

Greece: First Review Under the Stand-By Arrangement

The following documents have been released and are included in this package:

- The staff report, prepared by a staff team of the IMF, following discussions that ended on September 10, 2010 with the officials of the Greece on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on August 27, 2010. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.
- A Staff Supplement
- A Press Release
- A statement by the Executive Director for Greece

The document(s) listed below will be separately released.

Letter of Intent*

Memorandum of Economic and Financial Policies*

Technical Memorandum of Understanding*

LOI & Memorandum of Understanding on Specific Economic Policy

Conditionality (European Commission and European Central Bank)*

*Also included in Staff Report

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

Copies of this report are available to the public from

International Monetary Fund • Publication Services
700 19th Street, N.W. • Washington, D.C. 20431
Telephone: (202) 623-7430 • Telefax: (202) 623-7201
E-mail: publications@imf.org • Internet: <http://www.imf.org>

International Monetary Fund
Washington, D.C.

INTERNATIONAL MONETARY FUND

GREECE

First Review Under the Stand-By Arrangement

Prepared by the European Department in Consultation with Other Departments

Approved by Poul M. Thomsen and Martin Mühleisen

August 26, 2010

EXECUTIVE SUMMARY

- **Staff's overall assessment is that the program has made a strong start.** End-June quantitative performance criteria have been met, led by forceful implementation of the fiscal program, and major reforms are ahead of schedule. However, important challenges and risks remain.
- **Stand-by-Arrangement.** On May 9, 2010 the Executive Board approved a three-year Stand-By Arrangement (SBA) for Greece under the Emergency Financing Mechanism (EFM) in the amount of SDR 26.4 billion (3,212 percent of quota). The first purchase was SDR4.8 billion (€5.5 billion) upon SBA approval. The euro-zone partner countries committed €80 billion, and made a first disbursement of €14.5 billion. The staff report for the interim review, as required under the EFM, was issued as Country Report No. 10/217. The second disbursement, subject to the completion of this review, amounts to SDR 2.16 billion (about €2.5 billion); €6.5 billion will be contributed by the euro area countries.
- **Recent developments.** The recession is unfolding in line with expectations. Inflation is higher than expected from indirect tax hikes, but does not seem to have led to second round effects as wage growth is in fact moderating. The current account is adjusting somewhat slower than expected. Fiscal consolidation is broadly on track, with overperformance at the state budget offsetting slippages at sub-national levels of government. Liquidity in the banking system is tight but adequate, supported by the ECB's securities market purchase program (SMP) and other measures to boost banks' repo eligibility. Far-reaching pension and labor market reforms have been implemented ahead of schedule and other important reforms are underway.
- **Program status.** Despite slightly lower revenue, end-June performance criteria were met, but the indicative target on the non-accumulation of domestic arrears was missed, reflecting weak expenditure control at the sub-national level. To address still significant fiscal risks, tax administration steps and better expenditure monitoring and controls are envisaged to be in place by end-September, as elaborated with FAD TA. The measures required under the structural benchmarks have all been implemented albeit, in one case, with slight delays, except for the benchmark on the completion of the actuarial report, whose implementation has been delayed by staffing and data constraints.
- **Discussions** took place on July 26–August 4 with the Minister of Finance, Governor of the Bank of Greece (BoG), Minister of Labor and Social Security, Minister of Interior, Minister of Economy, Competitiveness and Shipping, Minister of Health, Minister of Infrastructure and Transport, Minister of Defense, and staff in these and other ministries and agencies, and private banks. The mission also met leaders of employees and labor unions and some opposition parties.
- **Staff** comprised P. Thomsen (head), B. Traa, G. Everaert, M. Moreno Badia, E. Perez Ruiz (all EUR); S. Eble and M. Soto (FAD); Y. Sun (SPR); and O. Frecaut and L. Zanforlin (MCM).

Contents		Page
I. Recent Economic Developments.....		3
II. Policy Discussions		4
A. Macroeconomic Framework		5
B. Fiscal Policy		6
C. Financial Sector.....		11
D. Structural Policy and Data Reporting.....		13
III. Program Modalities and Safeguards Assessment		18
IV. Staff Appraisal.....		18
 Boxes		
1. The Fiscal Management Bill		8
2. Pension Reform		10
3. Reforming State-controlled Banking Entities		13
4. Labor Market Reform.....		14
5. Road Freight Reform.....		16
6. Public Enterprises and Privatization.....		17
 Figures		
1. Selected Indicators, 2000–10		21
2. Labor Markets, 2001–10		22
3. Balance of Payments Indicators		23
4. Financial Indicators, 2007–10		24
5. Money and Banking Indicators, 2005–10		25
 Tables		
1. Selected Economic Indicators		26
2. General Government Operations, 2009–15		27
3. Public Sector Financing Requirements and Sources		28
4. Summary of Balance Payments, 2009–15		29
5. External Financing Requirements and Sources, 2008–15		30
6. Core Set of Financial Soundness Indicators for Deposit Taking Institutions, 2000–10.....		31
7. Access and Phasing under the Stand-By Arrangement, 2010–13		32
8. Indicators of Fund Credit		33
9. Monetary Survey		34
10 Modified General Government Cash Balance for Program Monitoring		35
 Annexes		
Annex 1. Public Debt Sustainability.....		36
Annex 2. External Debt Sustainability		40
 Attachments		
Attachment I. Letter of Intent		43
Attachment II. Memorandum of Economic and Financial Policies.....		45
Attachment III. Technical Memorandum of Understanding.....		54
Attachment IV. Memorandum of Understanding on Specific Economic Policy Conditionality (European Commission and European Central Bank).....		62

I. RECENT ECONOMIC DEVELOPMENTS

1. Macroeconomic indicators are evolving broadly in line with expectations (Figures 1 and 2).

- **The slowdown is progressing as expected**, with the year-on-year contraction in GDP increasing from 2.3 percent in Q1 to 3.5 percent in Q2. The unemployment rate increased to 11.8 percent (SA) in April. Private consumption growth was somewhat more resilient early in the year than expected, offset by a weaker foreign balance, but this may well be a temporary factor (households appeared to have been using their savings cushions and some income from parallel market activity).
- **Prices ticked up faster than expected, reflecting one-off tax effects.** July inflation reached 5.5 percent (year-on-year), but this is due to one-off effects from the higher-than-expected pass-through of indirect taxes to inflation. Notably, at constant taxes, inflation has fallen below the euro-area average for the first time since euro-adoption. The three-year national collective wage agreement signed in July freezes minimum wages until mid-2011 and gives increases equal to the average euro-area inflation from that point onwards.¹ This contributes to moderating private sector wage growth and, hence, there is no evidence of second round effects.
- **The current account is yet contracting only gradually.** Stronger domestic demand, higher oil prices, and increased payments for ship orders have kept the trade balance high up to April (Figure 3). Moreover, tourism receipts have been adversely affected by strikes and unrest, and strong price competition from Turkey and Croatia.

2. **Policy implementation has made a strong start.** All end-June performance criteria (PCs) and all structural benchmarks were implemented (with slight delays in some cases), except for the benchmark on the completion of the actuarial report, whose implementation has been delayed by staffing and data constraints—the final report is now expected for March 2011. Important structural reforms are ahead of schedule. The indicative target on the non-accumulation of domestic arrears was not met, reflecting evidence of the buildup of accounts payable at sub-national entities, but the monitoring system for general government commitments, accounts payable, and arrears is still being developed (end-September structural benchmark), and there is an understanding that arrears should be amortized by year-end (MEFP ¶4).

- **Fiscal performance was better than anticipated, albeit some overdue payments surfaced in sub-national entities.** Significant under-execution of discretionary expenditures resulted in a large margin under the state budget primary spending PC of €5.6 billion. Ordinary revenues fell slightly below the target as shortfalls in indirect

¹ Also, arbitration decisions granting wage increases above those in the national collective agreement will be voided.

taxes were offset by higher non-tax revenues, which reflect tax administration efforts to collect fines and other fees. This state-budget overperformance offset slippages in local government and the social security sector (such that the general government deficit PC was also met, but with a smaller margin).² In July, a total of €4.4 billion of three and six-month T-bills were sold, mostly to domestic banks at an average yield of 4.4 percent.

- **In the financial sector, liquidity remains tight amidst still tepid market confidence.** Despite some improvements in market sentiment (Figure 4), Greek banks have not yet regained access to wholesale markets. The downgrade of the Greek sovereign by Moody's in June put pressure on collateral valuations, while some intermittent deposit outflows continued. However, repo-eligible assets have been boosted through government guarantees of bank bonds and the ECB's intervention in the government bond market has helped support the value of collateral.³
- **Solvency ratios are affected by the economic downturn, as expected.** NPLs have reached 8.2 percent in Q1 (from 7.7 percent in December) with corresponding increases in provisions which, along with revaluation losses in the trading book, generated a loss for the system on a consolidated basis. Preliminary indications are that NPLs continue to edge upward in Q2. Nevertheless, all banks remained above the minimum capital adequacy requirement of 8 percent.
- **Monetary conditions are gradually becoming more constrained.** Funding costs do not appear to have increased substantially as banks have substituted deposits and wholesale funding with cheaper ECB repos. However, banks have started to restrict credit, particularly to households, but there is no evidence of sharply increasing lending rates (Figure 5).
- **Fiscal, banking, and structural reforms are ahead of schedule.** A major pension reform was approved in July. Substantive labor market reform is also underway. A significant budget legislation reform, local government reform, and legislation governing the Financial Stability Fund have been passed, as discussed below.

II. POLICY DISCUSSIONS

3. **The program objectives and strategy continue to be appropriate.** The key challenges remain restoring fiscal sustainability, safeguarding financial sector stability, and

² Lower transfers from the state budget to social security funds may have partially shifted the deficit of the state to the social security sector.

³ Purchases of government securities have virtually halted in recent weeks as market sentiment started to stabilize. Analysts estimate that the ECB has purchased over €40 billion in Greek government paper.

boosting competitiveness—and hence growth and employment. While establishing a track record of program implementation will require time, as foreseen in the program, the authorities felt that some skepticism is now gradually starting to fade. The authorities' strong ownership and determined implementation of the program so far, in the face of some unrest, has started to deliver results. Some reforms are being implemented ahead of schedule.

4. **Discussions focused on:**

- **Consolidating the fiscal achievements.** Fiscal consolidation is underway, and discussions focused on limiting deviations between cash and accrual outcomes and addressing risks in this regard to assure that fiscal targets continue to be met. In addition, priority is being given to advancing tax administration reform to secure revenues and enhance the fairness of adjustment.
- **Making financial sector safeguards effective.** Ensuring financial stability remains crucial, with some challenges (in particular liquidity pressures) that need continued vigilance and further policy steps.
- **Formulating concrete action plans for structural reforms through 2010, in line with the MoU.** The authorities and staff agreed that increased attention in reforms needs to be placed on eliciting an early supply response. Having initially focused mainly on macroeconomic stabilization and fiscal major reforms, more emphasis now needs to be placed on policies to restore real-economy flexibility and competitiveness. Limited price compression following tax increases and a slow current account adjustment are indicative of the need to boost those structural reforms that could help boost competition and supply in the short term.

A. Macroeconomic Framework

5. **The macroeconomic outlook remains broadly unchanged.** (LOI ¶2, and Table 3).

- **Staff and authorities agreed that nominal growth will be somewhat higher than originally anticipated.** Real GDP is still heading for a 4 percent decline this year and some 2½ percent decline in 2011, unchanged from the original program, but with a composition that may reflect marginally stronger domestic and weaker foreign demand. The nominal growth outlook, however, has been revised upward because of an uptick in prices. Inflation is now expected to be peaking, with some further tax effects possible in early 2011, before slowing more decisively.
- **The authorities saw the risks to the growth outlook as being on the upside.** They noted that the informal economy and unrevealed pockets of wealth act as a buffer and underpin private consumption data. Staff emphasized that those cushions are unlikely to be supportive of economic activity in a sustainable way, and that downside risks to growth could materialize, especially over the medium term given the still weak competitiveness position and external environment.

- **The external current account deficit for 2010 has been revised upward** to reflect the more gradual decline in imports (excluding oil and ship orders) and weaker tourism receipts, despite a rebound in shipping revenues. Financing is expected to be higher partly due to higher private financing of ship deliveries and higher-than-expected needs for liquidity support from the ECB.
- **The public and external debt sustainability outlook are little changed.** Higher nominal GDP growth implies a slightly lower public debt-to-GDP ratio, which now peaks at 144 percent of GDP in 2013 (compared to 149 percent in the May 2010 program projections). However, the new €25 billion government guarantee package for financial sector liquidity support has been added to contingent liabilities. Higher current account deficits over the medium term provide a more gradual decline in the external debt-to-GDP ratio, which now remains above 100 percent of GDP by end-2015 (Annex 2).

B. Fiscal Policy

6. **Early performance was encouraging, but pressures continue to exist.** The June program targets were met, and the full complement of program measures is expected to ramp up its yield in the second half of the year. However, risks exist on the revenue outlook as the economy will be contracting, and spending is not under full control in subnational entities of government. Moreover, some under-execution in state budget spending is expected to reverse (for instance, due to a bunching of interest payments, and higher military spending in H2), and clearing accounts payable in hospitals may exert further (cash) expenditure pressures. In addition, items which are not yet reflected in fiscal PCs (which are defined on a cash basis), such as called debt guarantees—are expected to reach €1.5 billion as public enterprises face difficulties in rolling over maturing liabilities.⁴ These claims are in the accrual ESA95 definition of the deficit but not in the cash PCs for now—causing some unexpected deviations between cash and accrual deficit targets, which need to be addressed as the program moves into 2011 so as to avoid undermining market confidence.⁵

7. **The authorities agreed to continue under-executing spending at the state level.** The authorities will limit spending (including military, domestic capital, and operating expenditures) by €4 billion below earlier program projections in the state budget by end-year, including after provisioning for increased transfers to social security funds to reduce the stock of accounts payable in hospitals. The authorities were confident that those cuts are

⁴ Information on a number of items (e.g. accounts payable in the hospital sector, called guarantees, extra-budgetary accounts) was not available at the time program targets were designed. This information will be included in the program definition of PCs and targets from 2011 and beyond once the monitoring mechanisms are in place.

⁵ The EU's Excessive Deficit Procedure focuses on accrual-based deficits.

attainable without new measures and without building up new arrears given slow execution so far in operations and investment spending (about 36 percent of the full-year appropriations was spent by June), revisions to the schedule for military spending (down by €0.9 billion), and the scope for further reducing inefficient spending.

8. Stronger public financial management and especially tax administration are needed to mitigate risks:

- **In the area of public financial management**, the new Fiscal Management Law (Box 1) has passed, which is a major milestone to strengthening fiscal management and control by the Ministry of Finance vis-a-vis the general government. The implementation of the law is now starting and implies, among others, setting up commitment registries (taking inventory of stocks and flows; a structural benchmark by end-September) to improve arrears monitoring and reporting, and preparing cash flow projections with clear expenditure prioritization on the basis of which spending commitments will be released. Given the problems in the hospital sector and the time required to establish fully the commitment controls, the government has already placed accounting firms in state hospitals to improve their financial management and spending control.
- **Advancing tax administration reform is a crucial priority** to limit risks of revenue shortfalls, and also to increase fairness in sharing the adjustment burden. With assistance from FAD TA, by September five specialized taskforces are expected to be put in place (on implementing new tax legislation, improving audits, boosting arrears collection, collecting large taxpayer payments, and improving tax compliance (including using presumptive taxation) and service). This will be the basis for designing and implementing an ambitious multi-year anti-tax evasion and compliance agenda (MEFP, ¶7).

9. The authorities emphasized several other reforms that are being implemented, and should limit budgetary risks going forward (MEFP, ¶9).

- *Health sector.* Changing procurement procedures to reduce pharmaceutical spending by 20 percent (starting September), improving profiles and benchmarking for patients and doctors to avoid unnecessary prescriptions, and enforcing and increasing copayments for outpatient and diagnostic services to contain health spending.
- *Local governments.* The recently passed Kallikratis law on local government reform will significantly reduce the number of local administrations, entities, and elected and appointed officials. While the mission saw some risks to targeted savings, the authorities assured that they will limit borrowing, reduce transfers in line with the savings targets, and control local government budgets consistent with the medium-term fiscal strategy.

- *State enterprises.* As the majority of called guarantees relate to the state-owned railroad operations, the restructuring in this sector will significantly reduce fiscal risks (below). In addition, to enhance transparency, the government has published financial statements of the largest loss-making enterprises on the web (ahead of the end-September structural benchmark).

10. **Preparations for the 2011 budget in line with the May program have started.** In light of the new Fiscal Management Law (Box 1), this will require preparation of consolidated budgets for the social security funds, extrabudgetary funds and local governments consistent with the program targets, so as to present to parliament, for the first time, the state budget and the general government budget position. Further, the government is reviewing the savings needs for 2011 that were agreed in May, to ensure the quality of the measures, secure their yield, head start their implementation, and formulate potential contingency measures.

Box 1. The Fiscal Management Law

Weak fiscal institutions, the absence of binding spending ceilings, and a lack of formal commitment controls have been at the root of the Greek fiscal deficit bias. The fiscal planning process has been only focused on the state budget (with most of the overruns occurring in other general government entities) and lacked a medium term context. Budget preparation has been divorced from macroeconomic and fiscal policies, and budget execution has lacked control on expenditure commitments. Moreover, the Ministry of Finance and Parliament have had no legal instruments to enforce budget discipline across the general government.

The Fiscal Management Law, passed in July and designed with FAD-led TA, overhauls the budget preparation, execution, and monitoring procedures to support the fiscal consolidation strategy and to enshrine fiscal discipline at the general government level. The new law introduces an annual rolling three-year fiscal and budgetary strategy for the consolidated general government; introduces top-down budgeting with medium-term expenditure ceilings for the state budget; introduces commitment controls to ensure spending is in line with budget ceilings; requires supplementary budgets for any overspending; establishes contingency reserves for unforeseen events; modernizes audits; and strengthens accountability and transparency including by creating a parliamentary budget office. Most elements of the new legislation will become effective for the preparation of the 2011 budget. Importantly, the new law extends budgeting and reporting obligations and commitments to all local governments, social security funds, and other entities.

The law also includes the principles to support fiscal consolidation after the government's current three-year program, which specifies annual fiscal targets, expires. It does so by including the general principles and basic elements for establishing a fiscal rule that could be introduced at a later stage. These principles emphasize comprehensive coverage, medium-term focus, transparency, and credibility, among others.

11. **Parliament approved a far-reaching pension reform in July** (Box 2). Preliminary estimates by staff indicate that the reform would lower the projected increase in pension spending in 2010–2050 from 12.5 ppts of GDP to 2.5–4.5 ppts of GDP, with the uncertainty reflecting pending adjustments to supplementary pension plans. The authorities are now shifting towards implementation to ensure a smooth transition to the new system within the tight deadlines of the reform. A full actuarial review of the effects of the reform was delayed by a few months due to staffing constraints and voluminous data requirements. Thus, the main priorities going forward are:

- **Quantifying the impact of the reform.** An actuarial review of the new pension system for the main pension funds is underway, to be completed by end-December 2010. This will be expanded to include the largest supplementary funds by end-March 2011. Allowing for EU peer review and to make adequate final parameter changes, any further adjustments to the main parameters of the system, as needed, will be completed by end-June 2011.
- **Addressing supplementary and welfare pensions.** Spending for these pension plans is about 1½ percent of GDP. Many of these plans are poorly funded and likely to face financial difficulties within the next 5–10 years. The authorities intend to do a full review of these plans in 2011 with the aim to reform the system by end-March 2012.

12. **Despite the good fiscal performance, budget liquidity remains tight, and this requires careful cash management.** Called guarantees and other stock-flow adjustments have raised the cash needs by at least €1.5 billion. To smooth the maturity profile and improve the T-bill market, the authorities plan to start monthly T-bill auctions beginning in September (from quarterly placements). This would allow smaller and more frequent placements, and provide more options for treasury management of domestic banks (who are primary investors). The authorities have no plans to return to the T-bond market any time soon.

Box 2. Pension Reform

Parliament has approved an overhaul of the pension system. The reform aims to ensure long-run sustainability of the retirement system, equalize rules across pension funds, increase labor force participation, and provide a safety net for the elderly. Key reform elements are:

- **Accrual rates/generosity:** The old system has different accrual rates across pension plans. The new law includes one profile of accrual rates for all workers, bringing these down from 2–3 percent a year to a much lower range of 0.80–1.50 percent a year, depending on the years of service. This measure simplifies the pension system and reduces costs. It creates incentives to participate longer as the accrual rate is progressive with working life.
- **Calculation of pensionable earnings:** The old system generally uses the top 5 years of the last 10 years of earnings as the pensionable base. The new law will use the full earnings history to calculate pensionable earnings.
- **Indexation of pensions:** The old system tends to adjust pensions with wage growth. The new system caps indexation at inflation.
- **Retirement age/years of contributions:** The old system often allows workers to claim full benefits before age 60. The new system sets the minimum age of retirement at 60 for all workers (men and women) by 2015; requires 40 years of contributions to receive full benefits; and reduces benefits by 6 percent a year for those who claim before age 65 without 40 years of contributions. In addition, the two anchors (60 and 65 years of age) are indexed to life expectancy going forward.
- **Arduous professions/disability verification:** The old system has a list of arduous professions including about a third of the labor force. The reform requires a revision of the list in 2011 to restrict the arduous classification to less than 10 percent of the working population. The new law also sets disability verification centers, establishes a register of individuals with disabilities, and allows for random checks to individuals claiming disability benefits.
- **Simplification:** the new law equalizes benefit formulas and retirement ages across all funds. Six pension funds remain: IKA (most wage and salary workers, including government employees and the military), OAEE (most self-employed workers), OGA (for the agricultural sector), ETAA (for lawyers, doctors, and engineers), ETAP-MME (journalists), and the fund of the BoG. Additionally, the new law separates pension funds from the health insurance component.
- **Compliance:** Under the new law, all transactions (contributions, benefit payments) to all social security bodies will be made through the banking system. The reform also establishes a pension audit system to cross-check beneficiaries using the social security number (AMKA). The reform also sets penalties for contribution evasion and conditions for the repayment of overdue contributions.
- **Monitoring:** starting 2011, the new law requires actuarial analysis of the pension system every two years; it also requires the Minister of Labor to brief the parliament on the finances of the social security system every six months.

Safeguard clause. The pension overhaul is far-reaching. The objective is to reduce the long-run increase in pension costs from 12½ ppts of GDP by 2060 under the old system to 2½ ppts of GDP under the new system. If the periodic actuarial evaluations show that the reform falls short, there is a provision in the new law that allows for a Ministerial Decision to adjust parameters of the system to achieve the final objective.

C. Financial Sector

13. **There was agreement that liquidity remains the immediate challenge.** Changes adopted by the ECB in the collateral valuation in the course of the summer have led, inter alia, to a decline of the value of the collateral assets submitted by Greek credit institutions. Furthermore, the amendments in the Eurosystem's risk control framework announced on 28 July 2010 (which will enter into force on 1 January 2011) could also further reduce the after-haircut value of some of the assets submitted as collateral. Moreover, some deposit losses continue and banks have increased interest rates to slow the outflow. In this context, to preserve adequate buffers, the authorities are preparing legislation to put in place a new tranche of guarantees for bank bonds for a total amount of €25 billion (a prior action for the first review). Such guarantees will ensure that the banks maintain a sufficient lending capacity, and will allow them to better withstand possible further market turbulence. In this regard, the authorities believe that continuation by the ECB of its SMP program is a desirable backstop. Banks are also taking initiatives to improve their liquidity positions, including selling some non-core assets and reducing their cost base. They have also opened a number of programs for covered bonds and restructured current ABSs to generate additional eligible collateral from their existing balance sheet assets.

14. **The Financial Stability Fund (FSF) has been formally approved to backstop capital needs.** On July 13 the Parliament enacted the Financial Stability Fund Law. This independent institution will be able to invest in viable banking institutions where capital has come under pressure and a private sector solution cannot be immediately found. In such a case, a restructuring process will take place under the lead of the FSF. The projected €10 billion for the financing of the FSF remains adequate. It is anticipated that the initial tranche will be disbursed to the FSF in September 2010. Other steps needed for the FSF to become fully operational by September are on course, including the appointment of board members, hiring staff, and premises.

15. **Banking supervision is being strengthened but additional efforts are needed.** Reporting requirements have heightened and reporting lags are being reduced. In view of a hiring freeze, staffing has not yet been increased for on-site inspections and off-site reviews. Progress in recruitment is becoming urgent, also taking into account the recently approved law on insurance companies which transfers supervisory oversight of insurance activities to the BoG. The authorities are considering ways to use a more flexible recruitment process that does not compromise on quality and does not increase net staffing.

16. **The government has commissioned an in-depth study on the strategic options for the banking sector** (Box 3). In this context, the authorities will request a preliminary due diligence analysis for the financial entities in which the state has a significant stake (which will be discussed at the time of the second review). The government, in consultation with the staff of the EC, the ECB and the IMF, will formulate a program to preserve financial stability and enhance efficiency in the banking system, taking into account the outcome of these reports.

17. **The authorities are also following up on the results of the July 2010 Committee of European Banking Supervisors (CEBS) stress tests.** The government has reaffirmed its full support to the state-owned ATE bank which did not pass the stress tests under the most stringent scenario. Priority will be given to the implementation of a comprehensive restructuring plan (by end-September) as required for institutions that have received significant amounts of state aid. In addition, pending the outcome of the due diligence, the bank has been instructed to implement a set of interim restructuring measures under the close oversight of the BoG with a view to containing costs and risks.

18. **The BoG continues to maintain close coordination with home and host country supervisors.** Regular communications with regulators in Southeastern Europe regarding risk assessments and liquidity contingency plans have intensified, while participation in colleges of supervisors continues.

19. **The authorities have also made good progress on their other commitments under the MEFP.** In this respect, the personal insolvency law has been adopted after it was amended in line with ECB recommendations to ensure that creditor's rights are adequately protected. The special law establishing an emergency corporate insolvency framework (facilitating the restructuring of debt) has expired and it has not been extended, a step welcomed by the banking industry.

Box 3. Reforming State-controlled Banking Entities

The government still controls a significant share of the banking sector in Greece. It holds a majority (77 percent) of the capital of ATE Bank (Agricultural Bank of Greece) which has a 7.3 percent share of the system's assets (as of end-2009), and is the controlling shareholder (33 percent of the capital) of the Hellenic Postbank which has a 4.1 percent share of the system's assets (as of end-2009). Through their participations, the government has also control or a key influence over two smaller banks. In addition, the Consignment Deposits and Loans Fund, a non-bank government institution with €6.6 billion of assets, competes with banks for deposits and extends loans to civil servants and public entities. Finally, through share ownership by pension funds, the state also participates indirectly in the National Bank of Greece (NBG) and the government normally appoints the NBG CEO. Total market share of banks in which the state has a direct controlling share (excluding NBG) exceeds 11 percent.

Significant unresolved challenges beset state-controlled banking entities. ATE Bank has an established history of extending loans that are not repaid and are eventually written-off, triggering the need for recurrent government recapitalization. It is facing this situation again now, and was the only Greek bank that failed the most severe scenario in the July 2010 CEBS stress-test. The Consignment Fund lacks appropriate controls, and has no proper mechanism to manage the liquidity and interest rate risks associated with its banking activities. Without access to ECB facilities or the interbank market, it tends to keep deposit interest rates high, thus distorting the market, albeit to a limited extend so far due to its small size and sparse network of branches.

The government has selected a coherent and comprehensive approach to resolving these problems:

- **Fact finding** by independent consultants will be completed by mid-September. The government has commissioned a strategic review of the future of the Greek banking system and the State's involvement. In addition, a preliminary targeted due diligence will be prepared for the banks with a material size in which the government has control or significant influence. The purpose will be to assess the economic value of the entities under review.
- **A reform program**, including all government interest in banking activities, will be defined after the fact finding. It will aim at preserving financial stability, by addressing pending issues in the weaker institutions, and at improving efficiency. It may include the possible sale of a significant part of the government interests in banking entities, in an open and transparent process, in line with national and EU rules, in which both domestic and international investors will have the opportunity to participate. This program approval date will be discussed at the time of the second review.

D. Structural Reform Policies and Data Reporting

20. **Labor market reform is underway.** Substantive legislative changes were introduced in July ahead of schedule (Box 4) to reduce labor-market distortions. These lowered employment protection restrictions and will increase the adjustment capacity of firms, ultimately boosting employment. As authorities view wage moderation as a critical component to regain competitiveness, further measures will be taken by end-September to reform collective bargaining. This will be important to ensure wage increases commensurate with productivity.

Box 4. Labor Market Reform

The authorities are implementing a comprehensive labor market reform in two steps. First, legislation was adopted in July to address institutional rigidities like dismissal costs, and facilitate labor market entry. Key elements are:

- **Minimum wage.** To facilitate youth entry into the labor market, the government has introduced a sub-minimum wage for newly-hired employees younger than 25— the gross wage for employers will be 84 percent of the wage level established in the National General Collective Labor Agreements (NGCLA). Employees' take-home pay will nevertheless remain unchanged as the Manpower Services Organization will cover their social security contributions. One-year apprenticeship contracts have been introduced for workers between 15 and 18 years old, which will pay 70 percent of the minimum wage.
- **Employment protection legislation.** Severance costs for white-collar workers, which traditionally have been higher than for blue-collar works, are reduced substantially through the shortening of the notification period (e.g. for an employee working 28 years or more, notification is reduced from 24 months to 6 months). As a result, the gap in severance costs between white-collar and blue-collar workers is cut by 20 percent although it is still high by European standards.
- **Collective dismissals.** Firing restrictions have been relaxed for all firms subject to collective dismissal rules. For firms with more than 600 employees, the maximum number of lay-offs per month has been increased from 12 up to 30 people.

