However, how easy is it for an enterprise which operates in an intensely competitive environment to utilize the rounding as an excuse to increase its prices? To what extent would the increases in prices, which coincide with the change in the currency, have happened without this change? Is it possible that the change to a currency which is used to measure prices exaggerates the impression of price increases? What will be the expected increase in the cost of living, from the introduction of the euro into Cyprus and which social groups would be most affected?

This commentary attempts to answer the above questions and to give the correct extent of the problem, within a context that makes it easy to understand what is myth and what is reality in the discussion with respect to rounding.

The experiences of other countries.

The experience of all the countries which adopted the euro on 1st January 2002 was generally very positive. The entry into the Eurozone brought structural changes ensuring macroeconomic stability. Countries suffering chronic inflation problems and devaluations of their national currencies, such as Italy, Portugal and Greece, assured a stable environment for price and interest rate determination. Interest rates and inflation fell dramatically in these countries, both during their course towards convergence prior to 1999, as well as later they were within the Eurozone.

The above positive long term affects of the entry to the Eurozone is shadowed to a certain extent by the argument that, during the process of conversion of the national currencies to the euro, price increases and profiteering arose. However, the facts do not support this concern. They simply show that there were small increases in the prices of certain products which facilitated transactions, particularly where the transaction is

---

[*] Article published February 2007.

[•] Translators note: convenient prices = prices which on their conversion would not require either rounding up or down.

undertaken in cash, by the price being adjusted to result in a number that was the multiple of 5 or 10 (or for the number to end in 95 or 99). Excessive price increases were noted (eg. in Germany, for certain services), however, these related to a small number of products and did not significantly affect the cost of living. The countries which introduced the euro in 2002, had on average the same inflation as that which they had in the previous three years, with only small increases for Greece, Ireland, Portugal and Spain. This is confirmed by the survey of the European Commission which showed that, the price increases which were caused by the conversion of the national currencies to euro were between 0.3% and 0.5%.

Divergence between reality and impressions.

As opposed to what is set out in the statistics, the impression of the layman in the countries which joined the Eurozone is that prices increased significantly after the 1/1/2002 and they remain at relatively high levels untill today. This phenomenon is particularly strong in Germany, Greece, Italy, Portugal, Spain and Holland. What can then explain this divergence between the very small real increases in prices and the large increases which consumers perceived had taken place, due to the introduction of the euro?

To begin with, the public compared the current prices in euro with the "stable" prices in national currencies, that existed prior to the introduction of the euro, creating thus the false impression that prices increased as from the introduction of the euro to these countries, also, many enterprises may have used the introduction of the euro as an opportunity to "cover" increases in prices which would have occurred anyway. Even in the cases where, the change in prices involved costs (eg. changes in menus, signs, etc.), enterprises may have delayed the price increases until the introduction of the euro. Nevertheless, the consumer did not realize that certain price increases, which were made to coincide with the introduction of the euro, were unavoidable. Thus he simply considered all price increases to have been due to the change in currency.

There are other reasons, also, which created the perception that price increases occurred in certain countries, as a result of the introduction of the euro, such as the lack of familiarity with the new currency, the confusing and approximate method used to convert prices into euro. For example, the conversion rate for the German Mark was 1.95583. Naturally, in the mind of the consumer the conversion from Marks to euro, for purposes of comparison, was done at the rate of 1 euro for 2 marks, an approach which overvalued the new prices by 2.26%.

What is expected to happen in Cyprus?

The central exchange rate parity of the pound to the euro in the exchange rate mechanism is 0.585274. Inevitably the consumer will continue for quite some time to "think" in terms of Cyprus pounds and to convert prices to their old currency value. This conversion will be done by approximation, most likely on the basis of one pound equaling 0.6 euro. A simple rule used by Cypriots today, on their visits to countries where the euro is used, is to divide the prices by two and to then add 10% to find the value in Cyprus pounds. If we assume that they will do the same after the introduction of the euro to Cyprus, then the mistaken impression will be created that the prices have risen by 2.5% compared with the period prior to the introduction of the euro. At the same time, if we add an increase of 2.5% which is expected to occur due to current inflationary trends, then the impression will be created of prices increasing at a rate of 5%. Based on these rough calculations, the consumer will "observe" an increase in

prices which he will mistakenly attribute to the euro, irrespective of whether or not and to what extent prices will be affected by rounding.
Certainly, all that has been said above does not mean that there will not be cases where some will try to exploit the confusion of the consumer, as a result of the change of the currency, to deceive him, or that the rounding will not be mainly upwards instead of downwards. However, these phenomena are expected to be limited given that the economy operates on certain basic principles from which it is difficult for an enterprise or a consumer to deviate. As we have already mentioned above, the experience of other countries shows that limited price increases did take place which did not evolve into inflation, either because they involved a small number of products whose weight in the Consumers Price Index was insignificant (newspapers, coffee, kebab, parking charges, chocolate), or because these increases were countered by reduction in prices of other products (electronic, communications).
For discussions sake, let us assume that this will not happen in Cyprus and that with the introduction of the euro, a number of enterprises will try to exploit the new order of things, so as to increase their prices disproportionately. Under conditions of free competition, the excess profits that will occur to these enterprises will be an incentive for other enterprises to also offer the same products, as a result supply will increase and prices will be reduced to normal levels. Should this not happen and prices remain higher than normal levels, then the purchasing power of consumers will be reduced and as a result demand will fall, which again will lead to counterbalancing reductions in prices. For example in Germany where, with the introduction of the euro, large price increases by restaurants were observed demand fell and in the period which followed, the rate of price increases slowed down substantially.
In other words, competition between enterprises and the fact that the purchasing power of consumers is given, do not permit margins for significant price increases. The introduction of the euro into Cyprus can not infringe these basic economic rules and thus lead to inflation, except if it becomes an excuse for increases not only of prices but also of wages/salaries. This scenario has not been observed in any country.

