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Estonia joins the eurozone

The euro became the official currency in Estonia on 1 January. The introduction of the common currency, which became possible owing to a policy of sharp budget cuts, crowns the difficult economic reforms and symbolically closes the process of Estonia's integration with Western structures. However, given the problems existing in the eurozone, it is difficult to predict whether the new currency will have a stabilising effect on the Estonian economy.

Estonia formally took its first efforts to join the eurozone in 2004. Despite the economic slump (its GDP fell by 14.1% in 2009), Tallinn managed to meet the convergence criteria. It was especially difficult to keep the budget deficit at a low level. This entailed the need to severely cut budget spending (the savings reached 9% of GDP in 2009). The consequences included maintaining a low level of deficit (as little as 1.7% of GDP in 2009) on the one hand, but on the other the impoverishment of its citizens and a significant growth in unemployment rate, (from 5.5% in 2008 through 13.9% in 2009 to 18.2% in 2010).

The adoption of the euro will reduce transaction costs, which is especially significant for the open and export-oriented Estonian economy. This will also have a positive impact on the investment climate and the banking system's stability, and lower the government's costs of obtaining funds for debt financing. However, on the other hand, the Estonian economy has become more vulnerable to crises in the eurozone. Tallinn will have to accept the need to provide financial backing to the less disciplined members of the eurozone as part of the European Financial Stability Facility being developed.

In political terms the introduction of the European currency is likely to be used as the main topic in the campaign of Andrus Ansip's centre-right government preceding the parliamentary elections in March 2011. Despite the strong dissatisfaction of Estonian public (around 40% of society) with the adoption of the euro and the present government's promises to continue the cost-saving fiscal policy, his party is likely to win the upcoming election. <dab>