Institutional changes relating to collective bargaining and arbitration procedures will be adopted by end-September 2010, with the aim of improving the link between wages and productivity. The reform will conform with the following principles:

- **Collective bargaining.** Wage *levels* established in the NGCLA are no longer a minimum requirement for occupational, sectoral or firm-level agreements as a result of legislation approved in May. The favourability principle will be abolished and assurances put in place to ensure that firm-level agreements will prevail over other levels of collective agreement. Finally, the automatic extension of sectoral or occupational agreements to those not represented in the negotiations will be eliminated.
- **Arbitration.** In the case of differences between employers and employees over sectoral or occupational agreements, the current system only grants recourse to arbitration to labor unions, thereby making wage moderation outcomes more difficult. The arbitration system will be amended so that both employees and employers can resort to arbitration if mediation fails, without exception regarding subject or coverage. The new system will operate according to transparent objective criteria and with an independent committee of arbitrators with no government representatives.

21. **Efforts are underway to increase competition and remove restrictions, including in the transport sector.** There was agreement that these reforms are particularly important for an early supply response.

- **Business entry.** Start-ups will be facilitated by making fully operational the general electronic commercial registry (GEMI), adequately equipping one-stop shops, and eliminating unnecessary fees (by end-December). On licensing, legislation will be adopted to simplify and accelerate the authorization (by end-December).

- **Hellenic Competition Committee (HCC).** The government will amend the Greek Competition Act to strengthen the independence of the HCC through the Parliamentary approval of the HCC president and its members (by end-December). The effectiveness of the HCC will also be enhanced by enabling it to prioritize cases and to undertake policy advocacy on its own initiative, and by strengthening the appeals system.
- **Services and closed professions.** The authorities will pursue an ambitious implementation of the Services Directive. To this aim, a comprehensive review of up to 160 technical occupations under the jurisdiction of the General Secretariat for Industry is being conducted, with emphasis on removing licensing obstacles and other entry barriers. A draft framework law should be ready by October 2010. Pervasive restrictions to entry in a number of important professions impose high costs on the economy. As a first step, the government will liberalize entry in the legal, pharmacy, notary, architecture, engineering, and auditing professions. This will include reducing licensing requirements, geographic restrictions and regulated tariffs (by end-December).
- **Transportation.** The draft law on the revocation of cabotage—to be ratified by the Parliament shortly—will allow non-EU flagged vessels to perform cruises departing/arriving at Greek ports. Moreover, the government will approve legislation to remove restrictions and liberalize prices in road freight by end-September (Box 5).
- **Tourism and retail.** The government will commission a report analyzing obstacles to development of the tourism and retailing sectors, and follow up with a time-bound action plan. As retail inefficiencies contribute significantly to inflation, an electronic price observatory has been created within the General Secretariat of Commerce to regularly evaluate price formation practices. When possible anti-competitive practices are identified, cases will be submitted to the HCC for further examination.

Box 5. Road Freight Reform

Freight transport in Greece has been regulated since the 1970s, with the government setting minimum tariffs and granting licenses to haulage operators. Distortions arising from government intervention include: (1) high-price, low-quality transportation services, encouraging firms to internalize transport activities; (2) large private rents accruing to incumbents; (3) lack of incentives for investment in the sector, characterized by poor technological innovation and productivity performance; and (4) excessive fragmentation and low utilization of economies of scale, which would have prevented Greek haulers from developing a wider chain of logistics services and taking their market share on the EU transport market. No new licenses have been sold since the 1970s.

The far-reaching liberalization of road haulage, scheduled to be passed by end-September, is expected to generate substantial efficiency gains. Main elements of the reform are:

- **Elimination of quantitative licensing restrictions:** The granting of licenses will be automatic upon meeting the objective criteria set by the law, namely certificates of professional qualifications, tax clearance and social security certificates, and criminal record copies.
- **Price of the licenses during the transition period:** During a transition period of 2.5 years, new entrants will be required to pay an entry fee equal to the “goodwill” of existing licenses, whose value is acknowledged by the government as “an element of the right of property”. The value of the entry fee will decrease at the rate of 30 percent in 2011, and 35 percent in 2012 and 2013. After 2013 the fee shouldered by the new entrants will exclusively cover administrative costs.
- **Freedom to negotiate cargo fares:** Administratively set prices for general cargo are abolished, but not for oil fuel, where the administration can still set maximum prices.

22. **The government will facilitate private investment including through the privatization program** (Box 6). Opening up private investment, including FDI, can generate short-term growth benefits, without burdening the budget. A number of reforms are underway:

- **Structural funds.** Use of state aid to sustain inefficient companies will be gradually cut. The government will adopt legislation to tackle delays of public works. A task force has been established with authority to overcome implementation bottlenecks and ensure a timely delivery of high-quality programs.
- **Network industries.** An enabling law to restructure the railway sector will be discussed in parliament by end-September and, in parallel, the government will approve a business plan with time-bound actions, including on cost-recovery tariffs, reduced payroll expenses, and closure of unprofitable lines. The government will also enable the effective liberalization of the wholesale electricity market and proceed with the rationalization of tariffs while ensuring that vulnerable groups are protected.
- **Other state-owned enterprises.** Privatization as a means to boost domestic and foreign direct investments to enhance growth could be particularly important in the

transportation sector—ports and regional airports are potential candidates—where Greece could consolidate its potential as a hub for Southeastern Europe. Thus, a list of privatization projects has been identified and is awaiting a fully elaborated plan to be prepared before end-December.

Box 6. Public Enterprises and Privatization

SOEs are a source of fiscal risk, which the authorities are beginning to address. The ten largest loss-making SOEs had combined losses of around 0.7 percent of GDP in 2009. The bulk of these losses is concentrated in the railway sector (60 percent), the Athens public transport system (25 percent), and in the defense sector (11 percent). In addition, loss-making SOEs are a main recipient of guarantees, which are regularly called, and investment in some of these companies is also in part conducted directly through the public investment budget.

The authorities have initiated two significant SOE reforms, to be completed by end-2010:

- **A privatization program has been announced but needs further elaboration.** The program covers the telecom, utility, transportation, real estate, and gaming sectors. Privatization will be conducted mostly through concession agreements, with outright sales and IPOs playing a smaller role. For 2011, a preliminary list of privatization projects (mainly in the gaming industry and through the extension of concessions) has been identified that could yield savings exceeding €1 billion. Elaboration of a full-fledged privatization plan is expected by end-December (structural benchmark).
- **The railroad sector is being restructured.** The reform aims to make the now loss-making train operator (TRAINOSE) viable and prepare for a possible combination with a strategic partner. A draft bill for the restructuring of TRAINOSE is being prepared, involving the unbundling of the operator and the infrastructure manager, limiting subsidies from the state against an assumption of debts, and reducing costs through higher tariffs, suspension of loss-making routes, and lower personnel costs.

23. **The authorities are improving data quality:**

- **Fiscal reporting.** While below-the-line fiscal reporting for non-state entities is ready to start in September, a questionnaire has also been launched to collect above-the-line fiscal outcomes. The authorities are now working on strengthening the response rate and reporting quality to switch to above-the-line reporting by year's end. Reconciliation for first quarter below-the-line cash data and ESA95 survey accrual data revealed limited differences for social security funds, with challenges in local government and extra-budgetary fund reporting remaining.
- **ELSTAT.** The President of the newly independent Statistical Office (ELSTAT) and other members of the board of directors have been appointed. MoUs between ELSTAT and the main data providing institutions (i.e. GAO, BoG, Ministry of Interior, Ministry of Labor and Social Security, and Ministry of Health) are closed to

completion. These will serve as a preparatory step for the regulations of statistical obligations (benchmark for end-December). Also, major work is underway to update the registry of public agencies, enterprises, and organizations which will help improve data coverage of the public sector.

III. PROGRAM MODALITIES AND SAFEGUARDS ASSESSMENT

24. **The attached Letter of Intent, Memorandum of Economic and Financial Policies and annexed tables, and the Technical Memorandum of Understanding (TMU) describe the authorities' progress in implementing their economic program** (LOI and MEFP ¶¶1–24, and MEFP Tables 1–2). The program's performance criteria and structural benchmarks remain as specified in May. The TMU has been modified to improve clarity in some definitions, and increase coverage of the program's fiscal deficit targets so that they mirror more closely the general government deficit on an ESA95 accrual basis to be applicable from 2011 onwards. No changes are proposed to the level of access or the schedule of purchases.

25. **The first safeguards assessment of the Bank of Greece (BoG) with respect to SBA approved in May 2010 was finalized on August 16, 2010.** The assessment found a well established safeguards framework at the central bank. The BoG adopted the relevant guidelines and good practices promulgated by the European Central Bank, its financial statements are independently audited and the results are published. The BoG has initiated reforms to strengthen its internal audit function, and an independent audit committee is being established. The assessment recommended a few measures to further enhance the financial reporting and audit mechanisms.

IV. STAFF APPRAISAL

26. **Staff's overall assessment is that the program has made a strong start.** The end-June quantitative performance criteria have been met, led by forceful implementation of the fiscal program, and major reforms are ahead of schedule. However, important challenges and risks remain.

27. **The ambitious fiscal consolidation program remains on track, but pressure points are evident.** The vigorous implementation of the fiscal program—not least the determination to under-spend at the state level in order to offset shortfalls at sub-national level—is much welcome. Staff projections suggest that continued under-execution of discretionary state budget spending, by €4 billion at year-end, is necessary to ensure that the end-December targets are met. Staff shares the authorities' assessment that this is possible, and that additional fiscal measures are not warranted at this juncture. However, such under-execution can only be a stop-gap measure until more fundamental fiscal reforms—improved expenditure control and tax administration, take hold.

28. **The program’s credibility hinges critically on improving tax compliance.** The government appears determined, but is likely to be fiercely tested by an entrenched and pervasive culture of tax evasion and opposition from within the tax service. Progress is bound to be gradual, but a determined pursuit of tax evaders through the presumptive tax mechanism and through the work of the task forces pursuing high-income individuals is essential. Without improved compliance, restoring fiscal sustainability will likely require additional hikes in tax rates and painful expenditure cuts in the coming years. With concerns about the fairness of the distribution of the burden of adjustment already evident, this would greatly risk the broad social and political support that is essential to the success of the program.

29. **Improving expenditure controls at sub-national levels of government is another important challenge.** The problems here are not unexpected considering institutional weaknesses and the extensive past recourse to guaranteeing borrowing by state enterprises. The sweeping reform of local governments now in place is likely to entail significant savings. But while a new (“golden”) rule limiting municipalities’ capital expenditure is sound, it could still allow a rise in total expenditure inconsistent with overall general government targets. The government should seek agreement with the new municipal governments to ensure that this does not happen. The strengthening of financial control and procurement in the health sector is also important. This sector is a main source of spending pressures, and efforts to improve its financial discipline must continue. As to state enterprises—for instance, the railways—a planned transfer of debt to the budget and a requirement that subsidies be included in the state budget will—by improving transparency—facilitate informed decisions about public spending. This must, however, be accompanied by reforms to ensure that these enterprises become financially sound.

30. **Restoring competitiveness and boosting growth are critical to the program’s success.** Competitiveness risks are highlighted by the jump in domestic inflation and tardy adjustment in the external current account. Looking forward, the focus therefore now naturally begins to shift from the immediate challenge of regaining fiscal control to the many areas of the real economy requiring deep reform. The adoption of far-reaching pension and labor market reforms ahead of schedule augurs well for the government’s determination to undertake difficult reforms. Indeed, the pension reform might be among the most ambitious undertaken by any country in one step. Substantive labor market reform is also underway. This has clearly impressed, in Greece and abroad.

31. **Looking forward, priority in structural reforms should be given to those that could start an early recovery in growth, competitiveness, and employment.** This points to liberalization of closed professions, deregulation, and the reduction in barriers to development of the tourism and retail sectors, where the growth potential appears to be particularly large. Consideration should also be given to strengthening the privatization program, which right now has a somewhat timid role in the government’s overall strategy. In some of these high-potential areas, resistance from entrenched vested interests is likely to be

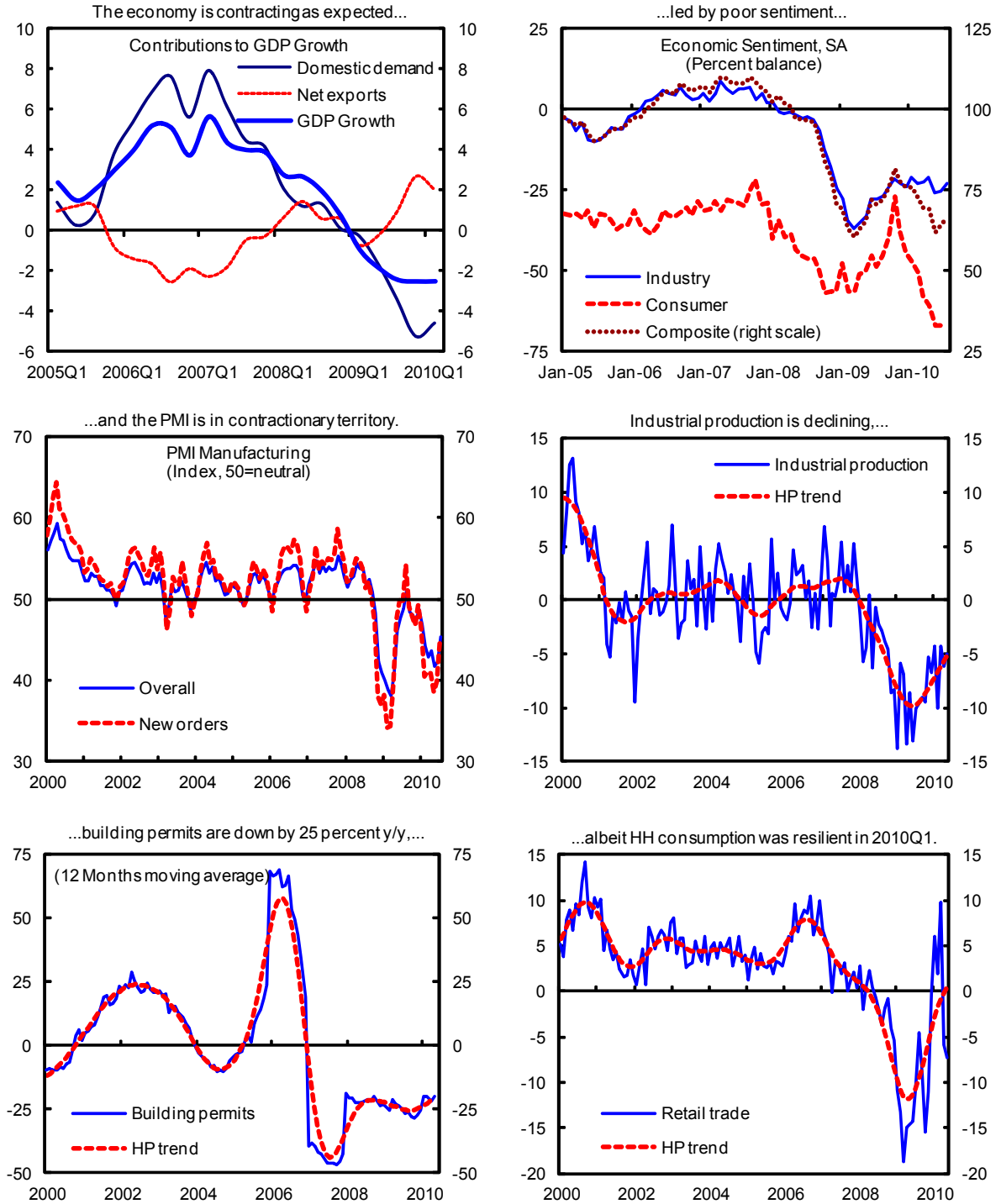
fierce; important political efforts should first and foremost be focused here. In this regard, the government's determination to persevere with a strongly-contested reform of road haulage has sent an important signal of its determination to push ahead with reforms in other areas.

32. **The liquidity situation in the banking system is tight but manageable.** The ECB's Security Market Purchase Program has contributed importantly to safeguarding the banking system's liquidity by stabilizing prices for government bonds. Continuation of this program would be desirable as long as malfunctioning of the sovereign bond market persists. On the assumption that this program remains in place, and that the government's guaranteeing of €25 billion of bank bonds will significantly increase repo-eligible collateral, staff believes that banks will have sufficient liquidity in the coming months.

33. **Stress on banking system capital also remains manageable.** The CEBS stress test confirmed that the Greek banking system is relatively well-capitalized. With the FSF now in place, the authorities have the back-stop required to deal with capital shortfalls that might emerge as the recession takes its toll on banks' balance sheets. In this regard, staff believes that the €10 billion allocated by the authorities for the financing of the FSF remains adequate. As to state banks, due diligence is now underway. The formulation of a comprehensive strategy for these banks must be a key objective for the coming months, starting with a plan for ATE Bank—the single Greek bank which failed the stress test.

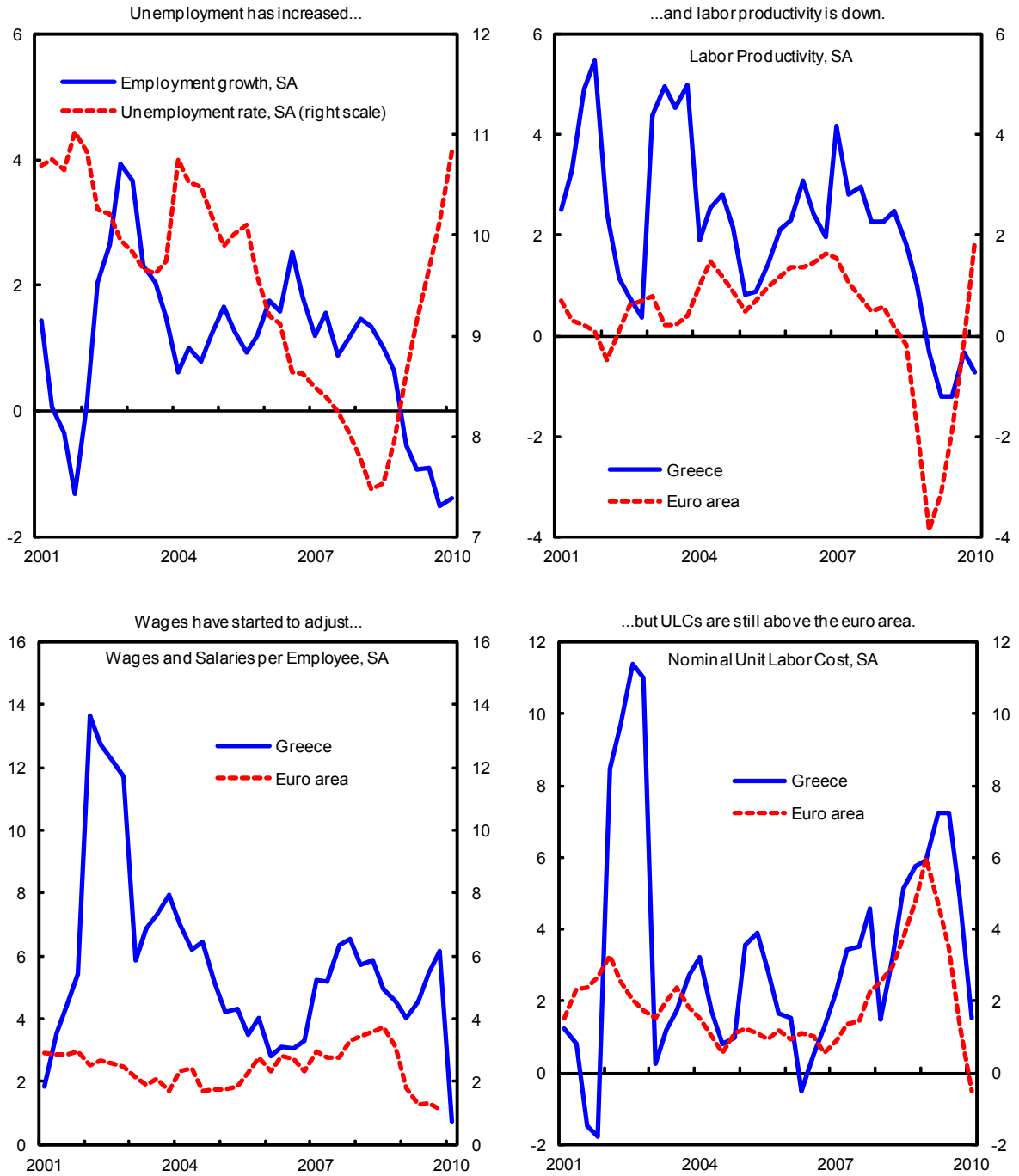
34. **Overall, the program is off to an impressive start.** This is fully in line with the high expectations expressed by the international community when agreeing to the extraordinary financial support package. A disappointment so far has been that, at this defining moment for Greece, the economic reforms have not had broader support from other political parties. While most of the difficult reforms still lie ahead, developments during this early phase of the program augur well for the government's determination to press ahead. Staff fully supports the conclusion of the review.

Figure 1. Greece: Selected Indicators, 2000–10
(Year-on-year percent change, unless otherwise indicated)



Sources: National Statistical Service; Eurostat; and IMF staff calculations and estimates.

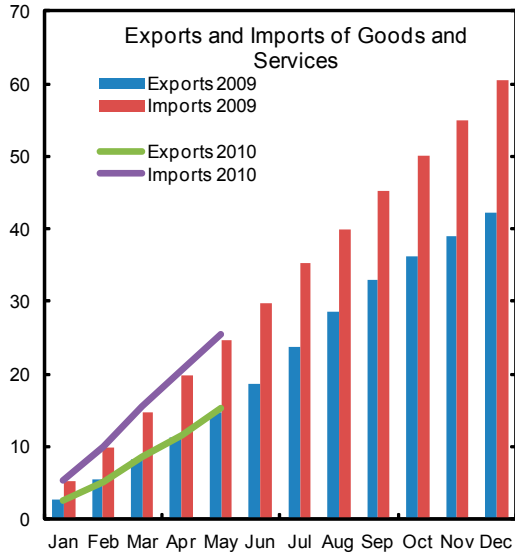
Figure 2. Greece: Labor Markets, 2001--10
(Year-on-year percent change, unless otherwise indicated)



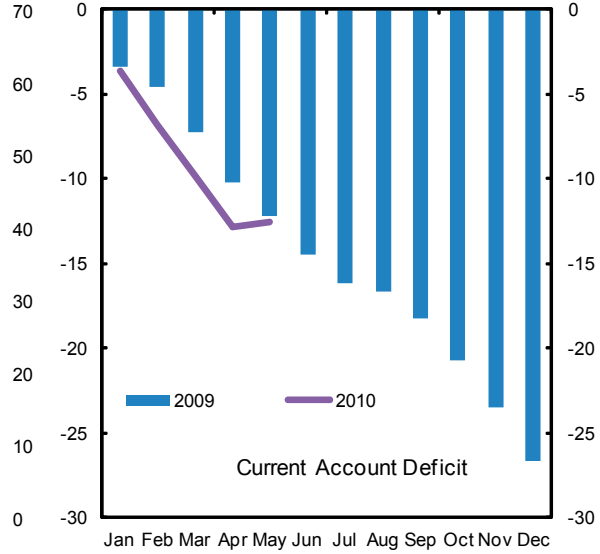
Sources: Eurostat; and IMF staff calculations.

Figure 3. Greece: Balance of Payments
(Billions of Euros, cumulative for beginning of the year)

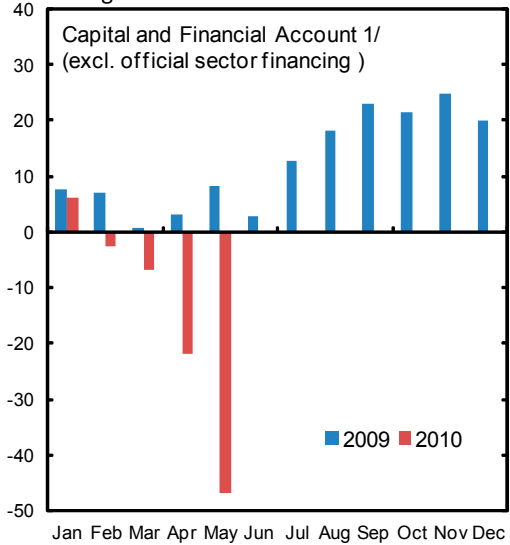
Exports and imports have trended similarly as in 2009 so far ...



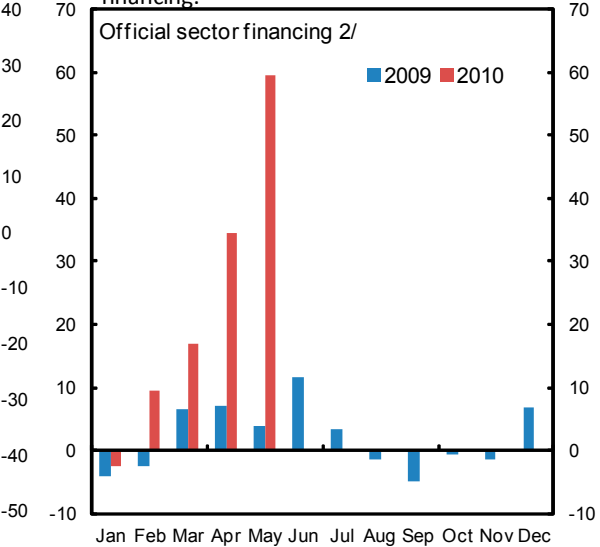
...resulting in little improvement in current account deficit .



Private sector financing turned sharply negative...



...offset by significant increase in official financing.

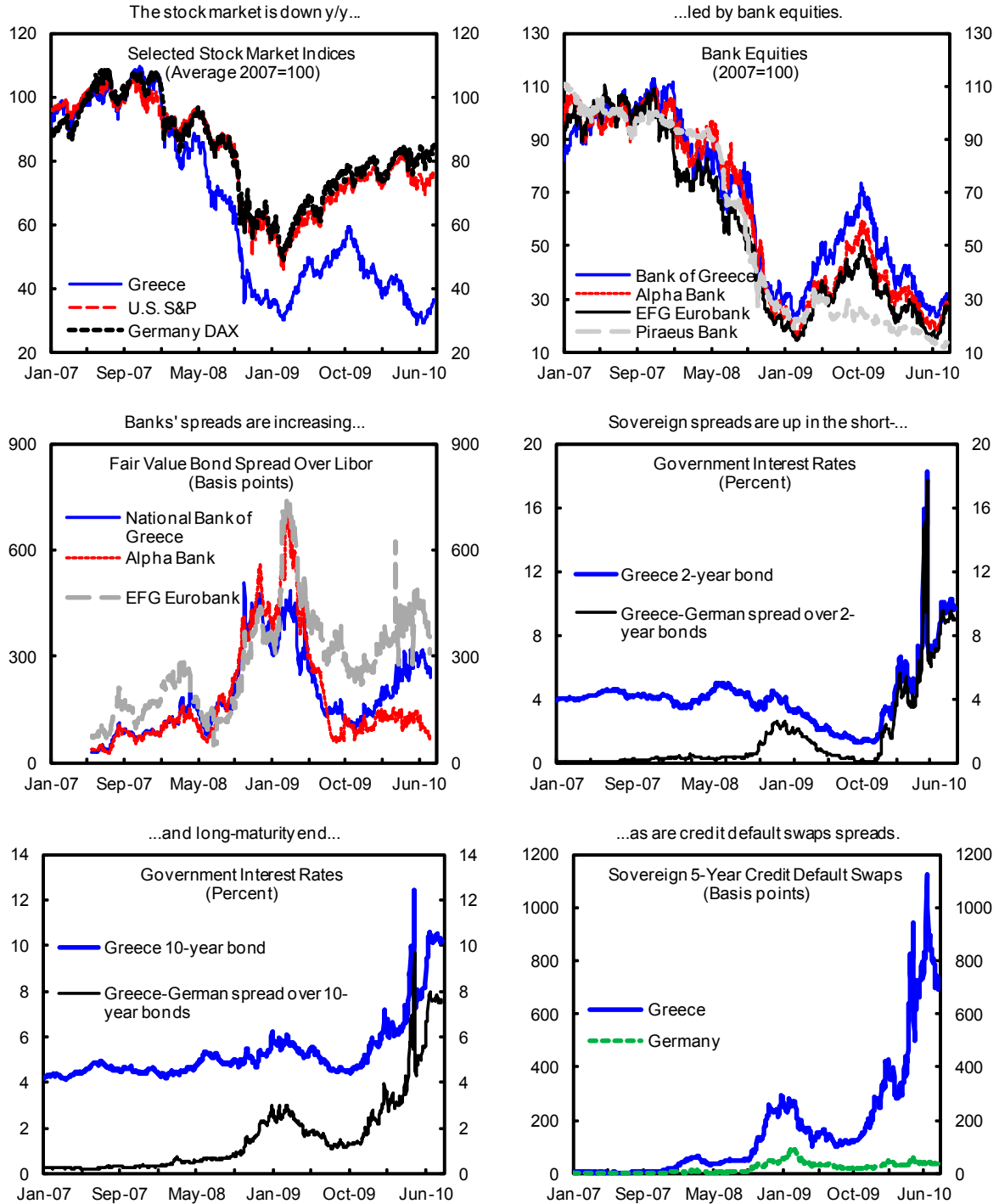


Sources: Bank of Greece; and IMF staff calculations.