Distortion of prices.
However unlikely the possibility of a general increase in the cost of living is, as a result of the introduction of the euro in Cyprus, it is certain that there will be rounding of prices which will create certain distortions in respect of the "relative" prices between products, which will change. The prices of certain products, particularly of necessities (eg. foodstuff) with an inelastic demand, are most likely to be rounded up. The opposite will tend to happen to the prices of products with elastic demand. As a result, there will be a redistribution of income from consumers to the benefit of enterprises producing products with inelastic demand.
As mentioned earlier, the distortion of prices due to rounding up of the prices of necessities, may be one reason that consumers in other countries have linked the introduction of the euro with the increase in the cost of living. In other words, the introduction of the euro has increased the cost of living of the lower income groups, which spend the greater part of their income on necessities, while leaving unchanged or reducing the cost of living of the higher income group consumers. The general price index was not affected significantly because, by its nature, it weighs the increase in the cost of living according to overall expenditure, thus the increase in the cost of living of the rich has greater weight than that of the poor.
One way to ameliorate this distortion of prices, due to rounding, is the extension of the use of electronic payment for small and/or frequent transactions, which are currently

settled in cash. The use of credit/debit cards for payments will reduce to a great extent the need for rounding up, so as to have "convenient" prices. For example, a newspaper of 50cents (of a pound), which would cost 85.43 cents (of a euro), would tend to be rounded to one euro if payment is to be in cash, while if payment is by card then a price nearer 85cents would be equally convenient.

It is important to emphasize that the distortions of prices due to rounding can not be on a large scale, since the necessities are also produced in a free competitive market. Rounding up of prices increase profits and encourage countering trends, such as the increase in their quantity supplied and/or improvement in quality. For example, if the kebabs costing 2.50 pounds become 5 euro, instead of 4.50 euro, there will be an increase in their quantity. The same will happen for other products, eg. periodicals and newspapers will improve their quality and/or quantity of content and coffee will be served in qualitatively improved surroundings. If this does not happen, then the increase of the price was necessary for other reasons and the enterprise simply combined it with the change of the currency. Only enterprises producing products without competitors (or in collusion with their competitors) can increase their prices, without worrying about the reactions of the consumer, but such enterprises do not need the change in the currency to increase prices.

How the flexibility of the market can resolve the problem of rounding can be seen by the example of the traditional envelop given at weddings to the newly wed couple. The popular envelope of 20 pounds is equal to 34.17 euro. Some may round up the amount to 40 euro, while others, may round down to 30 euro, so that on average the amount spent on such envelopes would remain about the same. If this does not happen and the envelope of 40 euro prevails as "socially acceptable", then most probably the number of weddings which the Cypriot family attends on average will be reduced, at least in the short run. To the extent that this also does not happen, then the family will be forced to reduce some other expenses in order to make ends meet, something that would pressure other prices downwards which would counterbalance the higher cost of thee envelope.

Conclusions.

On the basis of simple economic logic, the introduction of the euro into Cyprus is not expected to lead to a general increase of the cost of living, other than the minimum required for the rounding of prices. This is shown by the experience of other countries, where the changeover to the euro operated more as a factor for long term stability of prices. Nevertheless, in these countries the layman holds the opposite view, believing that the introduction of the euro brought about large increases in the cost of living.

It is to be expected that with the introduction of the euro in Cyprus rounding up of prices will be observed, particularly for necessities and/or low value products frequently purchased in cash, where it is important to set "convenient" prices. However the increase in prices due to this rounding can not be large, since the competition between enterprises and the given purchasing power of the consumer, will not permit such large margins.

The small increases in prices may be inflated in the mind of the consumer and be considered to be large increases in the cost of living, because they will be related mainly products bought by the public widely on a regular and systematic base. This is a subject that needs to be emphasized in the information given to citizens about the introduction of the euro into Cyprus. Specifically the reasons which may mislead the public into thinking that the introduction of the euro is the cause of the price increases, when this does not conform to reality, must be explained.

In concluding, the impact on the cost of living of the rounding is expected to be insignificant and it should not monopolize the discussion of the introduction of the euro into Cyprus. Neither must it become an excuse for unnecessary interventions in the determination of prices. The citizen must simply be correctly informed, so that he will not be swept away by mistaken impressions into incorrect behaviour , but use his power as a consumer to avoid profiteering against him.

Project Coordinator

Mrs. Maria Philippou,

Tel: 22601198

Fax: 22602057

E – Mail: mphilippou@planning.gov.cy

Useful Web Sites

Ministry of Finance

http://www.mof.gov.cy

EURO

http://www.euro.cy