1/ Includes errors and omissions.

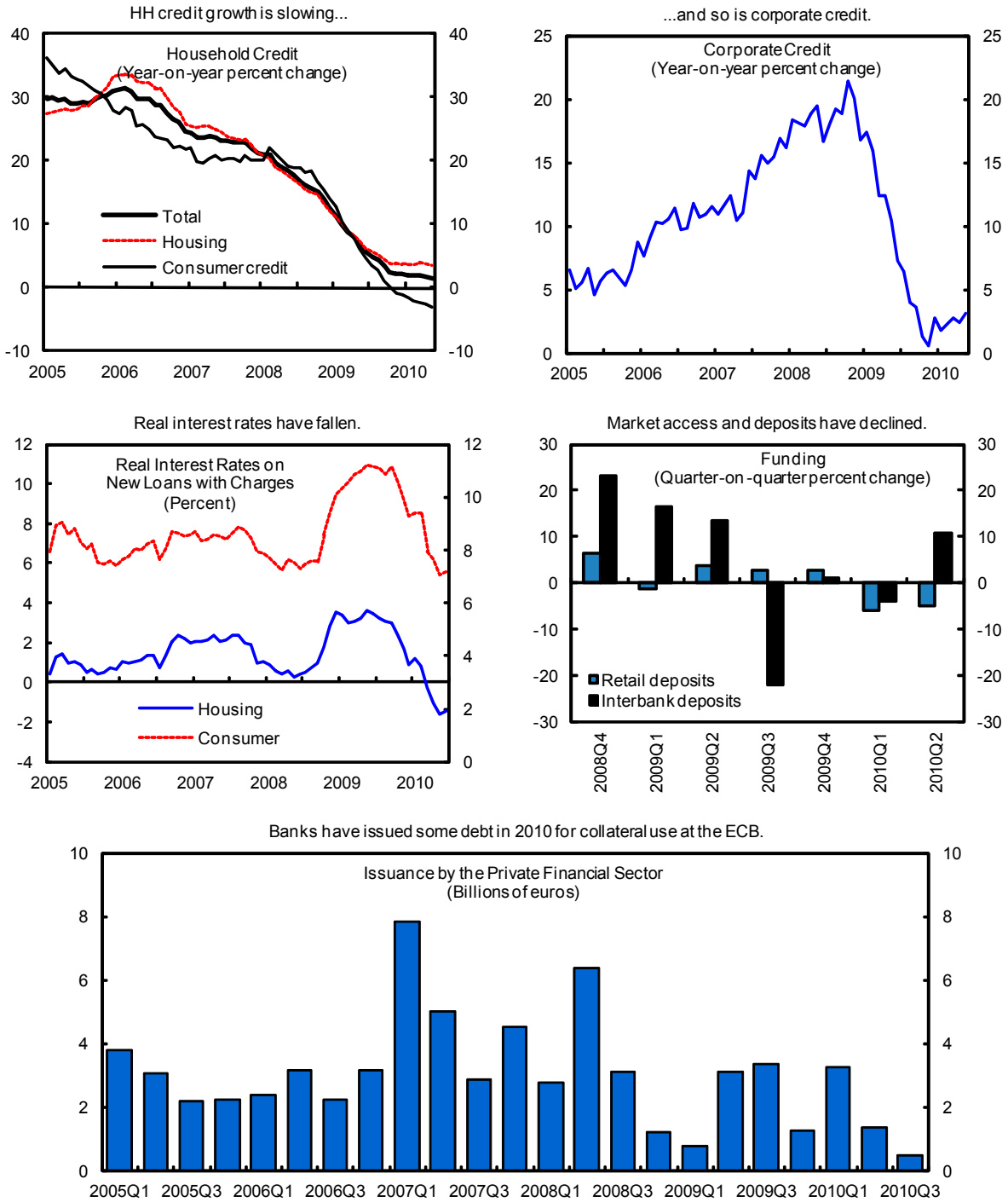
2/ Official sector financing includes loans to government and changes in BoG (ECB) credit to the banking system.

Figure 4. Greece: Financial Indicators, 2007–10



Sources: Bloomberg; and Moody's Creditedge.

Figure 5. Greece: Money and Banking Indicators, 2005–10



Sources: National Statistical Service; Bank of Greece; Bloomberg; ECB; and IMF staff calculations.

Table 1. Greece: Selected Economic Indicators

	2009	2010	2010	2011	2012	2013	2014	2015
		Program				Proj.		
(Percentage change, unless otherwise indicated)								
Domestic economy								
Real GDP	-2.0	-4.0	-4.0	-2.6	1.1	2.1	2.1	2.7
Output gap (percent of pot. output)	4.0	-1.1	-1.1	-4.7	-4.7	-4.0	-3.7	-3.1
Total domestic demand	-2.4	-7.1	-6.5	-5.3	0.2	1.7	1.8	2.1
Private consumption	-1.8	-4.0	-3.0	-3.9	0.7	2.8	2.5	2.5
Public consumption	9.6	-10.6	-10.6	-5.1	-3.0	-6.6	-3.2	-0.1
Gross fixed capital formation	-13.9	-11.4	-12.0	-11.7	0.9	4.8	3.4	2.2
Change in stocks (contribution)	0.0	-1.0	-1.0	0.0	0.0	0.0	0.0	0.0
Foreign balance (contribution)	0.7	3.8	3.3	3.1	0.9	0.4	0.2	0.5
Exports of goods and services	-18.1	4.5	3.0	5.5	5.9	6.0	5.9	6.0
Imports of goods and services	-14.1	-9.7	-8.6	-6.4	1.6	3.8	4.6	3.7
Unemployment rate (percent)	9.4	11.8	11.8	14.6	14.8	14.3	14.1	13.4
Employment	-1.4	-2.6	-2.6	-3.2	-0.2	0.7	0.3	0.9
Consumer prices (HICP), end of period	2.6	1.0	4.4	1.4	-0.3	0.8	1.2	1.0
Consumer prices (HICP), period average	1.3	1.9	4.6	2.2	0.5	0.7	1.0	1.0
Core prices, period average 1/	2.3	1.4	2.9	...	...	...	...	...
GDP deflator	1.4	1.2	3.5	1.3	0.4	0.7	1.0	1.1
(Percent of GDP)								
Balance of payments								
Current account	-11.2	-8.4	-10.8	-7.8	-6.9	-6.0	-5.1	-4.0
Trade balance	-7.6	-3.5	-7.1	-3.9	-3.0	-2.2	-1.4	-0.5
Export of goods and services	17.8	21.1	19.0	21.0	22.3	23.4	24.5	25.4
Imports of goods and services	25.4	24.6	26.2	24.9	25.3	25.6	25.8	25.9
Total transfers	0.5	0.4	0.3	0.3	0.3	0.4	0.3	0.5
Net income receipts	-4.1	-5.2	-4.0	-4.1	-4.2	-4.1	-4.1	-4.0
Net international investment position	-86	-95	-96	-104	-108	-110	-111	-110
Public finances (general government)								
Total revenues 2/	36.9	40.0	39.5	39.2	38.2	38.0	36.6	35.7
Total expenditures 2/	50.4	50.5	47.4	50.5	50.7	50.9	48.8	47.2
Primary expenditures 2/	45.4	44.9	41.8	43.9	43.4	43.1	40.7	39.4
Measures (cum.) 3/	...	2.5	...	3.9	6.2	8.1	9.8	9.5
Overall balance	-13.6	-8.1	-7.9	-7.3	-6.2	-4.7	-2.5	-2.0
Primary balance	-8.6	-2.4	-2.2	-0.8	1.0	3.0	5.7	5.9
Gross debt	115	133	130	139	144	144	139	134
Interest rates and credit								
Long-term lending interest rate 4/	5.7	...	6.1	...	...	...	...	...
Private credit growth 4/ 5/	4.2	...	2.8	...	...	...	...	...
Exchange rates								
Nominal effective exchange rate 6/	0.6	...	-4.2	...	...	...	...	...
Real effective exchange rate (CPI-based) 6/	1.7	...	-1.2	...	...	...	...	...
Memorandum item:								
Nominal GDP (billions of euros)	237	231	236	233	236	243	251	260
Nominal GDP (percentage change)	-0.7	-2.8	-0.6	-1.3	1.5	2.8	3.1	3.8

Sources: National Statistical Service; Ministry of Economy and Finance; Bank of Greece; and IMF staff estimates.

1/ Core prices exclude energy, food, alcohol, and tobacco. Data for 2010 refer to May.

2/ Excluding unidentified measures.

3/ Measures fully identified up to 2013.

4/ As of May 2010.

5/ Domestic credit growth of households and enterprises.

6/ As of June 2010.

Table 2. Greece: General Government Operations, 2009–15 1/

	2009	2010	2010	2011	2012	2013	2014	2015
	Program		Projections					
	(Euro billions)							
Revenue	87.5	93.5	93.3	91.3	90.3	92.4	91.7	93.0
Taxes on production, and imports	26.4	32.0	31.3	31.6	30.6	31.7	33.3	34.5
Taxes on income, and property	18.8	18.3	18.6	17.3	17.2	17.7	18.5	19.0
Social contributions	30.4	29.1	29.6	28.6	28.5	28.7	29.1	29.7
Other	8.8	9.1	9.2	8.9	9.0	9.3	9.6	9.9
Capital transfers	3.1	5.0	4.5	5.0	5.0	5.0	1.2	0.0
Primary expenditure	107.9	99.1	98.6	102.3	102.7	104.7	102.0	102.6
Wages	29.5	26.9	26.9	26.5	26.1	25.7	25.5	26.1
Social benefits	48.8	47.9	47.9	50.4	51.6	52.8	54.2	55.6
Goods and services	14.5	11.0	12.2	11.9	11.5	12.6	11.7	11.8
Subsidies	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3
Other current	3.9	3.7	3.7	3.8	3.8	3.8	3.9	3.9
Capital	10.9	9.4	7.7	9.5	9.4	9.5	6.4	4.9
Measures, cumulative 2/	...	...	...	9.2	14.8	19.7	24.5	24.8
Primary balance	-20.4	-5.6	-5.3	-1.8	2.4	7.4	14.2	15.2
Interest payments	11.9	13.0	13.3	15.2	17.1	18.9	20.4	20.3
Overall balance	-32.3	-18.6	-18.6	-17.0	-14.7	-11.5	-6.2	-5.1
Gross debt (Maastricht)	273.5	307.5	307.5	324.6	339.4	350.0	349.5	348.7
	(Percent of GDP)							
Revenue	36.9	40.5	39.5	39.2	38.2	38.0	36.6	35.7
Taxes on production, and imports	11.1	13.9	13.2	13.6	12.9	13.0	13.3	13.3
Taxes on income, and property	7.9	7.9	7.9	7.4	7.3	7.3	7.4	7.3
Social contributions	12.8	12.6	12.6	12.3	12.1	11.8	11.6	11.4
Other	3.7	4.0	3.9	3.8	3.8	3.8	3.8	3.8
Capital transfers	1.3	2.2	1.9	2.1	2.1	2.1	0.5	0.0
Primary expenditure	45.4	42.9	41.8	43.9	43.4	43.1	40.7	39.4
Wages	12.4	11.7	11.4	11.4	11.0	10.6	10.2	10.0
Social benefits	20.5	20.8	20.3	21.6	21.8	21.7	21.6	21.4
Goods and services	6.1	4.8	5.2	5.1	4.9	5.2	4.7	4.5
Subsidies	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Other current	1.6	1.6	1.6	1.6	1.6	1.6	1.5	1.5
Capital	4.6	4.1	3.2	4.1	4.0	3.9	2.5	1.9
Measures, cumulative 2/	...	...	...	3.9	6.2	8.1	9.8	9.5
Primary balance	-8.6	-2.4	-2.2	-0.8	1.0	3.0	5.7	5.9
Interest payments	5.0	5.6	5.6	6.5	7.2	7.8	8.1	7.8
Overall balance	-13.6	-8.1	-7.9	-7.3	-6.2	-4.7	-2.5	-2.0
Gross debt (Maastricht)	115.2	133.3	130.3	139.4	143.6	144.0	139.5	134.0
Memorandum items:								
Overall balance (prog. definition, € billions)	...	-18.6	-17.3	-17.2	-14.7	-11.5	-6.2	-5.1
Nominal GDP (€ billions)	237.5	230.8	236.1	232.9	236.4	243.0	250.6	260.2

Source: Greek authorities, and IMF staff estimates.

1/ ESA95.

2/ For 2010, measures are included in revenue and expenditure; for 2011 and beyond, they are reported separately.

Table 3. Greece: Public Sector Financing Requirements and Sources
(Billion of euros, unless otherwise stated)

	2009	2010	2010	2011	2012	2013	2014	2015
		Program			Projections			
Gross borrowing need	68.6	73.6	73.6	55.2	57.9	53.2	70.8	76.7
Overall balance	34.4	20.7	20.7	18.7	16.2	12.8	7.2	5.9
Amortization	29.7	37.4	37.4	35.3	40.5	34.1	40.6	36.8
M<	20.3	31.3	31.3	27.3	32.5	26.1	32.6	28.8
Domestic banks	4.6	15.7	15.7	10.3	16.0	13.6	16.6	14.7
BOP	15.8	15.6	15.6	17.0	16.5	12.5	16.1	14.0
ST	9.4	6.1	6.1	8.0	8.0	8.0	8.0	8.0
Domestic banks	3.9	4.2	4.2	5.0	5.0	5.0	5.0	5.0
BOP	5.5	1.9	1.9	3.0	3.0	3.0	3.0	3.0
Exceptional creditors						6.1	28.6	38.9
EU						4.5	20.8	28.3
IMF						1.7	7.8	10.6
Other 1/	4.5	15.5	15.5	1.2	1.2	0.2	-5.6	-4.8
Gross financing sources	68.6	35.6	35.6	15.2	33.9	45.2	70.8	76.7
Privatization receipts	0.9	0.0	0.0	1.0	1.0	1.0	1.0	1.0
Other	6.0	2.1	2.2	1.9	1.6	1.3	-2.7	0.9
Market access	61.7	33.4	33.4	12.4	31.4	42.9	72.5	74.8
M< 2/	55.6	25.4	25.4	4.4	23.4	34.9	64.5	66.8
Domestic banks	7.5	15.6	23.8	8.3	13.6	10.9	13.9	12.1
BOP	48.1	9.8	1.6	-3.9	9.7	23.9	50.6	54.7
ST	6.1	8.0	8.0	8.0	8.0	8.0	8.0	8.0
Domestic banks	4.2	5.0	5.0	5.0	5.0	5.0	5.0	5.0
BOP	1.9	3.0	3.0	3.0	3.0	3.0	3.0	3.0
Financing gap		38.0	38.0	40.0	24.0	8.0		
EU (8/11 of the gap)		27.6	27.6	29.1	17.5	5.8		
IMF (3/11 of the gap)		10.4	10.4	10.9	6.5	2.2		
Net market access	32.0	-4.0	-4.0	-22.9	-9.2	8.8	31.9	38.0
Domestic banks	17.6	0.7	8.9	-2.0	-2.4	-2.6	-2.7	-2.6
M<	17.3	-0.1	8.1	-2.0	-2.4	-2.6	-2.7	-2.6
ST (net increase)	0.3	0.8	0.8	0.0	0.0	0.0	0.0	0.0
BOP	14.3	-4.7	-12.9	-20.9	-6.8	11.4	34.6	40.7
M<	32.3	-5.8	-14	-20.9	-6.8	11.4	34.6	40.7
ST (net increase)	-18.0	1.1	1.1	0.0	0.0	0.0	0.0	0.0
Rollover rates of existing debt, percent		89.4	89.4	35.0	77.4	125.7	178.6	203.5
Total Maastricht debt in billions of euros	273.5	307.5	307.5	324.6	339.4	350.1	349.5	348.7
Exceptional creditors		38.0	38.0	78.0	102.0	103.9	75.2	36.4
EU		27.6	27.6	56.7	74.2	75.5	54.7	26.4
IMF		10.4	10.4	21.3	27.8	28.3	20.5	9.9
percent of quota		1110	1109	2277	2978	3033		
Private sector	274	270	270	247	237	246	274	312
Total Maastricht debt (percent GDP)		133.3	130.3	139.4	143.6	144.0	139.5	134.0
Exceptional creditors		16.5	16.1	33.5	43.1	42.7	30.0	14.0
EU		12.0	11.7	24.4	31.4	31.1	21.8	10.2
IMF		4.5	4.4	9.1	11.8	11.7	8.2	3.8

Sources: Ministry of Finance; and IMF staffs projections.

1/ It includes bank assistance and stock-flow adjustments.

2/ It includes stock-flow adjustments.

Table 4. Greece: Summary of Balance of Payments, 2009–15

	2009	2010		2010	2010	2011	2012	2013	2014	2015	
	Prel.	Q1		Program			Projections				
		Proj.	Act.								
	(In billions of euros)										
Current account balance	-26.6	-7.1	-9.9	-19.3	-25.6	-18.0	-16.2	-14.5	-12.8	-10.5	
Balance of goods and services	-18.1	-4.4	-7.1	-8.2	-16.9	-9.1	-7.2	-5.3	-3.4	-1.4	
Goods balance	-30.8	-6.5	-8.2	-25.9	-30.6	-26.2	-26.2	-26.4	-26.7	-27.2	
Exports	15.3	4.2	3.6	17.8	16.0	17.4	19.0	20.7	22.3	24.0	
Imports	46.1	10.8	11.8	43.7	46.6	43.6	45.2	47.0	49.0	51.2	
Services balance	12.6	2.2	1.2	17.7	13.7	17.0	19.0	21.0	23.3	25.7	
Credit	27.0	5.3	4.9	30.9	29.0	31.4	33.7	36.2	39.0	42.1	
Debit	14.3	3.1	3.8	13.2	15.3	14.4	14.7	15.2	15.7	16.3	
Income balance	-9.8	-3.0	-2.1	-12.1	-9.5	-9.6	-9.8	-10.0	-10.2	-10.4	
Credit	4.1	1.2	1.0	4.7	4.3	4.3	4.3	4.3	4.3	4.4	
Debit	13.9	4.2	3.1	16.8	13.7	13.9	14.1	14.3	14.5	14.7	
Current transfers (net)	1.3	0.2	-0.7	1.0	0.7	0.7	0.8	0.9	0.9	1.3	
Capital and financial account balance	27.2	7.1	9.6	-18.7	-12.4	-22.0	-7.8	6.5	12.8	10.5	
Capital account balance	2.0	0.7	0.1	2.8	2.8	2.9	2.8	2.7	2.6	2.5	
Financial account	25.2	6.4	9.4	-21.6	-15.3	-24.8	-10.6	3.8	10.1	8.0	
Direct investment	1.1	-0.1	0.9	1.0	1.0	1.6	2.0	2.5	2.9	3.1	
Portfolio investment	27.9	1.2	4.9	-2.1	-10.3	-13.6	2.2	14.8	60.7	65.1	
<i>of which: government</i>	31.1	0.6	n.a.	-4.7	-12.9	-20.9	-6.8	5.3	50.6	54.7	
Other investment (excl. program financing)	-3.6	5.3	3.6	-20.4	-5.9	-12.8	-14.8	-13.5	-53.5	-60.2	
Reserve assets (increase = -)	-0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Net errors and omissions	-0.6	0.0	0.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Program financing	...	...	...	38.0	38.0	40.0	24.0	8.0	...	...
	(In percent of GDP)										
Current account balance	-11.2	-3.0	-4.2	-8.4	-10.8	-7.8	-6.9	-6.0	-5.1	-4.0	
Balance on goods and services	-7.6	-1.9	-3.0	-3.5	-7.1	-3.9	-3.0	-2.2	-1.4	-0.5	
Goods balance	-13.0	-2.8	-3.5	-11.2	-13.0	-11.2	-11.1	-10.8	-10.7	-10.4	
Services balance	5.3	0.9	0.5	7.7	5.8	7.3	8.0	8.6	9.3	9.9	
Income balance	-4.1	-1.3	-0.9	-5.2	-4.0	-4.1	-4.2	-4.1	-4.1	-4.0	
Current transfers	0.5	0.1	-0.3	0.4	0.3	0.3	0.3	0.4	0.3	0.5	
Capital and financial account balance	11.5	3.0	4.1	-8.1	-5.3	-9.4	-3.3	2.7	5.1	4.0	
Capital account balance	0.8	0.3	0.1	1.2	1.2	1.2	1.2	1.1	1.0	1.0	
Financial account	10.6	2.7	4.0	-9.3	-6.5	-10.7	-4.5	1.6	4.0	3.1	
Direct investment	0.5	0.0	0.4	0.4	0.4	0.7	0.9	1.0	1.2	1.2	
Portfolio investment	11.7	0.5	2.1	-0.9	-4.4	-5.8	0.9	6.1	24.2	25.0	
<i>of which: government</i>	13.1	0.2	n.a.	-2.0	-5.5	-9.0	-2.9	2.2	20.2	21.0	
Other investment	-1.5	2.3	1.5	-8.8	-2.5	-5.5	-6.3	-5.5	-21.4	-23.1	
Reserve assets (increase = -)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Net errors and omissions	-0.3	0.0	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Program financing	...	...	...	16.5	16.1	17.2	10.2	3.3	...	...
Memorandum items:											
Program financing (billions of euro)	...	...	...	38.0	38.0	40.0	24.0	8.0	...	...
EU	...	...	...	27.6	27.6	29.1	17.5	5.8	...	...
IMF	...	...	...	10.4	10.4	10.9	6.5	2.2	...	...
External debt	170.0	174.6	175.8	185.0	183.5	189.0	195.8	200.9	203.8	202.0	
Public sector	111.1	118.8	118.8	142.7	132.6	135.3	139.9	140.4	140.0	134.9	
Private sector	59.0	55.8	56.9	42.4	50.9	53.6	55.9	60.5	63.9	67.1	

Sources: Bank of Greece; and IMF staff estimates.

Table 5. Greece: External Financing Requirements and Sources, 2008-15

	(In billions of euros)								
	2008	2009	2010 Program	2010 Proj.	2011 Proj.	2012 Proj.	2013 Proj.	2014 Proj.	2015 Proj.
GROSS FINANCING REQUIREMENTS	122.9	167.1	186.1	176.1	180.1	164.6	167.2	198.8	220.3
Current account deficit	34.8	26.6	19.3	25.6	18.0	16.2	14.5	12.8	10.5
Medium- and long-term debt amortization	19.9	28.2	22.8	22.8	28.1	25.8	25.4	47.7	55.3
Public sector	14.6	15.8	15.6	15.6	17.0	16.5	18.7	44.7	52.9
Banks	4.5	11.3	6.8	6.8	8.7	9.1	4.8	2.5	0.5
Corporates	0.8	1.1	0.3	0.3	2.3	0.2	1.9	0.6	1.9
Short-term debt amortization	68.2	112.2	144.0	127.8	134.0	122.6	127.3	138.3	154.5
Public sector & BoG	12.0	40.8	50.9	50.9	76.3	59.3	57.7	54.8	58.5
BoG 1/	10.8	35.3	49.0	49.0	73.3	56.3	54.7	51.8	55.5
Public sector 2/	1.2	5.5	1.9	1.9	3.0	3.0	3.0	3.0	3.0
Banks	54.9	70.2	92.1	75.8	56.9	62.6	68.8	82.6	95.0
Corporates	1.3	1.3	1.0	1.0	0.8	0.7	0.8	0.9	1.1
SOURCES OF FINANCING	122.9	167.1	148.1	138.1	140.1	140.6	159.2	198.8	220.3
Capital account (net)	4.1	2.0	2.8	2.8	2.9	2.8	2.7	2.6	2.5
Foreign direct investment (net)	1.4	1.1	1.0	1.0	1.6	2.0	2.5	2.9	3.1
Inward	3.1	2.4	2.3	2.3	3.0	3.5	4.0	4.5	4.7
Equities (net)	-0.8	-0.2	-0.5	-0.5	-0.8	0.8	1.3	1.8	2.2
by nonresidents	-3.7	0.5	0.2	0.2	-0.1	1.5	2.0	2.5	3.0
Assets drawdown (- increase)	-30.1	-26.1	-7.2	-7.2	7.8	-12.2	-17.2	-17.2	-12.2
New borrowing and debt rollover	148.0	191.8	151.9	142.0	128.7	147.2	169.9	208.6	224.7
Medium and long-term borrowing	35.7	64.0	16.3	8.1	6.0	19.9	31.6	54.1	57.2
Public sector	25.6	48.1	9.8	1.6	-3.9	9.7	23.9	50.6	54.7
Banks	7.3	7.7	6.1	6.1	7.9	10.0	5.8	3.0	0.6
Corporates	2.9	8.2	0.3	0.3	2.1	0.2	1.9	0.6	1.9
Short-term borrowing	112.2	127.8	135.7	134.0	122.6	127.3	138.3	154.5	167.4
Public sector & BoG	40.8	50.9	84.2	76.3	59.3	57.7	54.8	58.5	57.0
BoG 1/	35.3	49.0	81.2	73.3	56.3	54.7	51.8	55.5	54.0
Public sector 2/	5.5	1.9	3.0	3.0	3.0	3.0	3.0	3.0	3.0
Banks	70.2	75.8	50.6	56.9	62.6	68.8	82.6	95.0	109.2
Corporates	1.3	1.0	0.8	0.8	0.7	0.8	0.9	1.1	1.2
Other	0.3	-1.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0
PROGRAM FINANCING	...	...	38.0	38.0	40.0	24.0	8.0	...	...
European Union (8/11 of total)	...	...	27.6	27.6	29.1	17.5	5.8	...	...
IMF (3/11 of total)	...	...	10.4	10.4	10.9	6.5	2.2	...	...
<i>in percent of quota</i>	...	...	<i>946</i>	<i>946</i>	<i>996</i>	<i>597</i>	<i>199</i>	...	...
Memorandum item:									
Greece IMF quota (SDR millions)	823.0	823.0	823.0	823.0	823.0	823.0	823.0	823.0	823.0
Greece IMF quota (Euro millions)	1,095.8	1,095.8	1,095.8	1,095.8	1,095.8	1,095.8	1,095.8	1,095.8	1,095.8

Sources: Bank of Greece, Bloomberg, and staff estimates and projections.

1/ Includes liabilities to Eurosystem related to TARGET.

2/ Includes market instruments and trade credits.

Table 6. Greece: Core Set of Financial Soundness Indicators for Deposit Taking Institutions, 2000–10

(Percent)

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010Q1
Regulatory capital to risk-weighted assets 1/	13.6	12.4	10.5	12.0	12.8	13.2	12.2	11.2	9.4	11.7	11.7
Regulatory Tier I capital to risk-weighted assets 1/	13.5	10.9	8.8	9.8	10.0	10.9	9.9	9.2	7.9	10.6	10.6
Nonperforming loans net of provisions to capital	33.4	29.4	28.9	27.0	26.5	19.2	15.4	16.8	26.1	38.2	40.6
Nonperforming loans to total gross loans	11.7	8.3	7.4	7.0	7.0	6.3	5.4	4.5	5.0	7.7	8.2
Sectoral distribution of loans 2/											
Consumer credit	9.3	10.6	11.3	12.3	14.3	15.2	16.3	15.0	14.1	14.0	13.0
Lending for house purchase	18.8	21.0	24.4	26.1	27.7	31.4	33.4	34.5	32.4	35.0	35.5
Non-financial corporations	70.5	65.7	60.4	57.7	54.4	50.5	47.1	47.2	50.4	47.5	48.0
Insurance corporations and pension funds	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.2	0.1	0.0	0.0
Other financial intermediaries	1.1	2.2	3.2	2.6	2.3	1.6	1.8	1.5	1.5	1.9	1.9
Other	0.3	0.4	0.6	1.3	1.2	1.2	1.4	1.5	1.5	1.6	1.5
Return on assets (after taxes) 3/	1.4	1.0	0.5	0.6	0.4	0.9	0.8	1.0	0.2	-0.1	-0.6
Return on equity (after taxes) 3/	15.4	12.4	6.8	8.9	6.4	15.9	12.7	14.8	3.2	-1.5	-8.7
Interest margin to gross income 3/	54.5	62.8	72.5	73.9	77.0	75.5	72.3	71.9	83.1	74.8	98.1
Non-interest expenses to gross income 3/	53.0	59.0	69.0	63.0	64.3	54.5	52.2	52.6	60.0	57.4	65.8
Liquid assets to total assets 2/	46.4	41.1	39.5	37.0	33.4	34.0	33.6	35.1	38.7	45.2	45.9
Liquid assets to short-term liabilities 2/	60.7	53.0	48.7	46.5	43.2	47.0	46.5	48.0	50.0	56.9	57.4
Net open position in foreign exchange to capital 1/ 4/	...	3.5	7.2	5.7	3.5	2.8	4.8	3.9	7.9	11.7	10.8

Source: Bank of Greece.

1/ Data on a consolidated basis.

2/ On an aggregate resident-based approach (i.e. commercial banks, cooperative banks and foreign branches).

3/ From 2004 in accordance with IFRS.

4/ Based on revised figures from 2002 onwards.

Table 7. Greece: Access and Phasing under the Stand-By Arrangement, 2010–13

Review	Availability Date	Action	Purchase	
			In millions of SDRs	In percent of quota
	May 10, 2010	Board approval of SBA	4,805.9	583.9
First Review	August 30, 2010	Observance of end-June 2010 performance criteria, completion of first review	2,162.7	262.8
Second Review	November 30, 2010	Observance of end-September 2010 performance criteria, completion of second review	2,162.7	262.8
Third Review	February 28, 2011	Observance of end-December 2010 performance criteria, completion of third review	3,604.5	438.0
Fourth Review	May 30, 2011	Observance of end-March 2011 performance criteria, completion of fourth review	2,883.6	350.4
Fifth Review	August 30, 2011	Observance of end-June 2011 performance criteria, completion of fifth review	1,922.4	233.6
Sixth Review	November 30, 2011	Observance of end-September 2011 performance criteria, completion of sixth review	1,201.5	146.0
Seventh Review	February 28, 2012	Observance of end-December 2011 performance criteria, completion of seventh review	2,403.0	292.0
Eighth Review	May 30, 2012	Observance of end-March 2012 performance criteria, completion of eighth review	1,441.8	175.2
Ninth Review	August 30, 2012	Observance of end-June 2012 performance criteria, completion of ninth review	1,441.8	175.2
Tenth Review	November 30, 2012	Observance of end-September 2012 performance criteria, completion of tenth review	480.6	58.4
Eleventh Review	February 28, 2013	Observance of end-December 2012 performance criteria, completion of eleventh review	1,441.8	175.2
Twelfth Review	May 30, 2013	Observance of end-March 2013 performance criteria, completion of twelfth review	480.6	58.4
Total			26,432.9	3,211.8

Source: Fund staff projections.

Table 8. Greece: Indicators of Fund Credit
(In millions of Euros, unless otherwise specified)

	2010	2011	2012	2013	2014	2015	2016	2017	2018
Disbursements	10,773	11,340	6,804	2,268	...	...	...	...	...
(in percent of quota)	1,109.5	1,167.9	700.8	233.6	...	...	...	...	...
(Projected Debt Service to the Fund based on Existing and Prospective Drawings)									
Total	104	624	1,237	3,604	10,031	12,265	7,628	2,936	360
Interest	104	624	1,237	1,867	1,916	1,245	505	101	5
Amortization	0	0	0	1,736	8,115	11,021	7,123	2,835	354
Total debt service, in percent of									
Exports of goods and services	0.2	1.3	2.3	6.3	16.4	18.6	10.7	3.9	0.4
GDP	0.0	0.3	0.5	1.5	4.0	4.7	2.8	1.0	0.1
(Projected Level of Credit Outstanding based on Existing and Prospective Drawings)									
Outstanding stock	10,773	22,112	28,916	29,448	21,333	10,312	3,189	354	...
(in percent of quota)	1,110	2,277	2,978	3,033	2,197	1,062	328	36	...
(in percent of GDP)	4.6	9.5	12.2	12.1	8.5	4.0	1.2	0.1	...
Memorandum items									
Exports of goods and services (in billion of euros)	45.0	48.8	52.7	56.9	61.3	66.1	71.0	75.9	81.0
GDP (in billions of Euros)	236.1	232.9	236.4	243.0	250.6	260.2	276.4	287.3	300.2
Euro/SDR rate	1.1798								
Quota	971								

Source: Fund staff projections.

Table 9. Greece: Monetary Survey

	2005	2006	2007	2008	2009	2010 Program	2010 Proj.
(Billion of euros)							
Assets	241.4	264.9	298.5	357.7	381.2	394.9	410.3
Credit to the private sector	156.1	180.8	213.4	233.2	224.0	217.6	222.6
Credit to the government	59.8	57.3	55.4	53.5	71.1	72.8	80.1
Net credit to non-€ residents	-10.8	-10.5	-13.9	9.7	30.9	55.3	55.6
Other	31.0	31.6	38.3	56.2	49.8	43.9	46.6
Fixed assets	5.3	5.7	5.2	5.2	5.4	5.3	5.4
Liabilities	241.4	264.9	298.5	357.7	381.2	394.9	410.3
Total deposits	172.1	188.2	214.9	241.4	250.1	230.6	220.0
Other	45.3	50.8	53.4	86.6	89.8	124.2	149.0
Capital and reserves	24.0	25.9	30.2	29.8	41.3	40.1	41.2
(Percent change)							
Total deposits	7.7%	9.4%	14.2%	12.3%	3.6%	-7.8%	-12.0%
Credit to the private sector	17.8%	15.8%	18.0%	9.3%	-4.0%	-2.8%	-0.6%
Credit to the government	3.4%	-4.3%	-3.2%	-3.5%	33.0%	1.0%	12.5%
(Percent of GDP)							
Total deposits	88.1	89.4	94.9	100.9	105.3	99.9	93.2
Credit to the private sector	79.9	85.9	94.2	97.5	94.3	94.3	94.3
Credit to government	30.6	27.2	24.5	22.4	30.0	31.5	33.9
(Percent)							
Memorandum items:							
Capital to assets	8.5	8.0	8.0	6.7	9.3	9.1	9.1
Credit to government & private sector over deposits	129.1	130.5	129.9	119.9	118.7	126.8	138.5

Sources: Bank of Greece; and IMF staff calculations.

Table 10. Greece: Modified General Government Cash Balance for Program Monitoring (in billion of Euro, cumulative)

	2009 Actual	Program					
		Jun-10		Sep-10		Dec-10	
		Progr.	Actual	Progr.	Proj.	Progr.	Proj.
I. State budget							
Revenues 1/	50.5	25.1	24.2	41.2	38.7	58.4	56.8
Net income Ordinary Budget (A+B-C)	48.5	24.1	23.8	39.1	38.2	55.1	53.8
A. Recurrent/ordinary revenue	52.3	25.8	25.1	41.6	40.6	58.6	57.4
1. Direct taxes	21.4	9.0	8.9	15.3	15.0	21.7	21.4
Income taxes	16.6	6.3	6.0	11.5	10.8	16.6	15.6
PIT	10.9	4.5	4.3	7.7	7.5	10.9	10.7
CIT	3.4	1.0	1.1	2.2	2.0	3.5	3.0
Other	2.3	0.8	0.6	1.5	1.3	2.2	1.9
Property taxes	0.5	0.3	0.1	0.7	0.4	1.0	0.8
Tax arrears collection	2.4	1.3	1.2	1.7	1.6	2.2	2.2
Other direct taxes	1.9	1.2	1.6	1.6	2.2	2.0	2.8
2. Indirect taxes	28.3	15.6	14.8	24.4	23.4	34.1	32.9
Transaction taxes	17.9	9.4	8.9	14.9	14.3	20.2	19.5
VAT	16.6	8.7	8.4	13.6	13.4	18.5	18.4
other	1.3	0.8	0.5	1.3	0.9	1.7	1.2
Consumption taxes	9.6	5.8	5.5	8.8	8.5	12.9	12.5
Tax arrears collections	0.4	0.2	0.2	0.3	0.3	0.5	0.4
Other indirect taxes	0.4	0.2	0.2	0.3	0.3	0.4	0.4
3. Transfers EU	0.3	0.1	0.1	0.2	0.1	0.4	0.4
4. Nontax revenue	2.3	1.1	1.4	1.7	2.0	2.4	2.7
B. One-off revenue	1.1	0.7	0.9	1.0	1.2	1.4	1.5
C. Tax Refunds (-)	5.0	2.4	2.3	3.5	3.6	4.9	5.1
Public investment budget	2.0	0.9	0.4	2.1	0.5	3.3	3.0
A. EU flows	1.9	0.8	0.3	2.0	0.4	3.1	2.9
B. Own revenues	0.2	0.1	0.1	0.1	0.1	0.1	0.1
Total expenditure 1/ 2/	83.6	39.8	34.1	60.5	56.4	79.8	76.4
Total ordinary spending	70.3	34.2	30.2	51.6	49.6	67.9	66.1
Total ordinary primary spending	58.0	26.8	24.5	40.0	37.7	54.9	52.7
A. Remuneration and pensions	25.2	10.8	11.3	16.5	16.9	22.5	22.9
B. Insurance and Healthcare	17.6	8.7	7.4	12.8	11.5	18.1	17.0
C. Operating and other expenditure and returned resources	14.5	7.0	5.4	10.2	8.7	13.6	12.2
D. Payments in exchange of claims of insurance fund 3/	0.8	0.4	0.4	0.5	0.5	0.7	0.6
Interest expenditure	12.3	7.4	5.7	11.7	11.9	13.0	13.4
Transfers to hospitals for the settlement of past debt 4/	1.5	0.0	0.0	0.0	0.2	0.0	0.2
Investment spending	9.6	4.2	3.7	6.8	5.6	9.2	8.2
Spending on military procurement	2.2	1.4	0.2	2.0	1.0	2.7	1.8
State Budget primary spending 1/ 2/ (variable monitored for PC)	71.3	32.4	28.4	48.8	44.3	66.8	62.7
Balance state budget 1/ 2/	-33.1	-14.7	-9.9	-19.3	-17.7	-21.4	-19.6
II. Balance local governments 1/ 5/	0.0	0.9	0.2	1.0	0.2	0.1	0.0
III. Balance social security funds 1/ 5/	1.9	1.9	-0.2	3.1	1.6	2.6	2.3
IV. Modified general government cash balance	-31.2	-12.0	-10.0	-15.2	-15.9	-18.7	-17.2
of which: Modified general government primary cash balance (variable monitored for PC)	-18.9	-4.6	-4.3	-3.5	-3.8	-5.7	-3.6
V. Adjustments 6/	-1.1	...	...	...	...	0.1	...
VI. General government balance (ESA 95)	-32.3	...	...	...	...	-18.6	...
Memorandum items							
Floor on the modified general government primary cash balance 6/	...	-5.0	-4.3	-4.0	...	-5.7	...
Ceiling on state budget primary spending 7/	...	34	28	50	...	67	...

Source: Greek Ministry of Finance and Fund staff projections.

1/ Including measures taken in the context of the 2010 program.

2/ Including spending on military procurement.

3/ For the personnel of the Public Power Company.

4/ Such transfers are excluded from spending for measurement of the PCs.

5/ Change in net financial assets. Excludes valuation changes.

6/ National accounts adjustments and capital transfers to other bodies of general government using bonds.

7/ End-June and end-September targets include a margin to account for deviations from historical seasonality.

Annex 1. Public Debt Sustainability (updated)

The sharp increase of general government debt to 115 percent of GDP in 2009 can be attributed to three factors, which will continue to weigh on Greece for some time: (i) lower growth, (ii) higher real interest rates, and (iii) an elevated fiscal deficit.

Baseline and underlying assumptions

Under the baseline scenario, Greece's public debt as a share of GDP would peak at 144 percent in 2013 (compared to 149 percent in Country Report 10/110) and gradually decline to 111 percent by 2020 (compared to 120 percent in CR10/110).¹ The slightly better debt outlook reflects the higher 2010 inflation and thus a stronger adjustment in real terms. The baseline scenario assumes that the primary balance will improve from - 8.6 percent of GDP in 2009 to nearly 6 percent of GDP in 2014 and beyond. Output is expected to contract in 2010–11, but will reach its medium-term target of 2¾ percent after 2016, while inflation is moderately below the EU average. Interest rate spreads on new debt are projected to decline as confidence improves, even though the German bund rate is projected to rise over the medium term. Further, it includes in 2010 a €10 billion disbursement for the Financial Stability Fund (FSF)² and €5.5 billion for arrears clearance. After 2011 privatization proceeds of €1 billion every year are included. (Table A2).

In an unchanged policy scenario the public debt-to-GDP ratio would continue to rise to 181 percent of GDP by 2020. This reflects the still large fiscal deficit of around 8 percent of GDP in 2010.

In a scenario where key variables remain at their historical averages, the public debt-to-GDP ratio would increase moderately and be around 116 percent of GDP by 2020. This reflects the recent history of high catch-up growth, relatively high fiscal revenue, and high domestic inflation that depressed real interest rates.

Debt Structure

Although the average maturity of the debt is relatively high, there are large rollover needs in the next three to five years. The average remaining maturity of the general government debt is 8 years, but this largely reflects a few very long-term issues. More than one third of the debt stock will mature in the next three years, and almost half will mature in the next five years. **Other aspects of the government debt's composition are relatively favorable.** Of the total general government debt, 98.5 percent was denominated in Euro.

¹Maastricht debt definition.

²It is assumed that the €10 billion in investment by the FSF would be fully recovered by 2015.

Moreover, 89 percent was fixed rate debt at end-2009. The share of foreign currency (SDR) and floating rate debt is expected to go up to about 10 and 40 percent during 2012–13, respectively, with EU bilateral (floating) and IMF (floating, and foreign currency) loans amounting to 30 percent in the total stock of debt. The debt that is coming to maturity in the next few years was issued many years ago at relatively high nominal interest rates, so that the interest differential between new market debt and old maturing debt is not as high as in other crisis cases.

Sensitivity Analysis

Sensitivity analysis shows that the baseline public debt outlook is mainly affected by growth shocks (Figure A1 and Table A1). Several risk factors could have a large potential impact on the fiscal path: lower growth, lower inflation, higher interest rates, and contingent liabilities from state-owned enterprises and the banking system. While adverse shocks of reasonable size to each of the variables considered would be consistent with a turnaround in the debt dynamics, a combined adverse shock would render the dynamics clearly unsustainable. These include:

- **Recognition of implicit or contingent liabilities:** The chart includes: identified guarantees to public enterprises (for a total of €25.8 billion or 11 percent of GDP) and past swap operations of €5 billion. Further, the state-guaranteed liquidity support of the ECB to the financial system of €55 billion has also been included.³ All privatization proceeds are assumed to be zero. This would leave the debt at 176 percent of GDP by 2020.
- **Weaker fiscal adjustment:** a smaller adjustment of 1 percent of GDP per year would imply a more gradual decline to about 123 percent of GDP by 2020.
- **Weaker growth:** a one percentage point reduction in the GDP growth rate each year would result in debt rising to around 154 percent of GDP by 2020; (on the other hand, faster growth by one percentage point would bring the debt down to 74 percent of GDP by 2020.
- **More severe disinflation in 2011–2012:** 3 percentage point lower inflation than in the baseline would result in the debt to GDP ratio peaking at 144 percent of GDP and declining to 168 by 2020.
- **Higher interest rate:** an interest rate increase of 200bps (reflecting a higher Euribor and SDR rate) would increase public debt to 121 percent of GDP by 2020.

³ It is assumed that going forward any losses of public enterprises and guarantees called related to TEMPME would form part of the fiscal deficit ceiling. Hence, greater losses in public enterprises will require more fiscal effort to meet the agreed fiscal deficit targets.

Figure A1: Greece: Public Debt Sustainability Analysis (in percent of GDP)

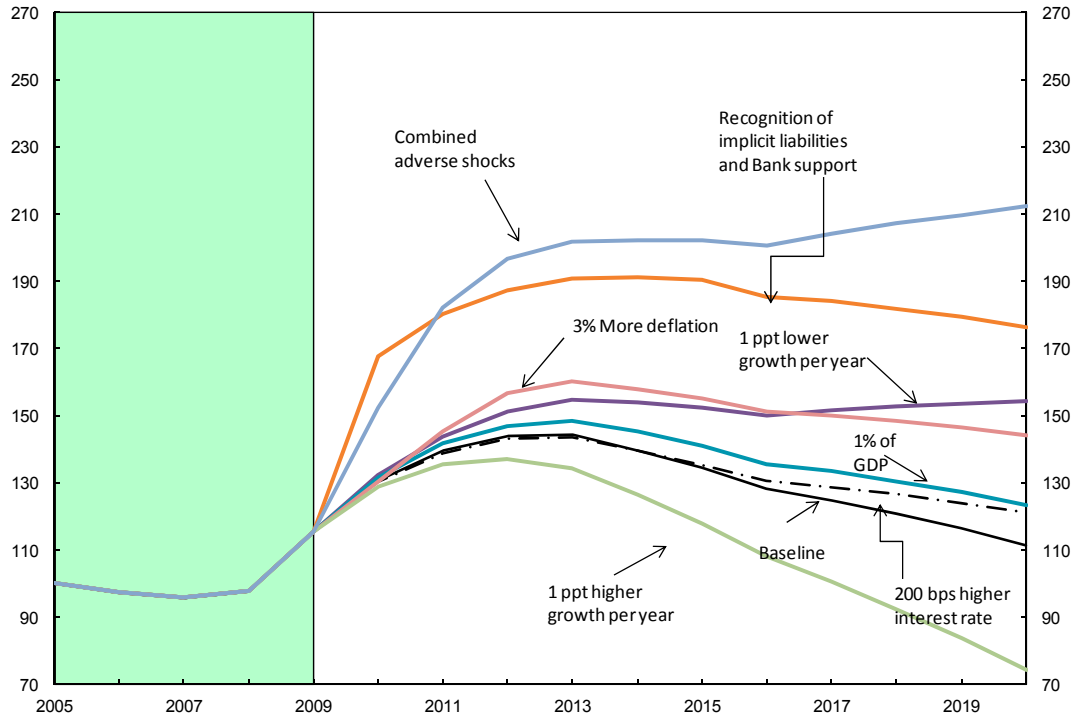


Table A1: Greece: Sensitivity Test of the Public Debt Sustainability 1/ (In percent of GDP)

	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Baseline scenario	115	130	139	144	144	140	134	128	125	121	116	111
Higher growth of 1 percent per year	115	129	135	137	134	126	118	108	101	92	84	74
Lower growth of 1 percent per year	115	132	144	151	155	154	152	150	151	152	153	154
Disinflation (3 percent lower inflation for 2011-2012)	115	130	145	157	160	158	155	151	150	148	146	144
Lower primary deficit (by 1% of GDP)	115	131	141	147	148	145	141	135	133	130	127	123
Recognition of contingent liabilities, and new debt 2/	115	167	180	187	190	191	190	185	184	182	179	176
200 bps higher interest rate on new debt	115	130	139	143	144	140	135	130	129	126	124	121

Source: Fund staff calculations.

1/ Changes in assumptions are relative to the baseline.

2/ This assumes €85.5bn in guaranteed debt.

Table A2. Greece: Public Sector Debt Sustainability Framework, 2008-2020
(In percent of GDP, unless otherwise indicated)

	Actual		Projections											Debt-stabilizing primary balance 9/
	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	
Baseline: Public sector debt 1/	98	115	130	139	144	144	140	134	128	125	121	116	111	1.1
Change in public sector debt	2.1	17.5	15.1	9.2	4.2	0.5	-4.5	-5.4	-6.1	-3.4	-4.1	-4.4	-4.8	
Identified debt-creating flows (4+7+12)	0.1	15.9	15.1	9.2	4.2	0.5	-4.5	-5.4	-6.1	-3.4	-4.1	-4.4	-4.8	
Primary deficit	0.7	8.7	2.2	0.8	-1.0	-3.0	-5.7	-5.9	-5.8	-5.9	-5.9	-6.0	-6.0	
Revenue and grants	39.9	36.7	39.6	41.6	41.9	42.5	42.5	42.0	40.4	40.2	39.7	39.3	38.7	
Primary (noninterest) expenditure	40.6	45.4	41.9	42.4	40.9	39.5	36.8	36.1	34.6	34.4	33.8	33.3	32.7	
Automatic debt dynamics 2/	-1.5	5.6	6.3	8.3	5.2	3.9	3.8	2.7	-0.4	2.4	1.7	1.5	1.1	
Contribution from interest rate/growth differential 3/	-1.5	5.6	6.3	8.3	5.2	3.9	3.8	2.7	-0.4	2.4	1.7	1.5	1.1	
Of which contribution from real interest rate	1.2	3.6	1.7	4.8	6.7	6.8	6.7	6.2	5.5	5.7	5.4	5.2	4.7	
Of which contribution from real GDP growth	-2.7	2.0	4.6	3.5	-1.5	-3.0	-2.9	-3.6	-5.9	-3.3	-3.6	-3.7	-3.6	
Contribution from exchange rate depreciation 4/	0.0	0.0	...	...	...	...	...	...	...	...	...	...	...
Other identified debt-creating flows	0.9	1.5	6.6	0.1	0.1	-0.3	-2.6	-2.2	0.1	0.1	0.1	0.1	0.1	
Privatization receipts (negative)	0.0	-0.4	0.0	-0.4	-0.4	-0.4	-0.4	-0.4	-0.4	-0.3	-0.3	-0.3	-0.3	
Recognition of implicit or contingent liabilities	0.9	0.3	6.6	0.5	0.5	0.5	0.5	0.5	0.4	0.4	0.4	0.4	0.4	
Other (specify, e.g. bank recapitalization)	0.0	1.6	0.0	0.0	0.0	-0.4	-2.7	-2.3	0.0	0.0	0.0	0.0	0.0	
Residual, including asset changes (2-3) 5/	2.0	1.6	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Public sector debt-to-revenue ratio 1/	244.7	313.6	328.6	335.4	343.0	339.0	328.9	319.8	317.0	309.9	304.2	295.9	287.8	
Gross financing need 6/	5.0	13.7	20.8	22.4	23.8	23.1	30.7	30.1	23.3	20.9	16.8	21.4	13.2	
in billions of U.S. dollars	17.9	44.8	10-Year	69.1	73.3	78.3	77.4	105.0	106.9	87.9	81.7	68.7	91.9	59.4
Scenario with key variables at their historical averages 7/			130	129	128	127	123	120	119	118	117	117	116	-1.5
Scenario with no policy change (constant primary balance) in 2010-2020		Historical	130	141	148	154	158	161	163	168	173	177	181	0.8
Key Macroeconomic and Fiscal Assumptions Underlying Baseline		<u>Average</u>												
Real GDP growth (in percent)	3.0	-2.0	3.5	-4.0	-2.6	1.1	2.1	2.1	2.7	4.7	2.7	3.1	3.2	3.3
Average nominal interest rate on public debt (in percent) 8/	4.9	5.0	5.5	4.9	4.9	5.3	5.6	5.8	5.8	5.9	5.9	5.9	6.1	5.9
Average interest rate on new market debt				5.0	5.3	5.4	5.5	5.6	5.6	5.6	5.6	5.7	5.7	5.8
Average interest rate on all new debt (includes EU bilateral and IMF debts)				3.8	4.8	5.6	6.0	6.2	6.1	5.8	5.7	5.7	5.7	5.8
Spreads above German bund				250	200	150	100	100	100	100	100	100	100	100
German bund rate				225	275	350	350	350	350	350	350	350	350	350
Average real interest rate (nominal rate minus change in GDP deflator, in p	1.4	3.7	2.2	1.3	3.6	4.9	4.9	4.8	4.7	4.4	4.7	4.6	4.6	4.3
Nominal appreciation (increase in US dollar value of local currency, in perc	114.6	-6.7	7.7	...	...	...	...	...	...	...	...	...	...	...
Inflation rate (GDP deflator, in percent)	3.5	1.4	3.3	3.5	1.3	0.4	0.7	1.0	1.1	1.4	1.2	1.4	1.5	1.6
Growth of real primary spending (deflated by GDP deflator, in percent)	5.3	8.0	5.7	-11.5	-1.5	-2.4	-1.4	-4.9	0.8	0.3	2.1	1.3	1.8	1.5
Primary deficit	0.7	8.7	0.5	2.2	0.8	-1.0	-3.0	-5.7	-5.9	-5.8	-5.9	-5.9	-6.0	-6.0

1/ General government.

2/ Derived as $[(r - \pi(1+g) - g + \alpha_d(1+r)] / (1+g+\pi+g\pi)$ times previous period debt ratio, with r = interest rate; π = growth rate of GDP deflator; g = real GDP growth rate; α_d = share of foreign-currency denominated debt; and ϵ = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).

3/ The real interest rate contribution is derived from the denominator in footnote 2/ as $r - \pi(1+g)$ and the real growth contribution as $-g$.

4/ The exchange rate contribution is derived from the numerator in footnote 2/ as $\alpha_d(1+r)$.

5/ For projections, this line includes exchange rate changes.

6/ Defined as general government deficit, plus amortization of medium and long-term general government debt, plus short-term debt at end of previous period.

7/ The key variables include real GDP growth; real interest rate; and primary balance in percent of GDP.

8/ Derived as nominal interest expenditure divided by previous period debt stock.

9/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

Annex 2. External Debt Sustainability Analysis¹ (Updated)

Greece's net external debt has been increasing. During the past several years, net external debt has increased from 51 percent of GDP in 2002 to 83 percent of GDP in 2009. This reflects rising current account deficits to 11 percent of GDP in 2009. The debt ratio could have been even higher, as it benefited from relatively low interest rates, relatively high inflation, and above trend GDP growth.

Looking forward, the net debt position is projected to deteriorate further under the baseline. The net debt-to-GDP ratio is projected to continue rising and peak at 104 percent of GDP in 2013 before declining to 100 percent of GDP in 2015. This evolution takes place as growth weakens, inflation declines to below the EU average, interest rates rise, and the current account improves.

The analysis shows that the net debt position is sensitive to adverse shocks. The debt dynamics will be adversely affected by weaker growth, more severe deflation that could arise with the large fiscal consolidation and private sector adjustment; higher interest rates as policy rates in the advanced economies including the euro zone increase more than anticipated, market sentiments remain negative; and a slower current account adjustment. For each individual shock, the debt ratio will increase, although the shape of debt path remains broadly similar. A combination of these shocks will have a large negative impact to the debt ratio and debt path. (Figure A3 and Chart A2)

- **Weaker real GDP growth.** A 1 percentage point lower GDP growth will increase net debt ratio by about 6 percentage points of GDP by 2015 relative to the baseline.
- **Higher deflation.** Reducing inflation by 3 percentage points in 2010 and 2012 will increase the debt ratio by 5 percentage points by 2015 relative to the baseline.
- **Higher interest rate.** A 100 basis points increase in the interest rate will increase the debt to GDP ratio by 6 percentage points by 2015 relative to the baseline.
- **Higher current account deficit.** A permanent $\frac{1}{4}$ standard deviation shock to the current account deficit will increase the debt to GDP ratio by 10 percentage points relative to the baseline.

¹ The analysis is done on net rather than gross external debt to be consistent with external account projections which include projections for changes in gross external assets and liabilities.

Table A3. Greece: Net External Debt Sustainability Framework, 2005-2015
(In percent of GDP, unless otherwise indicated)

	Actual					Projections						Debt-stabilizing non-interest current account 6/
	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	
Baseline: External debt	58.0	62.0	67.7	73.8	83.4	93.3	100.8	103.7	104.2	103.2	100.4	-3.0
Change in external debt	4.4	3.9	5.7	6.1	9.6	9.9	7.4	3.0	0.5	-1.0	-2.8	
Identified external debt-creating flows (4+8+9)	2.2	3.9	4.7	9.5	10.9	13.2	9.4	4.2	2.2	1.2	-0.4	
Current account deficit, excluding interest payments	5.7	9.1	11.8	11.4	8.6	8.3	5.1	4.1	3.3	2.4	1.4	
Deficit in balance of goods and services	6.2	9.5	11.0	11.3	7.6	7.1	3.9	3.0	2.2	1.4	0.5	
Exports	21.2	21.2	21.5	22.5	17.8	19.0	21.0	22.3	23.4	24.5	25.4	
Imports	27.4	30.6	32.5	33.8	25.4	26.2	24.9	25.3	25.6	25.8	25.9	
Net non-debt creating capital inflows (negative)	-2.8	-3.2	-5.3	-1.4	-0.8	-1.0	-0.9	-1.5	-1.6	-1.8	-1.8	
Automatic debt dynamics 1/	-0.8	-2.0	-1.7	-0.5	3.1	5.9	5.2	1.6	0.6	0.6	0.0	
Contribution from nominal interest rate	1.8	2.2	2.6	3.1	2.6	2.6	2.7	2.7	2.7	2.7	2.6	
Contribution from real GDP growth	-1.1	-2.4	-2.6	-1.3	1.5	3.3	2.5	-1.1	-2.1	-2.1	-2.6	
Contribution from price and exchange rate changes 2/	-1.5	-1.7	-1.8	-2.3	-1.0	-2.8	-1.2	-0.4	-0.7	-1.1	-1.2	
Residual, incl. change in gross foreign assets (2-3) 3/	2.2	0.0	1.0	-3.5	-1.3	-0.4	-0.7	-0.9	-1.0	-1.2	-1.2	
External debt-to-exports ratio (in percent)	273.4	292.9	314.2	327.3	468.1	489.8	480.8	465.6	445.2	422.0	395.4	
Gross external financing need (in billions of euros) 4/	49.8	68.8	90.4	106.8	166.1	171.0	171.4	145.1	132.9	151.1	164.4	
in percent of GDP	25.5	32.7	39.9	44.6	69.9	72.4	73.6	61.4	54.7	60.3	63.2	
Scenario with key variables at their historical averages 5/						93.3	95.7	97.9	99.9	101.8	103.7	-3.7
Key Macroeconomic Assumptions Underlying Baseline												
Real GDP growth (in percent)	2.2	4.5	4.5	2.1	-2.0	-4.0	-2.6	1.1	2.1	2.1	2.7	
GDP deflator in US dollars (change in percent)	2.8	3.1	3.0	3.5	1.4	3.5	1.3	0.4	0.7	1.0	1.1	
Nominal external interest rate (in percent)	3.6	4.1	4.6	4.9	3.5	3.1	2.8	2.7	2.7	2.7	2.7	
Growth of exports (euro terms, in percent)	5.2	7.4	9.6	10.4	-21.5	6.3	8.5	7.9	8.0	7.8	7.8	
Growth of imports (euro terms, in percent)	8.6	20.2	14.3	9.6	-25.2	2.4	-6.3	3.3	3.9	4.0	4.3	
Current account balance	-7.5	-11.3	-14.4	-14.6	-11.2	-10.8	-7.8	-6.9	-6.0	-5.1	-4.0	
Net non-debt creating capital inflows	2.8	3.2	5.3	1.4	0.8	1.0	0.9	1.5	1.6	1.8	1.8	

1/ Derived as $[-r - g - r(1+g) + ea(1+r)] / (1+g+r+gr)$ times previous period debt stock, with r = nominal effective interest rate on external debt; r = change in domestic GDP deflator in US dollar terms, g = real GDP growth, e = nominal appreciation (increase in dollar value of domestic currency), and a = share of domestic-currency denominated debt in total external debt.

2/ The contribution from price and exchange rate changes is defined as $[-r(1+g) + ea(1+r)] / (1+g+r+gr)$ times previous period debt stock. r increases with an appreciating domestic currency ($e > 0$) and rising inflation (based on GDP deflator).

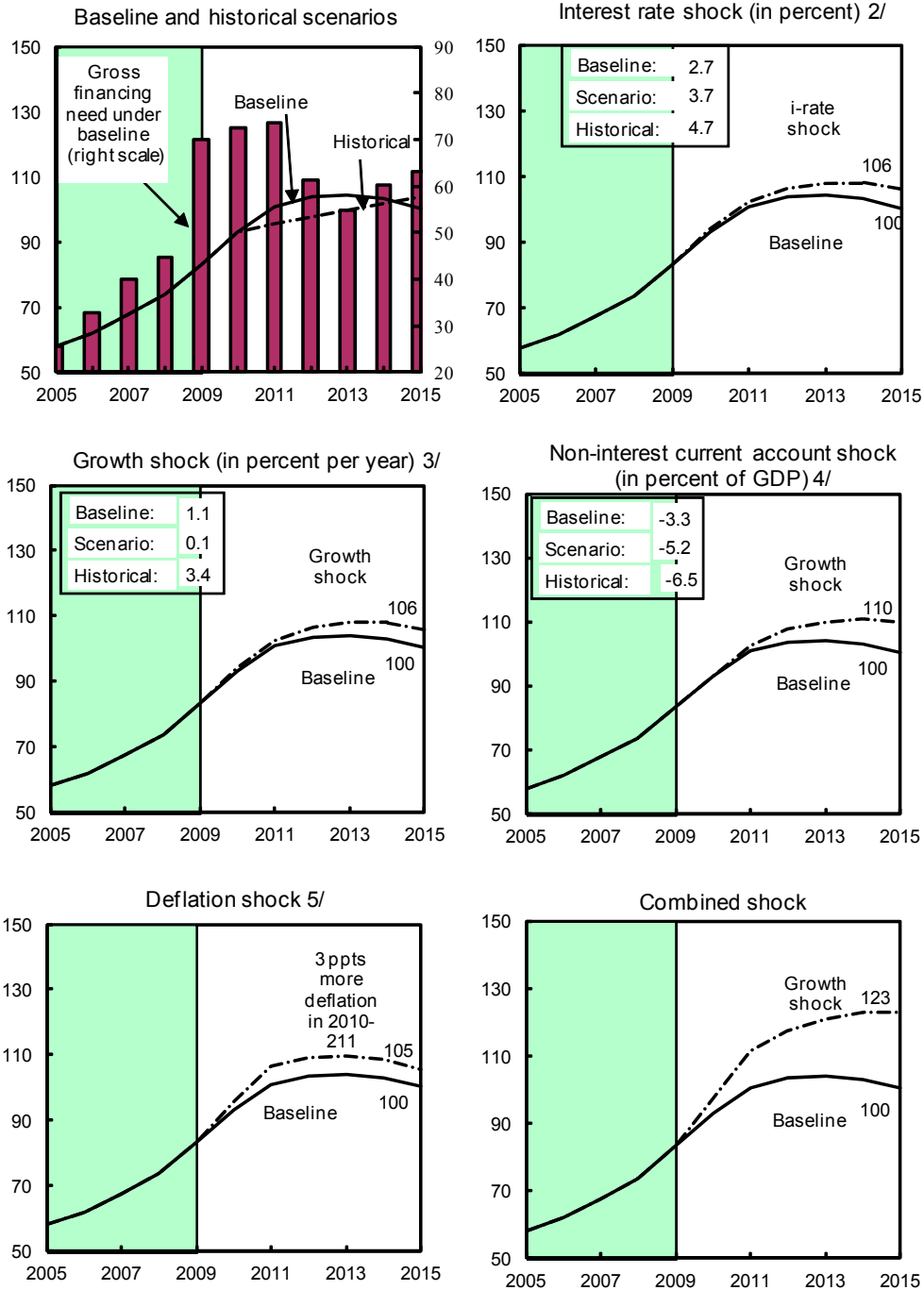
3/ For projection, line includes the impact of price and exchange rate changes.

4/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.

5/ The key variables include real GDP growth; nominal interest rate; dollar deflator growth; and both non-interest current account and non-debt inflows in percent of GDP.

6/ Long-run, constant balance that stabilizes the debt ratio assuming that key variables (real GDP growth, nominal interest rate, dollar deflator growth, and non-debt inflows in percent of GDP) remain at their levels of the last projection year.

Figure A2. Greece: Net External Debt Sustainability: Bound Tests 1/
(External debt in percent of GDP)



Sources: Greek authorities, and staff estimates.

1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.

2/ Interest rates are increased by 100bps for the projection period.

3/ Growth rates lower by 1 percentage point.

4/ Current account deficit higher by a 1/4 of standard deviation.

5/ Inflation lower by 3 percentage points in 2010 and 2011.

LETTER OF INTENT

Athens, August 6, 2010

Mr. Dominique Strauss-Kahn
Managing Director
International Monetary Fund
Washington DC

Dear Mr. Strauss-Kahn:

In the attached update to the Memorandum of Economic and Financial Policies (MEFP) of May 3, 2010, we describe the progress and policy steps towards meeting the objectives of the economic program that is being supported by a Stand-By Arrangement. The policies of the government of Greece remain fully oriented toward securing fiscal sustainability, safeguarding the stability of the financial system, and boosting potential growth and competitiveness.

We have made a vigorous start with our economic program. The fiscal program is progressing well, financial policies are being strengthened, and structural policies are ahead of schedule in key respects:

- The end-June quantitative performance criteria have all been met, led by a strong implementation of the fiscal program. Not unexpectedly, it has proven difficult to fully control expenditures at some entities, and in anticipation of such problems we significantly under-executed budget implementation at the state level, thereby ensuring that targets for the general government were met. Going forward, we are redoubling our efforts to strengthen controls at all levels of government and are determined to continue to over-perform at the state level until such controls become fully effective.
- Reflecting the weaknesses in expenditure controls at some entities, the indicative target on the non-accrual of domestic arrears has not been observed as the monitoring system for general government commitments, accounts payable, and arrears is still being developed and implemented. We commit to bringing these arrears down to zero by year-end, so that only a normal level of accounts payable is carried over into 2011.
- While the financial system continues to feel the effects of tight liquidity, sentiment indicators are gradually beginning to improve, and policy progress has been made by establishing the Financial Stability Fund to backstop any capital needs that banks might have in the future owing to an expected increase in impaired loans as the recession runs its course. Stress tests suggest that the funds allocated by the authorities for the FSF remain adequate.
- The government has made significant progress in structural reforms with far-reaching pension and labor market reforms being approved ahead of schedule. Parliament has also already adopted important budgetary reform and reforms of local government. Other major reforms that are at an advanced stage aim at liberalizing the trucking

industry and restructuring the railroad system, while reforms of the energy sector, protected professions, the licensing and business regulatory framework and preparations for implementation of the services directive are gaining momentum, as foreseen in our program.

On this basis and the completion of the prior action, we request completion of the first review under the Stand-By Arrangement, and the second purchase under this arrangement in the amount of SDR 2,162.7 million.

We believe that the policies set forth in the May 3, 2010 Letter of Intent and MEFP, and the attached update to the MEFP, are adequate to achieve the objectives under the program. We stand ready to take any corrective actions that may become appropriate for this purpose as circumstances change. We will consult with the Fund on the adoption of any such actions and in advance of revisions to the policies contained in this letter, in accordance with the Fund's policies on such consultations.

This letter is being copied to Messrs. Juncker, Rehn, and Trichet.

Sincerely,

/s/

/s/

George Papaconstantinou
Minister of Finance

George Provopoulos
Governor of the Bank of Greece

GREECE—MEMORANDUM OF ECONOMIC AND FINANCIAL POLICIES

1. **The government has made a vigorous start at implementing its economic program.** The fiscal program is progressing well, financial policies are being strengthened, and structural policies are ahead of schedule in key respects. The May 2010 Letter of Intent (LOI) and Memorandum of Economic and Financial Policies (MEFP) describing the 3-year economic program remain fully in force. This update to the MEFP combined with the updated MoU presents a review of achievements and policy steps toward the second review scheduled for late 2010.
2. **The growth outlook remains unaltered; short-run inflation is revised up.** The government continues to envisage a contraction of activity by about 4 percent in 2010 and some 2½ percent in 2011. However, because the government frontloaded a number of large indirect tax increases, which have been passed on as a step up in the price level, the rate of consumer price inflation and the implicit deflator have increased. The high pass through of indirect tax increases to final prices is indicative of a lack of competition and the prevalence of oligopolistic market structures. HICP inflation is now expected to approach 4¾ percent for the year. Inflation at constant taxes is falling and has declined below the euro-area average for the first time since the creation of the euro. Moreover, there is no evidence of pass through of higher prices to wages, and the national collective agreement just signed contributes to moderating wage growth and improving competitiveness.

Fiscal Policies

3. **The fiscal program is making good progress.** The cash state budget is leading the consolidation effort with an impressive cut in its deficit by over 40 percent in January-June (y/y). Current revenue has increased in the January-June period by 7 percent, despite the deepening recession, and current expenditure and transfers have been cut by some 10 percent. Local governments, hospitals, and social security funds have also taken steps but their progress is more gradual as controlling their expenditures is more difficult, as was expected. Through June, the large margin under the targets created in the state budget has offset the overruns to date in subnational entities. However, there has been some undesirable buildup in accounts payable/arrears in hospitals and social security funds and, as described below, steps are underway to gain a firmer grip on risks for the targets going forward.
4. **Looking to the second half of the year and consistent with the May program, the government will limit the annual general government fiscal deficit (on accrual terms) to €18.5 billion:**
 - **Continuing implementation of the measures:** The fiscal measures (VAT and excises, and particular the benefits from the pension and wage cuts) will be fully realized in the second half of the year and should generate substantial resources to allow all payments and the amortization of any mid-year arrears by end-2010.
 - **Under-execution of spending:** In the January-June period, the government under-executed state budget primary spending by €5.6 billion. The government intends to maintain this overperformance through September, and to end the year by a margin of

overperformance of €4 billion to cover risks coming from other parts of general government. The expenditure containment will focus on operating expenses while making all required transfers to the social security funds and local governments to allow them to become current in their payments. At any time, should performance run short of these objectives, or revenue drop below schedule, the government stands ready to take corrective actions.

5. **The government achieved an important milestone in end-July by passing a new budget law that strengthens the fiscal management framework.** This implies that the budget for 2011 will be part of a three-year rolling medium-term framework, and that the Minister of Finance will be able to set top-down expenditure ceilings for line ministries, local governments and social budgets so as to broaden the scope of fiscal policy to general government. Also, the budget will now contain standard contingency margins to facilitate absorbing shocks, and the government will set up commitment registers in the line ministries (a structural benchmark for end-September) to manage better accrual spending—beyond cash outlays. In addition, the government is also developing monthly fiscal reporting for general government entities (a benchmark by end-September).

6. **The preparation of general government budgets for 2011 in line with the new budget law commitments is underway.** The budgets will be prepared under the new law and the government will present the pre-budget to parliamentary committees in early October together with the consolidated draft local government and social budgets and consistent with a general government fiscal deficit target (in ESA95 terms) of €17 billion in 2011. The government will take into account the sustainability of discretionary spending cuts, and if needed replace them with permanent savings. At the same time, the government will put in place the 2011 fiscal measures that were agreed in May.

7. **In line with the original Memorandum, the government will focus on bolstering tax administration and fighting tax evasion in the months ahead.** Improving tax administration is essential for fairness in the adjustment program and to facilitate broadening the tax base, with moderate average tax rates. The government will kick-start the improved tax administration by implementing the recommendations received from technical experts. By end-September, the government will set up five dedicated task forces to:

- Ensure prompt implementation of the new tax legislation,
- collect tax arrears,
- reorganize the large tax payers unit,
- strengthen the audits for high-wealth and income individuals,
- strengthen filing and payment controls, and improving tax payer services.

Meanwhile, the government will make intensive use of payments receipts to bolster tax compliance, and cross-check tax information with data on wealth and spending habits to reduce tax abuse and evasion in particular of high-income and wealthy tax payers, while also reviewing the existing legal processes to ensure timely and effective prosecution of tax offenders.

8. **Public administration reform is advancing.** The government is setting up a single payment authority through which wages of civil servants in central government will be paid by end 2010 and for general government by March 2011. Plans to move in 2011 to a simplified remuneration system are facilitated by the completed public employment census. A functional review of central administration, beginning in the second half of 2010, will seek to identify operational steps to rationalize and make more efficient the public administration.

9. **The government envisages specific efforts to limit risks to its program, in particular to help strengthen expenditure control in subnational entities.**

- *Health sector.* In the hospital sector the government will accelerate payments to avoid the buildup of arrears and to limit the carryover of obligations into 2011. Further, the government has reduced procurement prices of pharmaceuticals by 20 percent by implementing price caps for approved drugs lists, and improved profiles and benchmarking for patients and doctors to avoid unnecessary prescriptions, which should yield important savings during the second half of this year. Indeed, the government stands ready to reduce pharmaceutical costs further (where there is room to expand the drugs lists, the use of generics, and by introducing e-prescriptions). The government will enforce the €3 for regular outpatient services in public hospitals and extend the “all day” operation of hospitals (afternoon shift) in order to develop and improve healthcare services and increase hospital revenues, including with increased copayments of outpatient and diagnostic services. The government has placed accounting firms in state hospitals to improve their financial management to gain control over spending and accounts payable.
- *Local governments.* The recently passed Kallikratis bill for local government reform will sharply reduce the number of local administrations, entities, and elected and appointed officials. The government will tightly implement the bill, in particular the targeted employment reduction and efficiency-enhancing reforms to secure improved budgetary results of €500 million subsequently in each of the three years during 2011-13. To ensure that those savings contribute to the overall fiscal consolidation of general government, the government will limit borrowing, reduce transfers, and control local government budgets consistent with the medium-term fiscal strategy.
- *State enterprises.* The government will strengthen performance of the major loss-making public enterprises in order to reduce contingent risks to the budget, including by enhancing efficiency, increasing tariffs in public transportation, and further reducing excessive allowances and overtime. In particular, the government will restructure the loss-making railroad enterprise as described below. Under the restructuring plan operating PSO’s (public service obligation—subsidies) will be limited to €50 million per year, and no new debt guarantees by the state will be provided to the restructured rail enterprise, which has to break with a long history of large losses. The 10 largest loss-making enterprises will have their financial statements through 2009 published on the web before end-September (structural benchmark) to enhance transparency in their financial condition.

10. **Parliament approved a substantial pension reform ahead of schedule.** It introduces a new system consisting of a contributory pension to top-up a non-contributory, means-tested, basic pension, aiming to control the increase in pension spending. The National Actuarial Authority will complete an assessment of the effects of the reform on the main pension funds by end-December 2010, and of the largest auxiliary pension funds by end-March 2011. These assessments will determine whether further adjustments to the parameters of the pension system would be needed to contain the increase in pension spending to 2.5 ppts of GDP between 2009–2060. Any further adjustments, if needed, will be completed by end of June 2011 in consultation with pension experts, as foreseen in Law 3863.

11. **Financing and cash management.** The latest assessment confirms that the state financing need in 2010–11 remains fully financed from the loans of the Euro-area member states and the IMF, with the government able—as foreseen in the program—to roll over its relatively small stock of T-bills. However, the tight liquidity position will require careful cash management. In this light, the public debt management agency will start monthly T-bill auctions beginning in September (from quarterly placements) to improve cash management and smooth maturity profiles.

Financial Sector Policies

12. **The Greek banking system continues to face a challenging environment.** In the first quarter of the year the banking system capital ratio declined by 0.05 percentage points to 11.7 percent as non performing loans grew to 8.2 percent from 7.7 percent at end 2009. Increases in provisions and revaluation losses in the trading book generated a loss for the system on a consolidated basis. All banks remained in compliance with the minimum capital adequacy requirement of 8 percent. The recent CEBS stress tests covered more than 90 percent of banking system assets and all but one bank passed. The results contributed to reduce market volatility.

13. **Liquidity conditions have remained strained although market volatility has declined.** The Greek banks have not regained access to wholesale markets to fund their operations and maturing interbank liabilities put pressure on their liquidity positions. The sovereign downgrade by Moody's in June put further pressure on collateral valuations and, to preserve adequate liquidity buffers in the sector, the authorities are committed to the adoption of the legislation enabling a new tranche of government guaranteed bank bonds in the amount of €25 billion (a prior action to proceed to the IMF Board meeting on September 10). Such guarantees will ensure sufficient loan provision from the ECB/Eurosystem to the Greek banks and economy, as well as to withstand possible further market turbulence.

14. **The FSF law was passed establishing a new backstopping facility for a sound level of bank equity.** On July 13 the Parliament enacted the Financial Stability Fund Law. Steps needed for the FSF to become operational by mid-September are well on course and it will receive its first tranche of funding at that time.

15. **Banking supervision is being strengthened.** Reporting requirements have heightened and reporting lags are being reduced. However expanding supervisory resources

is slow, especially taking into account the transfer of insurance supervision to the Bank of Greece. The necessary flexibility to address this issue will be provided.

16. **The government has commissioned an in-depth study on the strategic options for the banking sector.** In addition, the government has requested a preliminary due diligence analysis for those financial entities in which the state has a significant stake. Both the study and the due diligences will be completed by mid-September. Taking into account the outcome of the study and the due diligences, the Government, in consultation with experts, will formulate a program to preserve financial stability and enhance efficiency in the banking system.

17. **The authorities are following up on the result of the July 2010 CEBS stress tests.** While expecting the results of the due diligence, the single bank that did not pass the most stringent scenario will continue to implement interim restructuring measures under enhanced supervision by the BoG. The government has reaffirmed its full support to this bank and will ensure that it complies with the requirement of implementing a restructuring plan under the EU rules for state aid, including compliance with the 1 October 2010 deadline for submission.

18. **The Bank of Greece will maintain close coordination with home and host country supervisors.** Regular communications with regulators in SEE regarding risk assessments and liquidity contingency plans have intensified and participation in colleges of supervisors will continue. The authorities have also made good progress on their commitments under the MEFP and the personal insolvency law has been adopted after amending it to ensure that creditor's rights are adequately protected.

Structural reform policies

19. **Consistent with the May Memorandum, the government is making headway on structural reforms that promote growth, competitiveness, and reduce budgetary risks.** The potential for raising productivity and output growth is large. Unleashing growth potential requires pursuing a genuine competition culture and ensuring collective bargaining institutions that deliver wages commensurate with productivity. Also, the reform agenda aims at developing open markets in a business-friendly environment. Finally, measures are needed to remove restrictions that hamper activity, innovation, and reforms in state-owned enterprises, and to promote the absorption of structural funds.

20. **Labor market reform is almost completed.** Substantive legislative changes were introduced in July easing employment protection legislation and collective dismissals, reforming minimum wages, reducing overtime premia, and allowing firm-level agreements to prevail over other levels. Alongside reforms in public employment to reduce labor-market distortions, these will increase adjustment capacity of firms, ultimately boosting employment. Further measures will be taken to reform collective bargaining, including the elimination of the automatic extension of sectoral agreements to those not represented in the negotiations. Finally, the government will adopt legislation to introduce symmetry in the arbitration system while strengthening its independence and transparency.

21. **The government will reform and/or privatize state-owned enterprises:**

- **Railways.** The draft enabling law to restructure the railway sector will be discussed in parliament by end-September and, in parallel, the government will approve a business plan with time-bound actions. Cost reductions aim at significantly reducing fiscal pressures from the enterprises, while making the train operator profitable for the fiscal year 2011. The business plan will include a clear strategy to render the infrastructure manager economically viable over the medium term in line with EU law. If necessary, further measures will be implemented to ensure that financial objectives are achieved.
- **Energy.** The government will enable the effective liberalization of the wholesale electricity market and proceed with the rationalization of tariffs while ensuring vulnerable groups are protected.
- **Other state-owned enterprises.** Privatization could boost domestic and foreign direct investments and stimulate growth. Thus, a list of privatization projects has been identified and a fully elaborated plan will be prepared before end-December.

22. **Efforts are underway to increase competition and achieve a rebound in growth:**

- **Restricted professions.** Pervasive restrictions to entry in a number of important professions impose high costs on the economy. As a first step, the government will remove barriers in the legal, pharmacy, notary, architecture, engineering, and auditing professions. This will include reducing licensing requirements, geographic restrictions, and regulated tariffs.
- **Services sectors.** An ambitious and strategic implementation of the Services Directive will be pursued. In road freight transport, by end-September the government will seek approval for the law that removes restrictions on licenses and liberalizes prices.
- **Business environment.** The government will take measures to facilitate start-ups by making fully operational one-stop shops and eliminating unnecessary fees. On licensing, legislation will be adopted to simplify and accelerate the authorization for enterprises, industrial activities, and professions. Remaining restrictions to business activity and innovation will be identified and an action plan (“business friendly Greece”) will be formulated to remove the most important ones.
- **Tourism and retail.** The government will also commission a report analyzing the potential contributions of tourism and retailing to growth and jobs, and follow up with pointed actions and legislation.
- **HCC.** The government will amend the Greek Competition Act to strengthen the independence of the Hellenic Competition Committee and increase its effectiveness.

23. **The absorption of structural funds will be raised.** To enhance the growth impact of funds, recourse to non-targeted *de minimis* state aid measures will be gradually reduced. The government will adopt legislation to tackle delays related to environmental, archeological and expropriation impediments. A task force has been established to address these and other implementation bottlenecks.

Safeguards Assessment

24. **The Bank of Greece safeguards assessment has been completed by the IMF.** A Memorandum of Understanding between the Minister of Finance and the Bank of Greece Governor has been signed regarding the management and use of Fund disbursements.

Table 1. Greece: Quantitative Performance Criteria 1/
(Billions of euros)

	Jan-Jun 2010	Jan-Sep 2010	Jan-Dec 2010
1 Floor on primary balance			
Target	-5.0	-4.0	-5.7
Actual	-4.3		
Margin (+)	0.7		
2 Ceiling on state budget primary spending			
Target	34.0	50.0	67.0
Actual	28.4		
Margin (+)	5.6		
3 Ceiling on new domestic arrears 2/			
Target	0.0	0.0	0.0
Actual	1.0		
Margin (+)	-1.0		
4 Ceiling on the stock of debt			
Target	342.0	342.0	342.0
Actual	316.7		
Margin (+)	25.3		
5 Ceiling on new guarantees			
Target	2.0	2.0	2.0
Actual	0.3		
Margin (+)	1.7		
6 Ceiling on new external arrears			
Target	0.0	0.0	0.0
Actual	0.0		
Margin (+)	0.0		

Sources: LOI and MEFP; National authorities; and IMF staff calculations.

1/ As defined in the TMU.

2/ Indicative target.

Table 2: Greece: Structural Conditionality for 2010 1/

	Measures	Date	Status	Remarks
	Structural benchmarks	End-June		
1	Establish FSF		Observed	Law for FSF approved in parliament on July 13, 2010
2	Adopt Kallikratis law		Observed	Kallikratis Law approved in parliament on May 30, 2010
3	Adopt new Financial Management Law, amending the budget Law of 1995, and including: - 3-yr fiscal strategy - Top down budgeting with exp ceilings for state budget and expenditure estimates by line ministries - standard contingency margins - supplementary budget for overspending - commitment controls - effective for 2011 budget		Observed	New budget law approved in parliament on July 29, 2010
4	NAA to produce actuarial report		Incomplete	Rescheduled to end-December 2010 for main social security funds, and end-March 2011 for remaining supplementary funds, in recognition of size of task and to allow more data collection
Prior action for First Review Board Meeting				
1	Enactment of €25 billion bond guarantee tranche			To support bank liquidity
		End-September 2010		
1	Adopt comprehensive pension reform		Well advanced; and mostly observed, with follow up at end-December 2010 and end-March 2011	Pension reform law was adopted in parliament on July 8, 2010. Incremental pension costs now estimated at slightly above 2.5 percent of GDP. Safeguard clause to be triggered in June 2011 pending full actuarial report.
2	- Establish commitment register - Publish monthly data on GG - Report all arrears monthly			ongoing ongoing ongoing
3	Publish financial statement of 10 largest loss-making SOEs			ongoing
4	Kick-off the tax administration plan and set up five task forces - collection of tax arrears - Reorganize large tax payers unit - Strengthen audits for high-wealth and income individuals - Start prosecuting worst offenders - Strengthen filing and payment controls			Progress underway ;TA received with follow-up planned ongoing ongoing ongoing ongoing ongoing
		End-December 2010		
1	Report with single payment authorities on public sector remuneration structures			Work has begun; employment census has been completed
2	Adopt new regulations for Statistical Action Plan			Work has begun; MOUs are being drafted; Greece has received resident expert; new President of ELSTAT in place
3	Present detailed privatization plan with dates and revenue guidelines			Work has begun; potential privatization list has been drawn up; details need to be fleshed out

1/ Benchmarks for 2011 to be set in reviews for end-September and end-December 2010 (second and third review).

GREECE: TECHNICAL MEMORANDUM OF UNDERSTANDING

August 6, 2010

25. This Technical Memorandum of Understanding (TMU) sets out the understandings regarding the definitions of the indicators subject to quantitative targets (performance criteria and indicative targets), specified in the tables annexed to the Memorandum of Economic and Financial Policies. It also describes the methods to be used in assessing the program performance and the information requirements to ensure adequate monitoring of the targets. We will consult with the Fund, European Commission and ECB before modifying measures contained in this letter, or adopting new measures that would deviate from the goals of the program, and provide the European Commission, ECB and the Fund with the necessary information for program monitoring.

26. For program purposes, all foreign currency-related assets, liabilities, and flows will be evaluated at “program exchange rates” as defined below, with the exception of the items affecting government fiscal balances, which will be measured at current exchange rates. The program exchange rates are those that prevailed on April 30, 2010. In particular, the exchange rates for the purposes of the program are set €1 = 1.3315 U.S. dollar, €1 = 125.81 Japanese yen, €1.135 = 1 SDR.

General Government

27. **Definition:** For the purposes of the program, the general government includes:

- The central government. This includes:
 - The entities covered under the State Budget as defined in Chapter 2 of the Law 2362/1995 regarding “Public Accounting, Auditing of Government Expenditures and Other Regulations.”
 - Other entities or extra-budgetary funds (EBFs) not part of the State budget, but which are, under European System of Accounts (ESA95) rules (“*ESA95 Manual on Government Deficit and Debt*”), classified under central government.
- Local government comprising municipalities, prefectures, and regional governments including their basic and special budgets, including all agencies and institutions attached thereto, which are classified as local governments according to ESA 95.
- Social security funds comprising all funds that are established as social security funds in the registry of the National Statistical Service.
- This definition of general government also includes any new funds, or other special budgetary and extra budgetary programs that may be created during the program

- period to carry out operations of a fiscal nature. The government will inform IMF, European Commission and ECB staff of the creation of any such new funds, programs, or entities immediately. The general government, as measured for purposes of the program, shall not include entities that are re-classified from outside general government into general government during the course of 2010.

28. **Supporting material:** The Ministry of Finance (MoF) will provide to the European Commission, ECB and IMF detailed information on monthly revenues and expenditures, domestic and foreign debt redemptions, new domestic and foreign debt issuance, change in the domestic and foreign cash balances of the central government at the central bank of Greece, all other sources of financing including capital transactions, and arrears of the general government. Data will be provided within 30 days. The Bank of Greece will provide detailed monthly data on assets and liabilities of local authorities and social security funds in line with monetary survey data.

I. QUANTITATIVE PERFORMANCE CRITERIA, INDICATIVE CEILINGS, AND CONTINUOUS PERFORMANCE CRITERIA: DEFINITIONS AND REPORTING STANDARDS

A. Floor of the Modified General Government Primary Cash Balance (Performance Criterion)

29. **Definition:** The modified general government primary cash balance (MGGPCB) is defined as the modified general government cash balance (MGGCB) minus interest payments by the state budget. The MGGCB is defined as the sum of the cash balances of the ordinary state budget, the cash balance of the public investment budget, the change in net financial assets of local government, the change in net financial assets of social security funds, and the change in net financial assets of extra-budgetary funds. Privatization receipts will be excluded from cash receipts. Net lending operations by the state budget will be recorded as cash expenditures.

- **The cash balance of the ordinary state budget.** The cash balance of the ordinary state budget will be measured from above the line, based on ordinary budget revenues (recurrent revenue plus non-recurrent revenue minus tax refunds) minus ordinary budget expenditures (ordinary budget expenditures will exclude amortization payments but include salaries and pensions; grants to social security funds, medical care and social protection; operational and other expenditure; returned resources; payments in exchange of claims of insurance fund for the personnel working in the Public Electricity Company; interest payments; payments for military equipment procurement on a cash basis; and NATO expenses net of NATO revenues) of the ordinary state budget as published monthly on the official website of the General Accounting Office of the Ministry of Finance, and in line with the corresponding line items established in the ordinary state budget. Primary spending of the ordinary state budget shall also include capital transfers to social security funds by bonds, and called

- guarantees where the state or central government assumes payments on behalf of entities outside of the general government.
- **The cash balance of the public investment budget.** The cash balance of the public investment budget will be measured from above the line, based on investment budget revenues minus investment budget expenditures of the investment state budget as published monthly on the official website of the General Accounting Office of the Ministry of Finance, and in line with the corresponding line items established in the investment state budget.
- **The change in net financial assets of local governments** is defined on a transactions basis, as the change in the total of financial assets minus financial liabilities of local authorities adjusted for valuation changes by the Bank of Greece.
 - Financial assets include (but are not limited to) deposits of local governments in the Bank of Greece and deposits of local governments in the commercial domestic banking sector and in the Consignment Fund. Deposits will be measured at face value excluding accrued interest in line with recording for monetary survey data.
 - Financial liabilities include (but are not limited to) short and long term loans from the domestic banking system and in the Consignment Fund to local governments, measured at face value, consistent with recording for monetary survey data.
- **The change in net financial assets of social security funds** is defined on a transactions basis, as the change in the total of financial assets minus financial liabilities of social security funds, adjusted for valuation changes by the Bank of Greece; minus the change in the stock of accounts payable of public hospitals to the private sector.
 - Financial assets include
 - Deposits of social security funds in the Bank of Greece and direct deposits of social security funds in the domestic commercial banking system and indirect deposits held by the IKA mutual fund. Deposits are measured at face value excluding accrued interest, consistent with reporting requirements for monetary survey data.
 - Holdings of direct shares or indirect shares (through the IKA mutual fund), held by social security funds quoted on the Athens Stock Exchange.

- Direct or indirect holdings of Mutual Fund units issued by Greek management companies (other than the IKA mutual fund).
- Holdings of central government bonds, including short and long-term securities issued domestically, long-term securities issued abroad operated from Bank of Greece accounts, and indirect holdings through the IKA mutual fund. Holdings will be measured at nominal value.
- Bank bonds issued abroad.
- Financial liabilities include the short and long term loans from the domestic banking system to the social security funds, measured consistently with monetary survey data.
- The change in the stock of accounts payable of public hospitals to the private sector.
- **The change in net financial assets of extra-budgetary funds (EBFs)** is defined on a transactions basis, as the change in the total of financial assets minus financial liabilities of extra-budgetary funds, adjusted for valuation changes by the Bank of Greece. EBFs shall exclude ELGA and OPEKEPE.
 - Financial assets include
 - Deposits of EBFs in the Bank of Greece and deposits of EBFs in the commercial domestic banking sector. Deposits will be measured at face value excluding accrued interest in line with recording for monetary survey data.
 - Holdings of shares, held by EBFs quoted on the Athens Stock Exchange.
 - Direct or indirect holdings of Mutual Fund units issued by Greek management companies.
 - Holdings of central government bonds.
 - Bank bonds issued abroad.
 - Financial liabilities include the short and long term loans from the domestic banking system to EBFs, measured consistently with monetary survey data.

30. **Other provisions.**

- For the purpose of the program, the primary expenditure of the central government that is monitored excludes payments related to bank support, when carried out under the program's banking sector support and restructuring strategy. Transactions that may be excluded from the balance include loans to financial institutions and investments in equity of financial institutions (requited recapitalization); unrequited recapitalization; and purchases of troubled assets. However, any financial operation by central government to support banks, including the issuance of guarantees or provision of liquidity, will be immediately reported to IMF, European Commission and ECB staff.
- For 2010, capital transfers to social security funds by bonds and called guarantees will be excluded from primary spending. Similarly, during 2010, changes in the stock of accounts payable of public hospitals to the private sector will be excluded from the change in net financial assets of social security funds; the change in net financial assets of EBFs will also be excluded from the modified general government primary cash balance during 2010. However, from the 2011 fiscal year onward, these factors will be included.

31. **Revenue adjuster.** Further, this performance criterion will be adjusted upward for any possible revenue over-performance in the central government against the current projection as indicated below: Central government revenue (Cumulative from January 1, 2010)

- June 2010: €25,056 million
- September 2010: €41,232 million
- December 2010: €58,382 million.

32. **Supporting material.**

- Data on cash balances of the ordinary and state budgets will be provided to the European Commission, ECB and IMF by the General Accounting Office in the Ministry of Finance within three weeks after the end of the month. Data will include detailed information on revenue and expenditure items, in line with monthly reports that are published since January 2010 on the official website of the Ministry of Finance. Data will also include data on capital transfers to social security funds in bonds, and called guarantees.
- Data on net financial assets of local authorities and social security funds, and extra-budgetary funds will be provided to the IMF, European Commission and ECB by the

- Statistics Department of the Bank of Greece within four weeks after the end of the month. Data on accounts payable of public hospitals will be provided by the Ministry of Health.

B. Ceiling of State Budget Primary Spending (Performance Criterion)

33. **Definition:** The state budget primary spending consists of state budget spending (spending of the ordinary state budget plus spending of the public investment budget) minus interest expenditures paid by the state budget, in line with the definitions provided above. Primary expenditure of the central government that is monitored for the Performance Criterion excludes any cash payments related to bank restructuring, when carried out under the program's banking sector restructuring strategy. Costs that may be excluded from the balance include loans to financial institutions and investments in equity of financial institutions (requited recapitalization); unrequited recapitalization; and purchase of troubled assets. However, any financial operation by central or general government to support banks, including the issuance of guarantees or provision of liquidity, will be immediately reported to European Commission, ECB and IMF staff.

34. **Other provisions.** Capital transfers to social security funds by bonds and called guarantees will be excluded from primary spending during 2010. However, from the 2011 fiscal year onward, such exclusion will no longer apply.

35. **Supporting material.** The General Accounting Office of the Ministry of Finance will provide monthly expenditure data of the ordinary and investment state budget, as defined above.

C. Non-accumulation of Domestic Arrears by the General Government (Continuous Indicative Target)

36. **Definition.** For the purpose of the program, domestic arrears are defined as accounts payable to domestic suppliers past due date by 90 days. In case no due date is specified on the supplier contract, the due date is assumed to be 90 days of the initiation of the billing invoice. Data will be provided within four weeks after the end of the month. The continuous non-accumulation of domestic arrears is defined as no accumulation of arrears at the end of every month during which quarter the indicative target is being monitored.

37. **Supporting material.** The Ministry of Finance will provide data on monthly expenditure arrears of the general government, as defined above. Data will be provided within four weeks after the end of the month.

D. Ceiling on the Overall Stock of Central Government Debt (Performance Criterion)

38. **Definition.** The overall stock of central government debt will refer to debt that corresponds to the activities of the state budget and will be defined for the purposes of the

program as the total outstanding gross debt liabilities of the central government. It will include, but not be limited to, liabilities in the form of securities and loans. It will exclude accounts payable. Debt will be measured at nominal value. The program exchange rate will apply to all non-euro denominated debt. Inflation indexation will apply to inflation indexed debt, using the relevant index as specified in the debt instrument. For the purposes of the program, the ceiling on the stock of central government debt will exclude debt arising from payments for bank restructuring, when carried out under the program's banking sector restructuring strategy. This includes loans to financial institutions and investments in equity of financial institutions (requited recapitalization); unrequited recapitalization; and purchase of troubled assets. However, any financial operation by the central government to support banks, including the issuance of guarantees or provision of liquidity, with the exception of Hellenic Republic intermediation in repos between foreign and domestic financial institutions will be immediately reported to IMF, European Commission and ECB staff.

39. **Adjusters.** The ceiling on the overall stock of central government debt will be adjusted upward (downward) by the amount of any upward (downward) revision to the stock of end-December 2009 central government debt. In addition, the ceiling on the overall stock of central government debt will also be revised upward by the amount of debt assumed by the central government following the railway sector restructuring.

40. **Supporting material.** Data on the total stock of central government debt will be provided to the European Commission, ECB and IMF staff by the General Accounting Office consistent with the debt published in the public debt bulletin no later than 30 days after the end of each month.

E. Ceiling on New Central Government Guarantees (Performance Criterion)

41. **Definition.** The ceiling on the new central government guarantees shall include new guarantees granted by the state, as well as new guarantees granted by any other entity that is classified under ESA95 under central government. Guarantees issued by TEMPME shall be included in the ceiling. The ceiling shall exclude guarantees to support banks and exclude guarantees related to EIB financed loans. New guarantees are guarantees extended during the current fiscal year. The latter shall include also guarantees for which the maturity is being extended beyond the initial contractual provisions.

42. **Other provisions.** The end-September 2010 PC on new central government guarantees shall exclude any new guarantees extended by entities (including TEMPME) other than the state. For the end-December 2010 PC on new central government guarantees, these factors shall be included on a cumulative basis starting October 1, 2010.

43. **Supporting material.** All new central government guarantees will be reported in detail, identifying amounts and beneficiaries. The General Accounting Office will provide the data on a monthly basis within three weeks after the end of each month. Non-state entities classified under the central government shall report the new guarantees they extended to the

General Accounting Office on a monthly basis within three weeks after the end of each month.

F. Non-accumulation of External Debt Payments Arrears by the General Government (Continuous Performance Criteria)

44. **Definition.** For the purposes of the program, an external debt payment arrear will be defined as a payment on debt to non-residents contracted or guaranteed by the general government, which has not been made within seven days after falling due. The performance criterion will apply on a continuous basis throughout the program period.

45. **Supporting material.** The stock of external arrears of the general government system will be provided by the General Accounting Office with a lag of not more than seven days after the test date.

G. Overall Monitoring and Reporting Requirements

46. Performance under the program will be monitored from data supplied to the EC, ECB and IMF by the Ministry of Finance, the General Accounting Office, and Bank of Greece. The authorities will transmit to the IMF, EC and ECB staff any data revisions in a timely manner.

H. Monitoring of Structural Benchmarks

47. **Pension reform.** Parliament adopted separate laws reforming pensions for the public and private sector in mid-July, ahead of the end-September deadline under the program. An actuarial evaluation of this law is currently underway. The National Actuarial Authority will complete an assessment of the effects of the reform on the main pension funds by the end of December 2010, which will be expanded to include the largest auxiliary pension funds by end of March 2011. This actuarial assessment will determine whether further adjustments to the pension system would be needed to contain the increase in pension spending 2010–2060 at 2.5 percentage points of GDP. Any needed adjustments to the parameters of the main pensions will be completed by end of June 2011 in consultation with the EC/IMF/ECB; and a full review of the auxiliary and welfare funds would be completed by end of December 2011.

48. **Financial information of the ten largest loss-making public enterprises.** The ten largest loss-making public enterprises will be defined based on the 2009 net income, after state budget subsidies. Net income will be defined based on financial statements that are compiled in line with Greek accounting standards. Published information on financial statements, however, will include the IFRS financial statements.

**GREECE: LETTER OF INTENT AND MEMORANDUM OF UNDERSTANDING
ON SPECIFIC ECONOMIC POLICY CONDITIONALITY**

Athens, 6 August 2010

Mr. Jean-Claude Juncker
President
Eurogroup

Mr. Olli Rehn
Commissioner for Economic and Monetary Affairs
European Commission

Mr Jean-Claude Trichet
President
European Central Bank

Dear Messrs. Juncker, Rehn and Trichet,

In the attached update to the Memorandum of Economic and Financial Policies (MEFP) and the Memorandum of Understanding on Specific Economic Policy Conditionality of 3 May 2010, we describe the progress and further policy steps towards meeting the objectives of the economic program that is being supported by financial assistance provided by the euro-area Member States in the context of the loan facility agreement. The policies of the government of Greece remain fully oriented toward securing fiscal sustainability, safeguarding the stability of the financial system, and boosting potential growth and competitiveness.

We have made a vigorous start with our economic program. The fiscal program is progressing well, financial policies are being strengthened, and structural policies are ahead of schedule in key aspects:

- The end-June quantitative performance criteria have all been met, led by a strong implementation of the fiscal program. Not unexpectedly, it has proven difficult to fully control expenditures at some entities, and in anticipation of such problems we significantly under-executed budget implementation at the state level, thereby ensuring that targets for the general government were met. Going forward, we are redoubling our efforts to strengthen controls at all levels of government and are determined to continue to over-perform at the state level until such controls become fully effective.
- Reflecting the weaknesses in expenditure controls at some entities, the indicative target on the non-accrual of domestic arrears has not been observed as the monitoring system for general government commitments, accounts payable, and arrears is still

- being developed and implemented. We commit to bringing these arrears down to zero by year-end, so that only a normal level of accounts payable is carried over into 2011.
- While the financial system continues to feel the effects of tight liquidity, sentiment indicators are gradually beginning to improve, and policy progress has been made by establishing the Financial Stability Fund to backstop any capital needs that banks might have in the future owing to an expected increase in impaired loans as the recession runs its course. Stress tests suggest that the funds earmarked for the FSF under the program remain fully adequate.
- The government has made significant progress in structural reforms with far-reaching pension and labor market reforms being approved ahead of schedule. Parliament has also already adopted important budgetary reform and reforms of local government. Other major reforms that are at an advanced stage aim at liberalizing the trucking industry and restructuring the railroad system, while reforms of the energy sector, protected professions, the licensing and business regulatory framework and preparations for implementation of the services directive are gaining momentum, as foreseen in our program.

On this basis and the completion of the prior action, we request the disbursement of the second instalment of financial assistance by the euro-area Member States in the amount of EUR 6 500 million, in line with the loan facility agreement.

We believe that the policies set forth in the 3 May 2010 Letter of Intent, MEFP and MoU, and the attached updates, are adequate to achieve the objectives under the program. We stand ready to take any corrective actions that may become appropriate for this purpose as circumstances change. We will consult with the European Commission and the ECB, as well as with the IMF, on the adoption of any such actions and in advance of revisions to the policies contained in this letter.

We are copying this letter to Mr. Strauss-Kahn, Managing Director of the IMF.

Sincerely,

/s/

George Papaconstantinou
Minister of Finance

/s/

George Provopoulos
Governor of the Bank of Greece

Athens, August 6, 2010

Greece—Memorandum of Economic and Financial Policies

49. **The government has made a vigorous start at implementing its economic program.** The fiscal program is progressing well, financial policies are being strengthened, and structural policies are ahead of schedule in key respects. The May 2010 Letter of Intent (LOI) and Memorandum of Economic and Financial Policies (MEFP) describing the 3-year economic program remain fully in force. This update to the MEFP combined with the updated MoU presents a review of achievements and policy steps toward the second review scheduled for late 2010.

50. **The growth outlook remains unaltered; short-run inflation is revised up.** The government continues to envisage a contraction of activity by about 4 percent in 2010 and some 2½ percent in 2011. However, because the government frontloaded a number of large indirect tax increases, which have been passed on as a step up in the price level, the rate of consumer price inflation and the implicit deflator have increased. The high pass through of indirect tax increases to final prices is indicative of a lack of competition and the prevalence of oligopolistic market structures. HICP inflation is now expected to approach 4¾ percent for the year. Inflation at constant taxes is falling and has declined below the euro-area average for the first time since the creation of the euro. Moreover, there is no evidence of pass through of higher prices to wages, and the national collective agreement just signed contributes to moderating wage growth and improving competitiveness.

Fiscal Policies

51. **The fiscal program is making good progress.** The cash state budget is leading the consolidation effort with an impressive cut in its deficit by over 40 percent in Jan-Jun (y/y). Current revenue has increased in the Jan-Jun period by 7 percent, despite the deepening recession, and current expenditure and transfers have been cut by some 10 percent. Local governments, hospitals, and social security funds have also taken steps but their progress is more gradual as controlling their expenditures is more difficult, as was expected. Through June, the large margin under the targets created in the state budget has offset the overruns to date in subnational entities. However, there has been some undesirable buildup in accounts payable/arrears in hospitals and social security funds and, as described below, steps are underway to gain a firmer grip on risks for the targets going forward.

52. **Looking to the second half of the year and consistent with the May program, the government will limit the annual general government fiscal deficit (on accrual terms) to €18.5 billion:**

- **Continuing implementation of the measures:** The fiscal measures (VAT and excises, and particular the benefits from the pension and wage cuts) will be fully realized in the second half of the year and should generate substantial resources to allow all payments and the amortization of any mid-year arrears by end-2010.

- **Under-execution of spending:** In the January-June period, the government under-executed state budget primary spending by €5.6 billion. The government intends to maintain this overperformance through September, and to end the year by a margin of overperformance of €4 billion to cover risks coming from other parts of general government. The expenditure containment will focus on operating expenses while making all required transfers to the social security funds and local governments to allow them to become current in their payments. At any time, should performance run short of these objectives, or revenue drop below schedule, the government stands ready to take corrective actions.

53. **The government achieved an important milestone in end-July by passing a new budget law that strengthens the fiscal management framework.** This implies that the budget for 2011 will be part of a three-year rolling medium-term framework, and that the Minister of Finance will be able to set top-down expenditure ceilings for line ministries, local governments and social budgets so as to broaden the scope of fiscal policy to general government. Also, the budget will now contain standard contingency margins to facilitate absorbing shocks, and the government will set up commitment registers in the line ministries (a structural benchmark for end-September) to manage better accrual spending—beyond cash outlays. In addition, the government is also developing monthly fiscal reporting for general government entities (a benchmark by end-September).

54. **The preparation of general government budgets for 2011 in line with the new budget law commitments is underway.** The budgets will be prepared under the new law and the government will present the pre-budget to parliamentary committees in early October together with the consolidated draft local government and social budgets and consistent with a general government fiscal deficit target (in ESA95 terms) of €17 billion in 2011. The government will take into account the sustainability of discretionary spending cuts, and if needed replace them with permanent savings. At the same time, the government will put in place the 2011 fiscal measures that were agreed in May.

55. **In line with the original Memorandum, the government will focus on bolstering tax administration and fighting tax evasion in the months ahead.** Improving tax administration is essential for fairness in the adjustment program and to facilitate broadening the tax base, with moderate average tax rates. The government will kick-start the improved tax administration by implementing the recommendations received from technical experts. By end-September, the government will set up five dedicated task forces to:

- Ensure prompt implementation of the new tax legislation,
- collect tax arrears,
- reorganize the large tax payers unit,
- strengthen the audits for high-wealth and income individuals,
- strengthen filing and payment controls, and improving tax payer services.

Meanwhile, the government will make intensive use of payments receipts to bolster tax compliance, and cross-check tax information with data on wealth and spending habits to reduce tax abuse and evasion in particular of high-income and wealthy tax payers, while also

reviewing the existing legal processes to ensure timely and effective prosecution of tax offenders.

56. **Public administration reform is advancing.** The government is setting up a single payment authority through which wages of civil servants in central government will be paid by end 2010 and for general government by March 2011. Plans to move in 2011 to a simplified remuneration system are facilitated by the completed public employment census. A functional review of central administration, beginning in the second half of 2010, will seek to identify operational steps to rationalize and make more efficient the public administration.

57. **The government envisages specific efforts to limit risks to its program, in particular to help strengthen expenditure control in subnational entities.**

- *Health sector.* In the hospital sector the government will accelerate payments to avoid the buildup of arrears and to limit the carryover of obligations into 2011. Further, the government has reduced procurement prices of pharmaceuticals by 20 percent by implementing price caps for approved drugs lists, and improved profiles and benchmarking for patients and doctors to avoid unnecessary prescriptions, which should yield important savings during the second half of this year. Indeed, the government stands ready to reduce pharmaceutical costs further (where there is room to expand the drugs lists, the use of generics, and by introducing e-prescriptions). The government will enforce the €3 for regular outpatient services in public hospitals and extend the “all day” operation of hospitals (afternoon shift) in order to develop and improve healthcare services and increase hospital revenues, including with increased copayments of outpatient and diagnostic services. The government has placed accounting firms in state hospitals to improve their financial management to gain control over spending and accounts payable.
- *Local governments.* The recently passed Kallikratis bill for local government reform will sharply reduce the number of local administrations, entities, and elected and appointed officials. The government will tightly implement the bill, in particular the targeted employment reduction and efficiency-enhancing reforms to secure improved budgetary results of €500 million subsequently in each of the three years during 2011-13. To ensure that those savings contribute to the overall fiscal consolidation of general government, the government will limit borrowing, reduce transfers, and control local government budgets consistent with the medium-term fiscal strategy.
- *State enterprises.* The government will strengthen performance of the major loss-making public enterprises in order to reduce contingent risks to the budget, including by enhancing efficiency, increasing tariffs in public transportation, and further reducing excessive allowances and overtime. In particular, the government will restructure the loss-making railroad enterprise as described below. Under the restructuring plan operating PSO’s (public service obligation—subsidies) will be limited to €50 million per year, and no new debt guarantees by the state will be provided to the restructured rail enterprise, which has to break with a long history of large losses. The 10 largest loss-making enterprises will have their financial

statements through 2009 published on the web before end-September (structural benchmark) to enhance transparency in their financial condition.

58. **Parliament approved a substantial pension reform ahead of schedule.** It introduces a new system consisting of a contributory pension to top-up a non-contributory, means-tested, basic pension, aiming to control the increase in pension spending. The National Actuarial Authority will complete an assessment of the effects of the reform on the main pension funds by end-December 2010, and of the largest auxiliary pension funds by end-March 2011. These assessments will determine whether further adjustments to the parameters of the pension system would be needed to contain the increase in pension spending to 2.5 ppts of GDP between 2009-2060. Any further adjustments, if needed, will be completed by end of June 2011 in consultation with pension experts, as foreseen in Law 3863.

59. **Financing and cash management.** The latest assessment confirms that the state financing need in 2010–11 remains fully financed from the loans of the Euro-area member states and the IMF, with the government able—as foreseen in the program—to roll over its relatively small stock of T-bills. However, the tight liquidity position will require careful cash management. In this light, the public debt management agency will start monthly T-bill auctions beginning in September (from quarterly placements) to improve cash management and smooth maturity profiles.

Financial Sector Policies

60. **The Greek banking system continues to face a challenging environment.** In the first quarter of the year the banking system capital ratio declined by 0.05 percentage points to 11.7 percent as non performing loans grew to 8.2 percent from 7.7 percent at end 2009. Increases in provisions and revaluation losses in the trading book generated a loss for the system on a consolidated basis. All banks remained in compliance with the minimum capital adequacy requirement of 8 percent. The recent CEBS stress tests covered more than 90 percent of banking system assets and all but one bank passed. The results contributed to reduce market volatility.

61. **Liquidity conditions have remained strained although market volatility has declined.** The Greek banks have not regained access to wholesale markets to fund their operations and maturing interbank liabilities put pressure on their liquidity positions. The sovereign downgrade by Moody's in June put further pressure on collateral valuations and, to preserve adequate liquidity buffers in the sector, the authorities are committed to the adoption of the legislation enabling a new tranche of government guaranteed bank bonds in the amount of €25 billion (a prior action to proceed to the IMF Board meeting on September 10). Such guarantees will ensure sufficient loan provision from the ECB/Eurosystem to the Greek banks and economy, as well as to withstand possible further market turbulence.

62. **The FSF law was passed establishing a new backstopping facility for a sound level of bank equity.** On July 13 the Parliament enacted the Financial Stability Fund Law. Steps needed for the FSF to become operational by mid-September are well on course and it will receive its first tranche of funding at that time.

63. **Banking supervision is being strengthened.** Reporting requirements have heightened and reporting lags are being reduced. However expanding supervisory resources is slow, especially taking into account the transfer of insurance supervision to the Bank of Greece. The necessary flexibility to address this issue will be provided.

64. **The government has commissioned an in-depth study on the strategic options for the banking sector.** In addition, the government has requested a preliminary due diligence analysis for those financial entities in which the state has a significant stake. Both the study and the due diligences will be completed by mid-September. Taking into account the outcome of the study and the due diligences, the Government, in consultation with experts, will formulate a program to preserve financial stability and enhance efficiency in the banking system.

65. **The authorities are following up on the result of the July 2010 CEBS stress tests.** While expecting the results of the due diligence, the single bank that did not pass the most stringent scenario will continue to implement interim restructuring measures under enhanced supervision by the BoG. The government has reaffirmed its full support to this bank and will ensure that it complies with the requirement of implementing a restructuring plan under the EU rules for state aid, including compliance with the 1 October 2010 deadline for submission.

66. **The Bank of Greece will maintain close coordination with home and host country supervisors.** Regular communications with regulators in SEE regarding risk assessments and liquidity contingency plans have intensified and participation in colleges of supervisors will continue. The authorities have also made good progress on their commitments under the MEFP and the personal insolvency law has been adopted after amending it to ensure that creditor's rights are adequately protected.

Structural reform policies

67. **Consistent with the May Memorandum, the government is making headway on structural reforms that promote growth, competitiveness, and reduce budgetary risks.** The potential for raising productivity and output growth is large. Unleashing growth potential requires pursuing a genuine competition culture and ensuring collective bargaining institutions that deliver wages commensurate with productivity. Also, the reform agenda aims at developing open markets in a business-friendly environment. Finally, measures are needed to remove restrictions that hamper activity, innovation, and reforms in state-owned enterprises, and to promote the absorption of structural funds.

68. **Labor market reform is almost completed.** Substantive legislative changes were introduced in July easing employment protection legislation and collective dismissals, reforming minimum wages, reducing overtime premia, and allowing firm-level agreements to prevail over other levels. Alongside reforms in public employment to reduce labor-market distortions, these will increase adjustment capacity of firms, ultimately boosting employment. Further measures will be taken to reform collective bargaining, including the elimination of the automatic extension of sectoral agreements to those not represented in the

negotiations. Finally, the government will adopt legislation to introduce symmetry in the arbitration system while strengthening its independence and transparency.

69. **The government will reform and/or privatize state-owned enterprises:**

- **Railways.** The draft enabling law to restructure the railway sector will be discussed in parliament by end-September and, in parallel, the government will approve a business plan with time-bound actions. Cost reductions aim at significantly reducing fiscal pressures from the enterprises, while making the train operator profitable for the fiscal year 2011. The business plan will include a clear strategy to render the infrastructure manager economically viable over the medium term in line with EU law. If necessary, further measures will be implemented to ensure that financial objectives are achieved.
- **Energy.** The government will enable the effective liberalization of the wholesale electricity market and proceed with the rationalization of tariffs while ensuring vulnerable groups are protected.
- **Other state-owned enterprises.** Privatization could boost domestic and foreign direct investments and stimulate growth. Thus, a list of privatization projects has been identified and a fully elaborated plan will be prepared before end-December.

70. **Efforts are underway to increase competition and achieve a rebound in growth:**

- **Restricted professions.** Pervasive restrictions to entry in a number of important professions impose high costs on the economy. As a first step, the government will remove barriers in the legal, pharmacy, notary, architecture, engineering, and auditing professions. This will include reducing licensing requirements, geographic restrictions, and regulated tariffs.
- **Services sectors.** An ambitious and strategic implementation of the Services Directive will be pursued. In road freight transport, by end-September the government will seek approval for the law that removes restrictions on licenses and liberalizes prices.
- **Business environment.** The government will take measures to facilitate start-ups by making fully operational one-stop shops and eliminating unnecessary fees. On licensing, legislation will be adopted to simplify and accelerate the authorization for enterprises, industrial activities, and professions. Remaining restrictions to business activity and innovation will be identified and an action plan (“business friendly Greece”) will be formulated to remove the most important ones.
- **Tourism and retail.** The government will also commission a report analyzing the potential contributions of tourism and retailing to growth and jobs, and follow up with pointed actions and legislation.

- **HCC.** The government will amend the Greek Competition Act to strengthen the independence of the Hellenic Competition Committee and increase its effectiveness.

71. **The absorption of structural funds will be raised.** To enhance the growth impact of funds, recourse to non-targeted *de minimis* state aid measures will be gradually reduced. The government will adopt legislation to tackle delays related to environmental, archeological and expropriation impediments. A task force has been established to address these and other implementation bottlenecks.

Safeguards Assessment

72. **The Bank of Greece safeguards assessment has been completed by the IMF.** A Memorandum of Understanding between the Minister of Finance and the Bank of Greece Governor has been signed regarding the management and use of Fund disbursements and there are no outstanding issues.

Table 1. Greece: Quantitative Performance Criteria 1/
(Billions of euros)

	Jan-Jun 2010	Jan-Sep 2010	Jan-Dec 2010
1 Floor on primary balance			
Target	-5.0	-4.0	-5.7
Actual	-4.3		
Margin (+)	0.7		
2 Ceiling on state budget primary spending			
Target	34.0	50.0	67.0
Actual	28.4		
Margin (+)	5.6		
3 Ceiling on new domestic arrears 2/			
Target	0.0	0.0	0.0
Actual	1.0		
Margin (+)	-1.0		
4 Ceiling on the stock of debt			
Target	342.0	342.0	342.0
Actual	316.7		
Margin (+)	25.3		
5 Ceiling on new guarantees			
Target	2.0	2.0	2.0
Actual	0.3		
Margin (+)	1.7		
6 Ceiling on new external arrears			
Target	0.0	0.0	0.0
Actual	0.0		
Margin (+)	0.0		

Sources: LOI and MEFP; National authorities; and IMF staff calculations.

1/ As defined in the TMU.

2/ Indicative target.

Table 2: Greece: Structural Conditionality for 2010 1/

	Measures	Date	Status	Remarks
	Structural benchmarks	End-June		
1	Establish FSF		Observed	Law for FSF approved in parliament on July 13, 2010
2	Adopt Kallikratis law		Observed	Kallikratis Law approved in parliament on May 30, 2010
3	Adopt new Financial Management Law, amending the budget Law of 1995, and including: - 3-yr fiscal strategy - Top down budgeting with exp ceilings for state budget and expenditure estimates by line ministries - standard contingency margins - supplementary budget for overspending - commitment controls - effective for 2011 budget		Observed	New budget law approved in parliament on July 29, 2010
4	NAA to produce actuarial report		Incomplete	Rescheduled to end-December 2010 for main social security funds, and end-March 2011 for remaining supplementary funds, in recognition of size of task and to allow more data collection
Prior action for First Review Board Meeting				
1	Enactment of €25 billion bond guarantee tranche			To support bank liquidity
		End-September 2010		
1	Adopt comprehensive pension reform		Well advanced; and mostly observed, with follow up at end-December 2010 and end-March 2011	Pension reform law was adopted in parliament on July 8, 2010. Incremental pension costs now estimated at slightly above 2.5 percent of GDP. Safeguard clause to be triggered in June 2011 pending full actuarial report.
2	- Establish commitment register - Publish monthly data on GG - Report all arrears monthly			ongoing ongoing ongoing
3	Publish financial statement of 10 largest loss-making SOEs			ongoing
4	Kick-off the tax administration plan and set up five task forces - collection of tax arrears - Reorganize large tax payers unit - Strengthen audits for high-wealth and income individuals - Start prosecuting worst offenders - Strengthen filing and payment controls			Progress underway ;TA received with follow-up planned ongoing ongoing ongoing ongoing ongoing
		End-December 2010		
1	Report with single payment authorities on public sector remuneration structures			Work has begun; employment census has been completed
2	Adopt new regulations for Statistical Action Plan			Work has begun; MOUs are being drafted; Greece has received resident expert; new President of ELSTAT in place
3	Present detailed privatization plan with dates and revenue guidelines			Work has begun; potential privatization list has been drawn up; details need to be fleshed out

1/ Benchmarks for 2011 to be set in reviews for end-September and end-December 2010 (second and third review).

GREECE**Updated Memorandum of Understanding
on
Specific Economic Policy Conditionality**

August 6, 2010

The quarterly disbursements of bilateral financial assistance from euro area Member States will be subject to quarterly reviews of conditionality for the duration of the arrangement. The release of the tranches will be based on observance of quantitative performance criteria, and a positive evaluation of progress made with respect to policy criteria in the MEFP and in this Memorandum, which specifies the detailed criteria that will be assessed for the successive reviews, up to the end of 2011. Detailed criteria for the structural reform requirements in 2010 and 2011 have been updated and further specified during the summer 2010 mission.

The authorities commit to consult with the European Commission, the ECB and the IMF staffs on adoption of policies falling within the scope of this Memorandum allowing sufficient time for review. They will also provide them with all requested information for monitoring progress during program implementation and the economic and financial situation (Annex 1). Government provides quarterly a report in line with Article 4 of Council Decision 2010/320/EU.¹⁰

1. Actions for the second review (actions to be completed by end Q3-2010)**i. Fiscal consolidation**

Rigorously implement the budget for 2010 and the fiscal consolidation measures announced afterwards, including those in this Memorandum (including its previous version).

The Ministry of Finance ensures tight supervision of expenditure commitments by the government departments, and effective tax collection, to make certain that the general government deficit targets in cash and ESA95 bases (cumulative quarterly deficit ceilings in the Memorandum of Economic and Financial Policies (MEFP) including the Technical Memorandum of Understanding (TMU); and Article 1 of Council Decision 2010/320/EU) are achieved.

The 2011 budget will provide information and reliable projections on the entire general government sector and target a further reduction of the general government deficit in line with the original MEFP. It includes a detailed presentation of fiscal consolidation measures amounting to at least 3.2% of GDP (4.3% of GDP, if carryovers from measures implemented in 2010 are considered), and detailed information on the situation of public enterprises.

¹⁰ OJ L 145, 11.6.2010, p. 6.

The budget will include the following measures, as planned in the original version of this Memorandum (in exceptional circumstances, measures yielding comparable savings could be considered in close consultation with European Commission, IMF and ECB staffs):

- Implement the rule of replacing only 20 percent of retiring employees in the public sector (central government, public companies, local governments, state agencies and other public institutions);
- Reduction in intermediate consumption of the general government by at least EUR 300 million compared to the 2010 level, on top of savings envisaged in the context of reforming public administration and the reorganisation of local government (see next measure);
- Government starts implementing legislation reforming public administration and the reorganisation of local government with the aim of reducing costs by at least EUR 1500 million from 2011 to 2013, of which at least EUR 500 million in 2011.
- Freeze in the indexation of pensions, with aim of saving EUR 100 million;
- Reduction in domestically-financed investments by at least EUR 500 million, by giving priority to investment projects financed by EU structural and cohesion funds;
- Temporary "crisis levies" on highly profitable firms, yielding at least EUR 600 million in additional revenue per year in 2011, 2012 and 2013;
- Incentives to regularize land-use violations, yielding at least EUR 1500 million from 2011 to 2013, of which at least EUR 500 million in 2011;
- Enforce the presumptive taxation of professionals, with a yield of at least EUR 400 million in 2011 and increasing returns in 2012 and 2013;
- Broaden the VAT base by including services that are currently exempted and move a significant proportion (at least 30%) of the goods and services currently subject to the reduced rate to the normal rate, with a yield of at least EUR 1000 million, or a measure of the same yield to be agreed with the EC/IMF/ECB staffs;
- Start phasing in a "green tax" on CO2 emissions, with a yield of at least EUR 300 million in 2011;
- Collect revenue from the licensing of gaming: at least EUR 500 million in sales of licenses and EUR 200 in annual royalties;
- Expand the base of the real estate tax by updating asset values to yield at least EUR 400 million additional revenue;
- Increase taxation of wages in kind, including by taxing car lease payments (at least EUR 150 million);
- Initiate the collection of a special tax on unauthorized establishments (at least EUR 800 million per year);
- Increase taxes on luxury goods by at least EUR 100 million;
- The budget will establish detailed expenditure ceilings for each line-ministry, local governments, and social security funds consistent with the general government deficit target. This also pertains to the medium-term fiscal framework for 2012-2013;

- The budget will contain indicative information on monthly revenue per category, and expenditure per Ministry. Updated figures will be regularly made available online.

Government implements the new organic budget law, and ensures that the draft budget law for 2011 onwards contains detailed information on outturn and plans of the entire general government sector – including local government, social security, hospitals and legal entities. An annex to the budget will present key figures on the financial performance of the largest public enterprises, concomitant budgetary and tax expenditures, and related fiscal risks.

ii. Structural fiscal reforms

Tax administration

Parliament adopts legislation to improve the efficiency of the tax administration and controls, implementing recommendations provided by the European Commission and IMF staffs. In particular, they put in place an effective project management arrangement (including tight oversight by the Ministry of Finance and taskforces) to implement the anti-evasion plan to restore tax discipline through:

- strengthened collection enforcement and recovery of tax arrears (coordinated with the social security funds) of the largest debtors;
- a reorganized large taxpayer unit focused on the compliance of the largest revenue contributors;
- a strong audit program to defeat pervasive evasion by high-wealth individuals and high income self-employed, including prosecution of the worst offenders; and
- a strengthened filing and payment control program.

Accounting and control

Government implements the reform of the general accounting office (GAO), including the following elements:

- Strengthening of the role of the GAO in budget planning and control;
- Provision of the necessary resources in terms of high-level personnel, infrastructure and equipment support, managerial organization and information-sharing systems;
- Provision of safeguards for GAO staff against political interference, and personal accountability in the provision of reliable data;
- Strengthen the institutional mechanisms for providing reliable and plausible official budgetary forecasts that take into account available recent execution developments and trends; to this end, the official macroeconomic forecasts should be reviewed by external experts.

Government takes the following measures to ensure timely provision of reliable fiscal accounts and statistics:

- GAO starts, in June 2010, the publication of timely monthly statistics (on a cash basis) on revenue, expenditure and financing and accounts payable for the

"available general government" and its sub entities (state, social security, hospitals, local governments and legal entities);

- Government adopts a detailed time-bound action plan, agreed with Eurostat, to improve collection and processing of general government data required under the existing EU legal framework, in particular by enhancing the mechanisms that ensure the prompt and correct supply of these data, and ensure personal responsibility in cases of misreporting; and receive appropriate resident technical assistance to ensure rapid progress;
- Government starts to publish timely information on the financial situation in public enterprises (at least the 10 largest loss-making ones) and other public entities not classified in the general government (including detailed income statements, balance sheets and data on employment and the wage bill). To this end, a regular and timely reporting mechanism is introduced.

The Ministry of Finance establishes a comprehensive central registry for public enterprises.

iii. Financial sector regulation and supervision

The Bank of Greece and the Government ensure that the Financial Stability Fund is fully operational.

Government makes available an in-depth study on the strategic options for the banking sector as well as a preliminary due diligence analysis for those financial entities in which the state has a significant stake.

Following up on the result of the July 2010 CEBS stress tests, the bank which did not pass the test implements interim restructuring measures under enhanced supervision by the Bank of Greece. Government provides its full support to this bank and ensures that it complies with the requirement of implementing a restructuring plan under the EU rules for state aid, including compliance with the 1 October 2010 deadline for submission.

The Bank of Greece commits to reduce remuneration of its staff in light of the overall effort of fiscal consolidation.

iv. Structural reforms

To strengthen labour market institutions

Following dialogue with social partners, Government adopts and implements legislation to reform wage bargaining system in the private sector, which should provide for a reduction in pay rates for overtime work and enhanced flexibility in the management of working time. . Government ensures that firm level agreements take precedence over sectoral agreements which in turn take precedence over occupational agreements. Government removes the provision that allows the Ministry of Labour to extend all sectoral agreements to those not represented in negotiations.

Government amends employment protection legislation to extend the probationary period for new jobs to one year, and to facilitate greater use of temporary contracts and part-time work.

Government amends regulation of the arbitration system, (Law 1876/1990), so that each of the parties can resort to arbitration if they disagree with the proposal of the mediator without exceptions on subject or coverage, according to the provisions of Law 3863/2010. It should provide for an arbitration procedure that operates according to transparent objective criteria, and with an independent committee of arbitrators with decision making capacity free from government influence. The objectives of the arbitration should ensure that due attention is paid to cost competitiveness, thereby supporting job creation.

To modernise public administration

Public sector wages and human resource management

Government launches the process, including the principles and timetable, for establishing a simplified remuneration system covering basic wages and allowances. It shall apply to all public sector employees, and be part of an overall reform of Human Resource management. This should lead to a system where remuneration reflects productivity and tasks. As a general principle, it should avoid increases in remuneration for employees as a result of the transition process.

Functional reviews

Government launches independent functional reviews of the public administration at central level and of existing social programmes. It is to be conducted by internationally renowned and external experts. The Terms of Reference for the reviews will be agreed with the European Commission, IMF and ECB staffs. To ensure ownership, participation shall *inter alia* include the office of the Prime Minister, the Ministry of Interior, the Ministry of Finance, the Ministry of Labour and Social Security and the Ministry of Health and Social Solidarity.

The objectives of the review on public administration at central level are:

- To take stock of the use of resources, including human resources, to carry out government functions (e.g., employment, goods and services) in the central government and subordinated public institutions;
- To identify actions to rationalize the organisation of public administration and generate productivity gains, and quantify possible fiscal savings from implementation of these actions. The review shall encompass horizontal issues related to planning, organisation, staffing and control functions (including internal audit), and shall include specific studies for all main ministries and key public bodies.

The objectives of the review on existing social programmes are:

- To assess effectiveness and appropriateness of existing social programmes and make proposals for reform or cancellation of the least effective ones, while quantifying possible fiscal savings from implementation of these actions.

- To assess the options for reform of the overall health care system (both public and private) with the aim of securing more efficient use of public resources and delivery of better quality health care services.

Public procurement

Government agrees an action plan, with a timetable for concrete actions, leading to the creation of a central procurement authority, involving a swift implementation of the electronic platform for public procurement and introducing the use of an e-auctioning system. It should ensure a common approach across government authorities for tendering procedures, *ex ante* and *ex post* controls.

To strengthen competition in open markets

Services Directive

Under the Services Directive, the government finalizes the review (screening) of existing sectoral legislation, and provides a list of restrictions that are being abolished or amended as a result.

The Government also ensures that the electronic point of single contact is operational with a user-friendly internet portal which:

- lists all relevant information for the specific service;
- for each service activity provides an overview of procedures to be complied with, distinguishing between the requirements that apply in establishment cases and for cross-border service provision;
- allows common procedures (including for the most important regulated professions and in the areas of tourism, retail, education and construction) to be completed by electronic means with the necessary forms available on-line and recognising electronic signatures in accordance with Decision 2009/767/EC.

Transport

Government adopts a law on road freight transport that removes restrictions not provided for in Directive 96/26/EC of 29 April 1996 on admission to the occupation of road haulage, including minimum fixed prices.

The government adopts legislation, proposed by the Ministry of Infrastructure, Transport and Networks, establishing the necessary enabling conditions for the development and the implementation of a business plan in the railway sector and submits it to Parliament for voting. The legislation should *inter alia*:

- ensure compliance with all relevant EU legislation on the railway sector to effectively ensure market opening, employment and social policies, as well as competition and state aid policy
- establish an upper limit of EUR 50 million for the annual Public Service Obligation (PSO) contribution from the general government for the period 2011-2013 and establishes the principle that the State provides no additional explicit or implicit support to TRAINOSE;

- provide for any future changes to the level of PSO transfers to the railway operators to be approved only after an independent and transparent assessment by the Hellenic Competition Commission and to be fully in line with all legislation related to budgetary control and execution;
- provide certainty that the managing boards of TRAINOSE and OSE have the legal authority to negotiate new collective agreements covering remuneration and employment conditions and to take staffing decisions that assure a viable business;
- ensure that decisions on the transfer of debt to the State become effective only after the implementation of key actions in the approved business plan;

The government adopts a business plan, proposed by the Ministry of Infrastructure, Transport and Networks, with a detailed timetable for concrete actions, which *inter alia*:

- specifies how operational activities will be made profitable, including covering depreciation costs, as from 2011 including by closing loss-making lines, by increasing tariffs and by reducing wages and staffing;
- provides a detailed sensitivity analysis on the implications for wage costs of various scenarios for the outcome of collective agreement. This provides information on several options concerning staff;
- ensures the effective implementation of EU Directives, including EU Directives 2007/59/EC and 20078/57/EC on the Train Driver Certificate and on the Interoperability of the Rail System, respectively, allowing for competition amongst providers of railway services;
- provides for the restructuring of the holding company, including the sale of land and other assets.

To promote investments and exports

Government takes measures, in line with EU competition rules, to facilitate FDI and investment in innovation in strategic sectors (green industries, ICT, etc...), the adoption of measures to facilitate public private partnerships (PPPs), action to fast-track large FDI projects and measures to strengthen export promotion policy. These actions focus on removing rigidities and administrative constraints and must be fully in line with the fiscal requirements of the Memorandum of Understanding.

2. Actions for the third review (to be completed by end Q4-2010)

i. Fiscal consolidation

Government achieves the programme target for the 2010 general government deficit.

Parliament adopts the budget for 2011 targeting a further reduction in the general government deficit and including the required consolidation measures including those specified in this Memorandum.

The Ministry of Finance ensures tight supervision of expenditure commitments by the several government departments, and effective tax collection, to make certain that general government deficit target in cash and ESA95 bases (see respectively Table 2 of MEFP and Article 1 of Council Decision 2010/320/EU) are achieved.

Government prepares a privatization plan for the divestment of state assets and enterprises with the aim to raise at least EUR 1 billion a year during the period 2011-2013. The restructuring and privatization programme will span the state's holdings in rail, road transport, airports, ports, utilities, the gaming industry and public real estate; leverage private investment so as to restructure the economy, foster economic growth and contribute to fiscal consolidation; use the know-how of the private sector through outright sales of government holdings, concession agreements, initial public offerings, strategic public-private partnerships and the establishment of new holding companies.

Accounting and control

Government ensures that the central registry for public enterprises is operational.

ii. Structural fiscal reforms

The fiscal framework

Government implements legislation to strengthen the fiscal framework. The following elements should be part of the reform:

- Introduce a medium-term fiscal framework covering the general government based on rolling three-year expenditure ceilings for the State, social security entities and local governments;
- Strengthen the position of the Finance Minister vis-à-vis line ministries in both budget preparation and execution phases (giving him/her veto power on spending decisions and execution);
- Introduce a compulsory contingency reserve in the budget, corresponding to 10 percent of total appropriations of government departments other than wages, pensions and interest; the use of the contingency reserve will be decided by the Finance Minister;
- Ensure that Parliament does not modify the overall size of the budget at the approval stage, and focus on the composition of public expenditure and revenue, and reliability of projections for expenditure and revenue;
- Introduce stronger expenditure monitoring mechanisms, particularly by implementing an appropriate control of spending commitments, through which spending entities (line ministries, local authorities, social security funds, hospitals and legal entities) will report on a regular basis to the Treasury on their outstanding expenditure commitments against their authorised appropriations in the budget law;
- Introduce a revenue rule for the general government, according to which the allocation of higher-than-expected revenues should be specified *ex-ante* in the budget law;

- Creation of a fiscal agency attached to Parliament providing independent advice and expert scrutiny on fiscal issues, and reporting publicly on the budgetary plans and execution of the spending entities of the general government, and on macroeconomic assumptions used in the budget law.

Parliament adopts the reform of the public wage legislation consistent with this Memorandum.

To complete the pension reform

The National Actuarial Authority provides by 1 December 2010 interim long-term projections of pension expenditure up to 2060 under the July 2010 legislation covering the main pension schemes (IKA, OGA, OAE, public sector scheme).

iii. Financial sector regulation and supervision

Taking into account the outcome of the strategic study and the due diligences of banks, the Government formulates a programme to preserve financial stability and enhance efficiency in the banking system.

iv. Structural reforms

To reform and modernise public administration

Local administration

Government adopts all necessary legislation and decrees for the full entry into force of the local administration reform (*Kallikrates*) and ensures that it achieves savings of EUR 500 million in 2011 and additional EUR 500 million per year in 2012 and 2013 for the general government as a whole. Government shall adopt a decree disallowing local governments to run deficits at least until 2014.

Public sector wages and human resource management

The Ministry of Finance together with the Ministry of Interior completes the establishment of a Single Payment Authority for the payment of wages in the public sector. The Ministry of Finance publishes a detailed report, in collaboration with the Single Payment Authority, on the structure and levels of compensation and the volume and dynamics of employment in the general government. The report should present plans for the allocation of human resources in the public sector for the period up to 2013 that *inter alia* specifies plans to reallocate qualified staff to areas necessary to implement the Memorandum of Understanding, including the tax administration, GAO, the labour inspectorate, regulators and Hellenic Competition Commission.

Government presents a detailed action plan with timeline to complete and implement a simplified remuneration system.

Better Regulation

Government adopts legislation and measures needed to implement the Better Regulation agenda.

To modernise the health care systems

Government adopts legislation on the institutional framework for health supplies (Law 3580/2007, as revised in May 2010 by Law 3846/2010), establishes new systems for the management of drugs that favour more use of generic medicines, including a new system for the electronic monitoring of doctors' prescriptions. The aim is to move to the average EU generic drug penetration rate, including by procurement of pharmaceutical products by hospitals and doctors' prescriptions on the basis of drastic substances.

Government enforces the payment of EUR 3 for regular outpatient services in public hospitals and extends the 'all day' functioning of hospitals (afternoon shift) in order to develop and improve healthcare services and increase revenue, including by increasing co-payment of outpatients and diagnostic services.

Government completes the programme of hospital computerisation, upgrading hospital budgeting systems, and the reform of management, the accounting (including double-entry accrual accounting) and financing systems.

Government ensures greater budgetary and operational oversight of health care spending by the Finance Minister, the publication of audited accounts and improvement in pricing and costing mechanisms.

Government seeks technical assistance from independent international experts on all aspects of the efficiency and effectiveness of the health procurement system and management of hospitals, aiming at enhancing efficiency and reducing waste.

To enhance competition in open markets

Government makes the General Commercial Registry (GEMI) fully operational.

Services directive

Government adopts changes to existing (sectoral) legislation in key services sectors such as tourism, retail and education services. New legislation should:

- facilitate establishment, in particular, by
 - abolishing or amending requirements which are prohibited by the Services Directive; and
 - significantly reducing requirements, including those relating to quantitative and territorial restrictions, legal form requirements, shareholding requirements, fixed minimum and/or maximum tariffs and restrictions to multidisciplinary activities.

- facilitate the provision of cross-border services so that service providers providing cross-border services only have to comply with specific requirements laid down in Greek legislation in exceptional cases (when admitted by Articles 16 or 17 of the Services Directive).
- provide legal certainty for service providers providing cross-border services by clearly setting out in the respective (sectoral) legislation which requirements can and which requirements cannot be applied to cross-border services.

Government specifies, a limited number of priority service sectors, which are key for growth, a timetable for adopting sectoral legislation by end Q2 2011 that ensure full compliance with the requirements of the Services Directive.

Restricted professions

Government proposes legislation to remove restrictions to competition, business and trade in restricted professions including:

- the legal profession, to remove unnecessary restrictions on fixed minimum tariffs, the effective ban on advertising, territorial restrictions on where lawyers can practice in Greece;
- the pharmacy profession, covering limits on the number of pharmacies and minimum profit margins;
- the notary profession, covering fixed tariffs, limits on the number of notaries, territorial restrictions on where notaries can practice and the effective ban on advertising;
- architects, covering fixed minimum tariffs;
- engineers, covering fixed minimum tariffs;
- auditing services, covering fixed tariffs.

Government adopts legislation and takes all necessary measures to complete the effective transposition of EU rules on recognition of professional qualifications, including compliance with all ECJ rulings (*inter alia*, related to franchised diplomas), the setting up of the administrative structures responsible for the application of the rules of recognition of professional qualifications as well as timely information of citizens about their pending requests for recognition.

Sectoral growth drivers

Government presents a report analysing the potential contribution of the tourism sector to growth and jobs in the Greek economy. It should identify all legislative, administrative and other obstacles hindering competition and market entry to the realisation of the potential.

Government presents a report analysing the potential contribution of the retail sector to price flexibility, growth and jobs in the Greek economy. It should identify all legislative, administrative and other obstacles hindering competition and market entry to the realisation of the potential.

Business environment

Government adopts legislation to simplify and accelerate the process of licensing enterprises, industrial activities and professions, which *inter alia* revises Law 3325/05, makes the spatial plan and Law 3333/05 for business areas operational.

Government adopts an 'action plan for a business friendly Greece' that presents a timetable for the removal of 30 of the most important remaining restrictions to business activity, investment and innovation.

Government accelerates the completion of the land registry and prepares a progress report, including an action plan.

Government adopts a law modifying the existing institutional framework of the Hellenic Competition Commission (HCC) with the aim of abolishing the notification system for all agreements falling within the scope of Article 1 of Law 703/1977/, to give the HCC the power to reject complaints, to increase the independence of HCC members, and to establish reasonable deadlines for the investigation and issuance of decisions.

Energy

Government presents its detailed plans for the liberalisation of the energy market, including opening up lignite-fired electricity generation to third parties in line with EU requirements.

Government adopts plan for phased transitory cost-based access to lignite-fired generation, taking into account the decommissioning of the power plants scheduled under the Government's Energy Plan to meet the 20-20-20 target. This access will remain in place until effective implementation of the liberalisation has taken place.

Government adopts a plan to either award the hydro reserves management to an independent body or to assign this role to the independent system operator.

Government adopts a mechanism to ensure that the energy component of regulated tariffs reflects, gradually and at the latest by June 2013, wholesale market prices, except for vulnerable consumers. Government adopts a revised definition of vulnerable consumers and a tariff for this category of consumers.

In order to ensure that network activities are unbundled from supply activities as foreseen in the second and third energy liberalisation packages, Government identifies the assets and personnel associated with the electricity transmission system and the electricity distribution system.

To promote investments and exports

Government carries out in depth evaluation of all R&D and innovation actions, including in various Operational Programmes, in order to adjust the national strategy and limit the use of government subsidies and guarantees.

Government creates an external advisory council financed through the 7th R&D programme, to consider how to foster innovation, how to strengthen links between public research and Greek industries and the development of regional industrial clusters.

To raise the absorption rates of Structural and Cohesion Funds

Government meets targets for payment claims in the absorption of Structural and Cohesion Funds set down in the table below. Compliance with the targets shall be measured by certified data. In addition, Government achieves an annual target of submitting 10 major projects applications to the Commission services. In meeting absorption rate targets, recourse to non-targeted *de minimis* state aid measures should be gradually reduced.

Government presents a report on the activities of the task force assessing progress in ensuring the rapid implementation and absorption of structural funds, and proposing improvements when necessary.

Programming period 2007-2013 <i>(in EUR million)</i>	Payment claims to be submitted between 2010 and 2013			
	2010	2011	2012	2013
<i>European Regional Fund and Cohesion Fund</i>	2330	2600	2850	3000
<i>European Social Fund</i>	420	750	880	890
<i>Target of first half of the year</i>		1105	1231	1284
<i>Target of second half of the year</i>		2245	2499	2606
<i>Total annual target</i>	2750	3350	3730	3890

Without prejudice to the Greek Constitution, Government adopts legislation to tackle delays in the implementation of public works and investment projects in general. Legislation should *inter alia*:

- shorten and simplify judicial procedures challenging contract awards or land expropriation decisions;
- shorten deadlines to get permits by the Central Archaeological Council in Athens;
- simplify and shorten procedures to complete studies on environmental impact and to get the approval of environmental terms for infrastructure projects.

3. Actions for the fourth review (to be completed by end Q1-2011)

i. Fiscal consolidation

Government rigorously implements the budget for 2011 in line with this Memorandum. Progress is assessed against the (cumulative) quarterly deficit ceilings in the MEFP (including the TMU).

ii. Structural fiscal reforms

Parliament adopts legislation to strengthen the fiscal framework, consistent with this memorandum.

To complete the pension reform

The National Actuarial Authority submits comprehensive long-term projections of pension expenditure up to 2060 under the adopted reform; the projection will be peer-reviewed and validated by the EU Economic Policy Committee and the European Commission, IMF and ECB. The projections shall encompass the supplementary (auxiliary) schemes, based on comprehensive set of data collected and elaborated by the National Actuarial Authority.

iii. Structural reforms***To reform and modernise public administration****Public procurement*

Government completes effective transposition of Directive 2007/66/EC on public procurement regarding remedies, and at the same time ensures that responsibility for the review of award procedures be vested with the administrative courts. Government completes the transposition of Directives 2009/81 on defence and security expenditure.

Reforms to improve the business environment:*Restricted professions*

Government adopts specific legislation on restricted professions including for the legal profession, the pharmacy profession, the notary profession, architects, engineers and auditing services.

Sectoral growth drivers

Government adopts legislation and takes other structural actions to implement the findings of the report analysing the potential contribution of the tourism sector to growth and jobs in the Greek economy.

Government adopts legislation and takes other structural actions to implement the findings of the report analysing the potential contribution of the retail sector to price flexibility, growth and jobs in the Greek economy.

To enhance competition in open markets*Energy*

Government commences implementation of plan for opening up lignite-fired electricity generation to third parties.

Government implements its decision to either award the hydro reserves management to an independent body or to assign this role to the independent system operator.

Government starts to implement the mechanism to ensure that the energy component of regulated tariffs reflects, gradually and at the latest by June 2013, wholesale market prices, except for vulnerable consumers.

In order to ensure that network activities are unbundled from supply activities as foreseen in the second and third energy liberalisation packages, the following measures are implemented:

- Government adopts decision on the modalities of unbundling of the transmission system operator in line with the third energy liberalization package and adopts necessary legislation to ensure the creation of fully unbundled electricity and gas transmission system operators by March 2012.
- Government ensures the creation of an independent Distribution System Operator, in line with the third energy liberalisation package.

Government transfers to RAE (Regulatory Authority for Energy) all regulatory powers assigned to EU energy regulators in the third energy liberalisation package (licensing, network access, network charges, market monitoring, etc).

Government adopts measures to ensure the independence of RAE (impartial and transparent nomination of board, management authority with regard to budget and personnel, etc. in line with the third energy liberalisation package).

4. Actions for the fifth review (to be completed by end Q2-2011)

i. Fiscal consolidation

Government rigorously implements the budget for 2011 in line with this Memorandum, and the fiscal consolidation measures in the budget. Progress is assessed against the quarterly deficit ceilings in the MEFP (including the TMU).

ii. Structural fiscal reforms

To complete the pension reform

Government revises the main parameters of the pension system provided by Law 3863/2010, if the projections by the National Actuarial Authority show that the projected increase in public pension expenditure would exceed the limit of 2.5 percentage points of GDP over 2009-60. The revision should be designed in close consultation with the European Commission, the IMF and the ECB staffs.

Government implements an in-depth revision of the functioning of supplementary/auxiliary public pension funds. The aim of the revision shall be to stabilise pension expenditure and guarantee the budgetary neutrality of supplementary/auxiliary schemes.

Government substantially revises the list of heavy and arduous professions, and reduces its coverage to no more than 10% of the labour force. The new list of Difficult and Hazardous Occupations shall apply with effect from 1 July 2011 to all current and future workers.

The Bank of Greece commits not to grant pension privileges to its staff and to revise the main parameters of its pension scheme to align them with those of IKA.

iii. Structural reforms

To modernise public administration

Public sector wages and human resource management

Government adopts legislation establishing a simplified remuneration system covering basic wages and allowances that applies to all public sector employees ensuring that remuneration reflects productivity and tasks: this reform should be part of an overall reform of Human Resource management in the public sector.

Functional reviews

Government assesses the results, including operational policy recommendations, of a first phase of the independent functional review of public administration at central level are presented by the external experts. This should include the results of studies applied to a number of core ministries. The functional review of existing social programmes is finalised.

Public procurement

Government implements the reform of the public procurement system, as defined in the action plan.

To strengthen labour market institutions

Government completes the reform to strengthen the Labour Inspectorate, which should be fully resourced with qualified staff and has quantitative targets on the number of controls to be executed.

Government adapts the legislation on tackling undeclared work to require the registration of new employees before they start working.

Review the scope for improvements in the targeting of social expenditures to enhance the social safety net for the most vulnerable.

To strengthen competition in open markets:

Services Directive

Government adopts legislation on a limited number of priority service sectors identified in Q4 2010. Government specifies, for a limited number of priority service sectors, a timetable for adopting sectoral legislation by end Q4 2011 that ensure full compliance with the requirements of the Services Directive.

Business environment

Government presents an impact assessment evaluating Law 3853/2010 on simplification of procedures for the establishment of personal and capital companies in terms of the savings achieved in time and cost to set up a business.

Government ensures that the point of single contact is fully operational and completion of procedures by electronic means possible in all sectors covered by the Services Directive.

Energy

Government removes regulated tariffs for customers except households and small enterprises (as defined in the second and third energy liberalisation packages).

To raise the absorption rates of Structural and Cohesion Funds

Government meets targets for payment claims to be measured against certified data.

Government presents a report on the activities of the task force assessing progress in ensuring the rapid implementation absorption of structural funds, and proposing improvements when necessary.

5. Actions for the sixth review (to be completed by end Q3-2011)

i. Fiscal consolidation

Government rigorously implement the budget for 2011 in line with this Memorandum. Progress is assessed against the quarterly deficit ceilings in the MEFP (including the TMU).

Government adopts the draft budget for 2012 aiming at a further reduction of the general government deficit in line with the programme and including the detailed presentation of consolidation measures amounting to at least 2.2% of GDP, including the following measures (in exceptional circumstances, measures yielding comparable savings could be considered in close consultation with European Commission, IMF and ECB staffs):

- Reduce public employment on top of the rule of 1 recruitment for each 5 retirements in the public sector; the reduction in public employment on top of the 5-to-1 rule should allow savings of at least EUR 600 million;
- Establish excises for non alcoholic beverages, for a total amount of at least EUR 300 million;
- Continue the expansion of the base of the real estate tax by updating asset values to yield at least EUR 200 million additional revenue;
- Continue the reorganisation of local government, to generate at least EUR 500 million in savings;
- Nominal freeze in pensions;¹¹
- Continue to increase the effectiveness of the presumptive taxation of professionals, with the aim of collecting at least additional EUR 100 million;
- Reduction of transfers to public enterprises by at least EUR 800 billion following their restructuring;

¹¹ Adjustments may be needed in case of negative inflation.

- Make unemployment benefits means-tested (aiming at savings of EUR 500 million);
- Collect further revenue from the licensing of gaming: at least EUR 225 million in sales of licences and EUR 400 in annual royalties;
- Further broadening of VAT base with the aim of collecting at least additional EUR 300 million.

ii. Structural reforms

To modernise public administration

Government ensures full operation of the Better Regulation Agenda to reduce administrative burden by 20% compared with 2008 level, and sends report to the European Commission.

To improve the business environment

Government changes legislation to mitigate tax obstacles to mergers and acquisitions such as the non-transfer of accumulated losses, together with the company and the complex computation of "excessive benefit" (Law 3522/2006, Article 11) in the transfer of private limited companies.

Government takes decisions to simplify the process to clear customs for exports and imports and give larger companies or industrial areas the possibility to be certified to clear cargo for the customs themselves; Government abolishes the requirement of registration with the exporter's registry of the chamber of commerce for obtaining a certificate of origin.

6. Actions for the seventh review (to be completed by end Q4-2011)

i. Fiscal consolidation

Government achieves the programme targets for the 2011 general government deficit.

Parliament adopts the budget for 2012 a further reduction of the general government deficit and including consolidation measures amounting to at least 2.2% of GDP, in line with Memorandum.

ii. Structural reforms

To modernise public administration

Functional reviews

Government assesses the results of a second phase of the independent functional review of public administration at central level are presented by the external experts. The government adopts legislation and measures to implement the first set of operational recommendations of

the functional review of public administration at central level and the review of existing social programmes.

To strengthen competition in open markets

Energy

Government removes regulated tariffs for customers except households and small enterprises (as defined in the second and third energy liberalisation packages).

To raise the absorption rates of Structural and Cohesion Funds

Government meets targets for payment claims (to be measured against certified data).

Government introduces web-based open-access monitoring tool of procedures for approval of project proposals and for implementation of public projects.

Government ensures that the managerial capacity of all Managing Authorities and Intermediate Bodies of operational programmes under the framework of the National Strategy Reference Framework 2007-2013 has been certified by the International Organization for Standardization according to the standard ISO 9001:2008 (Quality Management).

Government presents a report on the activities of the task force assessing progress in ensuring the rapid implementation absorption of structural funds, and proposing improvements when necessary.

Annex 1. Provision of data

During the programme, the following indicators and reports shall be made available to the European Commission, the ECB and the IMF staffs by the authorities on a regular basis.

To be provided by the Ministry of Finance

Preliminary monthly data on the state budget execution (including functional breakdown by main categories of revenue and expenditure and by line ministry)	Monthly, 15 days after the end of each month; these data should also be included in subsequent transmissions in case of revision
Updated monthly plans for the state budget execution for the remainder of the year, including functional breakdown by main categories of revenue and expenditure and by line ministry	Monthly, 30 days after the end of each month
Preliminary monthly cash data on general government entities other than the State	Monthly, 30 days after the end of each month, these data should also be included in subsequent transmissions in case of revision
Monthly data on the public wage bill (of general government, including a functional breakdown in nominal wage and allowances paid to government employees per line ministry and public entity), number of employees (including a functional breakdown per ministry and public entities outside the central government) and average wage (including the relative shares of the base wage, allowances and bonuses).	Monthly, 30 days after the end of each month (starting in June 2010)
Quarterly data on general government accounts, and debt as per the relevant EU regulations on statistics	Quarterly accrual data, 90 days after the end of each quarter
Weekly information on the Government's cash position with indication of sources and uses as well of number of days covered	Weekly on Friday, reporting on the previous Thursday
Data on below-the-line financing for the general government	Monthly, no later than 15 days after the end of each month; these data should also be included in subsequent transmissions in case of revision
Data on expenditure pending payment (including arrears) of the general government, including the State, local government, social security, hospitals and legal entities	Quarterly, within 55 days after the end of each quarter
Data on expenditure pending payment (arrears) of the State and hospitals	Monthly, 30 days after the end of each month
Public debt, and new guarantees issued by the general government to public enterprises and the private sector	Monthly, within one month
Income and expenditure statement and balance sheets of 30 largest public enterprises by total expenditures	Quarterly, three months after the end of the quarter

Data on EU project grants (reimbursements and advances), capital expenditures and subsidies covered by EU advances or eligible for EU reimbursement on EU supported projects specifically agreed with the EU	Monthly, within three weeks of the end of each month
Monthly statement of the transactions through off-budget accounts	Monthly, at the end of each month
Monthly statements of the operations on the special account	Monthly, at the end of each month
Report on progress with fulfillment of policy conditionality	Monthly, at the end of each month

To be provided by the Bank of Greece

Assets and liabilities of the Bank of Greece	Weekly, next working day
Assets and liabilities of the Greek banking system - aggregate monetary balance sheet of credit institutions	Monthly, 30 days after the end of each month
Evolution of the external funding provided by Greek banks to their subsidiaries abroad ¹²	Monthly, 15 days after the end of each month
External funding flows for the banking, corporate and government sector, including also expected developments in the 12 months ahead	Monthly, 30 days after the end of each month
Report on banking sector liquidity situation	Weekly, next working day
Report on the evolution of financial stability indicators	Quarterly, 15 days after the end of each quarter depending on data availability
Report on results from the regular quarterly solvency stress tests	Quarterly, 15 days after the end of each quarter depending on data availability
Detailed report on the balance sheet of the Financial Stability Fund with indication and explanation of changes in the accounts	Weekly, next working day

¹² All forms of debt instruments and capital, as well as net deposits provided to subsidiaries abroad.

Annex 2. Financial Stability Fund

General

- The purpose of the Financial Stability Fund (the ‘Fund’) is to maintain the stability of the Greek banking system by providing equity capital in case of a significant decline of capital buffers.
- The Fund will not provide liquidity support, which will be provided under existing arrangements.
- The equity will be provided in the form of preference shares to credit institutions authorised to operate in Greece by license from the Bank of Greece. The preference shares will be convertible into ordinary shares at a later stage under certain conditions to be further specified in the legislation establishing the Fund.
- Participation in the Fund will be mandatory, based on a trigger linked to the minimum required level of capital adequacy requirements, as established for specific credit institutions by the Bank of Greece, in its capacity as the competent supervisory authority, if no private solution has been found.
- If banks are then not able to expeditiously raise additional capital on their own and repay the Fund, a restructuring process will take place under the lead of the Fund, in line with EU competition and state aid requirements
- The Fund will be established by specific Greek legislation.
- An initial lifespan of seven years will be set for the Fund. After the end of the lifespan of the Fund, the ownership of the Fund rests with the Greek state to the extent of its shareholding in the Fund

Legal status

- The Fund will be established as a private law legal entity in order to enhance its flexibility and efficiency (e.g., to facilitate the recruitment and remuneration of appropriately qualified staff).
- The legal structure of the Fund should allow for private participation.

Funding

- The FSF will be fully funded by the government out of the resources available under the EU-IMF program for this purpose in the amount of EUR 10 billion. This implies that the risk of losses arising out of the Fund’s operations would lie exclusively with the Greek Government, as the primary shareholder in the Fund. The purchase of preference shares by the Fund shall be made in cash.

Organizational issues

- The Fund will be managed by a Governing Council composed of (1) a Chairperson, a Chief Executive and three directors appointed by the Governor of the Bank of Greece and (2) two ex officio directors who represent the Minister of Finance and the Governor of the Bank of Greece. The European Commission and the ECB will each nominate an

observer who would have a right to participate, without voting, in meetings of the Governing Council (without prejudice, in the case of the Commission observer, to the application by the Commission of state aid and competition rules).

- The Chairperson, Chief Executive and the non-ex officio directors will be required by law to be persons of recognised standing in banking or financial matters in Greece, the EU or internationally.
- Each of the Chairperson and the non-ex officio directors will be appointed to a five year term of office, renewable for a further two years, and may only be compulsorily removed from office by an appropriate Greek court on application of either the Governor of the Bank of Greece or the Governing Council of the Fund where (1) no longer capable of fulfilling the conditions required for the performance of the duties of office or (2) guilty of serious misconduct.
- No member of the Governing Council may be represented on the board of directors of any credit institution.
- The legislation establishing the Fund will provide that, when exercising the powers and carrying out the tasks and duties conferred upon them under the legislation, neither the Governor of the Bank of Greece nor the members of the Governing Council of the Fund shall seek or take instructions from the Greek Government or any other State entity, institution, body or undertaking.
- The Governing Council will present a semi-annual report to the Greek Parliament, the European Commission, the ECB and the IMF.
- The operating expenses will be covered by the Fund.

Powers of the Fund

- In order to fulfill its purposes the Fund will enjoy certain powers over credit institutions receiving capital from the Fund, to be exercised following consultation of the BoG. These powers will be without prejudice to the supervisory powers of the Bank of Greece, and will include, without limitation, the power:
 - o to require the BoG to provide the Fund with all information on financial institutions necessary for it to fulfill its tasks;
 - o to appoint a member of the Board of Directors of a credit institution;
 - o to require a credit institution to present a restructuring plan;
 - o to veto key decisions of a credit institution (e.g., business strategy, dividend distributions, salary caps, liquidity and asset-liability management, etc.);
 - o to call a general shareholders' meeting for a credit institution in accordance with Greek company law;
 - o to require conversion of preference shares into ordinary shares insofar as a credit institution fails to meet (1) the minimum required level of capital adequacy requirements established for credit institutions generally under applicable regulatory requirements or (2) certain financial conditions to be established in the restructuring plan for the credit institution; the legislation establishing the Fund will further specify an objective procedure to be followed in establishing a market-based conversion price, taking account of the impact of the Fund's intervention, the rights of shareholders under Greek law and EU state aid requirements; and

- to conduct diagnostic studies and special audits with the help of outside consultants to assess the solvency of a credit institution where the Fund considers this necessary.
- Each of the Bank of Greece, in its capacity as the competent authority for the supervision of credit institutions, and the Fund will be authorised to exchange confidential information with one another to the fullest extent permitted by EU law.

Conditions applicable to capital increases

- The conditions applicable to any capital increases should be aligned with the Commission Decision of 19.11.2008 (N 560/2008 support measures for the credit institutions in Greece). The granting of equity capital is made subject to the following conditions in particular.
- The credit institutions will be expected to pay a market-oriented, non-cumulative remuneration unless an analysis of the restructuring plan warrants an alternative approach. A market-oriented, non-cumulative remuneration can either be 10% as stipulated in the above decision or depending on the risk profile of the credit institution and the quality of the capital, between 7% and 9.3%, whereas core tier 1 capital for fundamentally sound credit institutions should normally be remunerated at not less than 9%.
- The credit institutions will not pay dividends or coupon on hybrid capital, unless they are legally obliged to do so, which is typically the case when a credit institution is profit making (the credit institution should however not be allowed to use reserves to book a profit).
- Preference shares shall be repurchased by the credit institution for an amount that is equivalent to the amount originally invested in the credit institution. After five years the shares shall be repurchased or be remunerated at penal rates. If they cannot be repurchased because the capital adequacy requirements are not fulfilled, the preference shares shall be converted into ordinary shares.

Approval of restructuring plan by European Commission

- Any restructuring plan needs to be in accordance with State aid rules and approved by decision of the European Commission ensuring that the credit institutions will restore viability at the end of the restructuring period, burden sharing of shareholders is achieved and distortion of competition is limited.

INTERNATIONAL MONETARY FUND

GREECE

**Staff Report for the First Review Under the Stand-By Arrangement
Supplementary Information**

Prepared by the European Department
(In Consultation with Other Departments)

Approved by Poul M. Thomsen and Martin Mühleisen

September 8, 2010

73. **An update has occurred since the Staff Report was issued.** This reflects new and more detailed reporting requirements for financial institutions in euro area countries introduced by ECB Regulation No 25/2009. As a result, the authorities have improved their information on deposit and loan data for local governments and the social security funds. Specifically, the update shows higher net financial assets of local governments and the social security sector, which impacts the calculation of the performance criterion on the modified general government primary cash balance (MGGPCB).

74. **This update implies stronger overperformance than reported in the staff report.** Taking into account the new data, the primary balance (MGGPCB) has been revised from € -4.3 billion to € -3.9 billion, therefore resulting in a wider margin than shown in the staff report (Tables 1 and 2).

75. **The new reporting templates remain in effect from now on.** Changes in the templates are infrequent, with intervals of five years being the recent experience as determined by the ECB. Staff will continue to monitor program performance with data provided under the new templates.

Table 1. Greece: Quantitative Performance Criteria 1/
(Billions of Euros)

	Jan-Jun 2010		Jan-Sep 2010	Jan-Dec 2010
	EBS/10/157	Update		
1 Floor on primary balance				
Target	-5.0	-5.0	-4.0	-5.7
Actual	-4.3	-3.9		
Margin (+)	0.7	1.1		
2 Ceiling on state budget primary spending				
Target	34.0	34.0	50.0	67.0
Actual	28.4	28.4		
Margin (+)	5.6	5.6		
3 Ceiling on new domestic arrears 2/				
Target	0.0	0.0	0.0	0.0
Actual	1.0	1.0		
Margin (+)	-1.0	-1.0		
4 Ceiling on the stock of debt				
Target	342.0	342.0	342.0	342.0
Actual	316.7	316.7		
Margin (+)	25.3	25.3		
5 Ceiling on new guarantees				
Target	2.0	2.0	2.0	2.0
Actual	0.3	0.3		
Margin (+)	1.7	1.7		
6 Ceiling on new external arrears				
Target	0.0	0.0	0.0	0.0
Actual	0.0	0.0		
Margin (+)	0.0	0.0		

Sources: LOI and MEFP; National authorities; and IMF staff calculations.

1/ As defined in the TMU.

2/ Indicative target.

Table 2. Greece: Modified General Government Cash Balance for Program Monitoring (in billion of Euro, cumulative) 1/

	2009 Actual	Program					
		Jun-10		Sep-10		Dec-10	
		Progr.	Actual	Progr.	Proj.	Progr.	Proj.
I. State budget							
Revenues 2/	50.5	25.1	24.2	41.2	38.7	58.4	56.8
Net income Ordinary Budget (A+B-C)	48.5	24.1	23.8	39.1	38.2	55.1	53.8
A. Recurrent/ordinary revenue	52.3	25.8	25.1	41.6	40.6	58.6	57.4
1. Direct taxes	21.4	9.0	8.9	15.3	15.0	21.7	21.4
Income taxes	16.6	6.3	6.0	11.5	10.8	16.6	15.6
PIT	10.9	4.5	4.3	7.7	7.5	10.9	10.7
CIT	3.4	1.0	1.1	2.2	2.0	3.5	3.0
Other	2.3	0.8	0.6	1.5	1.3	2.2	1.9
Property taxes	0.5	0.3	0.1	0.7	0.4	1.0	0.8
Tax arrears collection	2.4	1.3	1.2	1.7	1.6	2.2	2.2
Other direct taxes	1.9	1.2	1.6	1.6	2.2	2.0	2.8
2. Indirect taxes	28.3	15.6	14.8	24.4	23.4	34.1	32.9
Transaction taxes	17.9	9.4	8.9	14.9	14.3	20.2	19.5
VAT	16.6	8.7	8.4	13.6	13.4	18.5	18.4
other	1.3	0.8	0.5	1.3	0.9	1.7	1.2
Consumption taxes	9.6	5.8	5.5	8.8	8.5	12.9	12.5
Tax arrears collections	0.4	0.2	0.2	0.3	0.3	0.5	0.4
Other indirect taxes	0.4	0.2	0.2	0.3	0.3	0.4	0.4
3. Transfers EU	0.3	0.1	0.1	0.2	0.1	0.4	0.4
4. Nontax revenue	2.3	1.1	1.4	1.7	2.0	2.4	2.7
B. One-off revenue	1.1	0.7	0.9	1.0	1.2	1.4	1.5
C. Tax Refunds (-)	5.0	2.4	2.3	3.5	3.6	4.9	5.1
Public investment budget	2.0	0.9	0.4	2.1	0.5	3.3	3.0
A. EU flows	1.9	0.8	0.3	2.0	0.4	3.1	2.9
B. Own revenues	0.2	0.1	0.1	0.1	0.1	0.1	0.1
Total expenditure 2/ 3/	83.6	39.8	34.1	60.5	56.4	79.8	76.4
Total ordinary spending	70.3	34.2	30.2	51.6	49.6	67.9	66.1
Total ordinary primary spending	58.0	26.8	24.5	40.0	37.7	54.9	52.7
A. Remuneration and pensions	25.2	10.8	11.3	16.5	16.9	22.5	22.9
B. Insurance and Healthcare	17.6	8.7	7.4	12.8	11.5	18.1	17.0
C. Operating and other expenditure and returned resources	14.5	7.0	5.4	10.2	8.7	13.6	12.2
D. Payments in exchange of claims of insurance fund 4/	0.8	0.4	0.4	0.5	0.5	0.7	0.6
Interest expenditure	12.3	7.4	5.7	11.7	11.9	13.0	13.4
Transfers to hospitals for the settlement of past debt 5/	1.5	0.0	0.0	0.0	0.2	0.0	0.2
Investment spending	9.6	4.2	3.7	6.8	5.6	9.2	8.2
Spending on military procurement	2.2	1.4	0.2	2.0	1.0	2.7	1.8
State Budget primary spending 2/ 3/ (variable monitored for PC)	71.3	32.4	28.4	48.8	44.3	66.8	62.7
Balance state budget 2/ 3/	-33.1	-14.7	-9.9	-19.3	-17.7	-21.4	-19.6
II. Balance local governments 2/ 6/	0.0	0.9	0.3	1.0	0.2	0.1	0.0
III. Balance social security funds 2/ 6/	1.9	1.9	0.0	3.1	1.6	2.6	2.3
IV. Modified general government cash balance	-31.2	-12.0	-9.6	-15.2	-15.9	-18.7	-17.2
of which: Modified general government primary cash balance (variable monitored for PC)	-18.9	-4.6	-3.9	-3.5	-3.8	-5.7	-3.6
V. Adjustments 7/	-1.1	...	...	...	...	0.1	...
VI. General government balance (ESA 95)	-32.3	...	...	...	...	-18.6	...
Memorandum items							
Floor on the modified general government primary cash balance 8/	...	-5.0	-3.9	-4.0	...	-5.7	...
Ceiling on state budget primary spending 8/	...	34	28	50	...	67	...

Source: Greek Ministry of Finance and Fund staff projections.

1/ This is an update of table 10 in the Staff Report.

2/ Including measures taken in the context of the 2010 program.

3/ Including spending on military procurement.

4/ For the personnel of the Public Power Company.

5/ Such transfers are excluded from spending for measurement of the PCs.

6/ Change in net financial assets. Excludes valuation changes.

7/ National accounts adjustments and capital transfers to other bodies of general government using bonds.

8/ End-June and end-September targets include a margin to account for deviations from historical seasonality.



Press Release No. 10/335
FOR IMMEDIATE RELEASE
September 10, 2010

International Monetary Fund
Washington, D.C. 20431 USA

IMF Completes First Review Under Stand-By Arrangement with Greece and Approves €2.57 Billion Disbursement

The Executive Board of the International Monetary Fund (IMF) today completed the first review of Greece's performance under an economic program supported by a 3-year, SDR 26.4 billion (about €30 billion) Stand-By Arrangement (SBA). The completion of the review enables the immediate disbursement of an amount equivalent to SDR 2.16 billion (about €2.57 billion), bringing total disbursements under the SBA to SDR 6.97 billion (about €8.28 billion).

The SBA, which was approved on May 9, 2010 (see [Press Release No. 10/187](#)), is part of a cooperative package of financing with Euro area member states amounting to €110 billion over three years. It entails exceptional access to IMF resources, amounting to more than 3,200 percent of Greece's quota, and was approved under the Fund's fast-track Emergency Financing Mechanism procedures.

Following the Executive Board's discussion, Mr. Murilo Portugal, Deputy Managing Director and Acting Chair said:

“The Greek authorities have made a strong start with their economic program, and their determined implementation has started to deliver results. All quantitative performance criteria for end-June were met, and major structural reforms are ahead of schedule. It is essential to continue implementing the program rigorously, supported by the large-scale financial support of the international community, while securing public consensus for reforms.

“The fiscal strategy is on track. Continued tight expenditure control and monitoring will be key, in particular at sub-national levels. The authorities are determined to strengthen tax administration and reduce tax evasion to secure revenues and promote fairness in adjustment.

“Restoring competitiveness and boosting potential growth is critical. Impressive progress has been made in structural reforms. A far-reaching pension reform has been approved by

parliament, and substantive labor market reform is underway. Priority now needs to be given to opening closed professions, moving forward with deregulation, implementing the services directive, and eliminating barriers to tourism and retail trade, where potential for growth remains high.

“Liquidity in banks remains tight but manageable, supported by the ECB and the government’s guarantee program. The new Financial Stability Fund provides an important back-stop for capital adequacy. Moreover, the Greek authorities have commissioned a strategic review for the banking sector and a due diligence for state banks. Continued close monitoring of the financial sector will be important,” Mr. Portugal said.

Statement by Panagiotis Roumeliotis, Alternate Executive Director for Greece

September 10, 2010

We thank staff for the excellent report and for their efforts to assist the Greek authorities in the implementation of the Stand-By Arrangement.

The first review of the economic adjustment program follows a joint EC/IMF/ECB mission in Athens between July 26th and August 4th, which concluded that Greece has achieved impressive budgetary consolidation during the first half of 2010 and has also made remarkable progress in major structural reforms.

More specifically, the fiscal program is progressing well, as all budgetary criteria for June 2010 have been met and all fiscal measures planned for 2010 have been adopted. Significant progress is being made in structural fiscal reforms, while major pension as well as labor market reforms have been adopted ahead of plan. Financial policies are being strengthened, the financial stability fund has been established, and the collection and processing of fiscal data has improved. Important structural reforms are being promoted in several sectors.

Economic Outlook

The contraction of the economic activity is estimated at about 4 percent in 2010, but nominal growth will be higher than expected, which implies a slightly lower-than-projected public debt-to-GDP ratio. For 2011, GDP is projected to decline by 2.6 percent. Growth is expected to resume in 2012, to 1.1 percent, before picking up to 2.1 percent in 2013 and 2014.

According to recent estimates by the Bank of Greece, in 2010 total employment will fall by 2¼-2½ percent, and the unemployment rate may increase to above 12 percent.

HICP inflation is expected to approach 4.8 percent by the end of 2010. The total impact of higher indirect taxation is estimated at 2.9 percentage points. Inflation is expected to decline substantially in 2011 and 2012.

In 2010, the current account deficit has been revised upward because of stronger domestic demand and higher oil prices. In January-June 2010, the current account deficit rose year-over-year by only 0.2 percent. This mainly reflected an increase in the oil bill by 23.4 percent, a fall in the surplus of the current transfers account, and, to a smaller extent, an increase in the net payments for purchases of food. Exports of goods, excluding oil and ships, fell by 4.9 percent, while imports fell by 8.7 percent.

Fiscal Policy

Fiscal consolidation is underway. One of the main objectives of the program is to reduce the fiscal deficit to below 3 percent of GDP by 2014, with the debt-to-GDP ratio beginning to stabilize by 2013 and declining gradually thereafter.

According to estimates by the Bank of Greece, on a year-over-year basis, in January-August 2010 the central government net borrowing requirements fell by 28.0 percent on a cash basis. The Bank of Greece's figures show a rise in ordinary budget revenues by 3.5 percent. Ordinary budget primary expenditure fell by 13.6 percent and interest payments rose by 7.1 percent. Public investment spending fell by 32.8 percent.

Despite the strong start of the fiscal consolidation program, the first review highlights that major challenges and risks remain in the fiscal area, in particular with regard to the performance of general government entities below the state level (chiefly local authorities and social security funds).

However, the authorities remain committed to the program's fiscal target. In the second half of the year, the Greek authorities will limit the fiscal deficit of the general government by fully implementing the agreed fiscal measures (VAT, excises, and benefits from the pension and wage cuts); revenue increases will allow all payments and the amortization of any mid-year arrears by end-2010.

The joint EC/ECB/IMF mission now projects that the general government deficit will decline to 7.9 percent of GDP in 2010 (instead of the initially projected 8.1 percent), on the basis of the government's commitments to: (a) keeping the state budget primary spending below the original program's ceiling so as to address risks to the revenue outlook; and (B) taking additional corrective action as needed, including curtailing domestically-financed investment.

Controlling expenditure of local governments, hospitals, and the social security system has been more difficult to implement than initially expected, but major steps have been taken in this direction. The Greek authorities agreed to continue under-executing spending at the state level and they will limit spending by €4 billion below the earlier program's projections in order to cover risks coming from other parts of the general government. As mentioned in the Memorandum of Economic and Financial Policies, at any time, should fiscal outcomes fall below the targets, the Greek authorities stand ready to take corrective actions.

A far-reaching pension reform has been approved by the Greek Parliament ahead of schedule, introducing a new defined-contribution system to top-up a non-contributory, means-tested, basic pension. This reform will contribute to controlling further the increase in pension spending. The Greek authorities are committed to proceeding with further adjustments to the parameters of the previous system, if needed, in order to reduce the long-run increase in pension costs from 12.5 percentage points by 2060 under the old system to 2.5 percentage points of GDP under the new system.

On structural budgetary policies, important achievements have been realized. The tax reform aims at making the system more progressive by abolishing tax exemptions, fighting tax evasion, and broadening the tax base. Important steps have been made by promoting payment receipts, and by cross-checking tax information with data on wealth and spending habits, in particular of high-income and wealthy tax payers.

In addition, the Greek authorities promoted a new law that strengthens the fiscal management framework, following the suggestion of the IMF technical assistance mission. This implies that the budget for 2011 will be part of a three-year rolling medium-term framework, and the Minister of Finance will be able to control the local government and social budget.

In the health sector, the Greek authorities have accelerated payments to avoid the buildup of arrears, reduced procurement prices of pharmaceuticals by 20 percent by implementing price caps for approved drugs lists, and limited unnecessary prescriptions. Finally the Greek authorities placed accounting firms in state hospitals to improve their financial management. These measures will allow significant savings of resources.

On reforming local governments, the new bill will reduce the number of local administrations and will reduce their budget by €500 million in each of the three years during 2011-2013.

Major reforms have been promoted in the field of state enterprises in order to strengthen performance and reduce contingent risks to the budget. By enhancing efficiency, increasing tariffs in public transportation, and reducing excessive allowances and overtime, the Greek authorities intend to reduce the state guarantees provided to those enterprises and the attendant fiscal risk. In particular, the draft law to restructure the railway sector will be discussed in the Parliament by end-September. Its implementation will produce cost reductions and will make the train operator profitable for the year 2011.

Financial Sector Policies

In the financial sector, liquidity remains tight and solvency ratios are affected by the economic downturn, but the situation of the financial sector is manageable. The Greek banking sector as a whole remains resilient in the face of a challenging macroeconomic environment. All banks remain in compliance with the minimum capital adequacy requirement of 8 percent. In August, private deposits stabilized after a downward trend in the previous months.

The recent CEBS stress tests covered more than 90 percent of banking system assets and all but one bank passed. To facilitate the access by Greek banks to wholesale markets, the authorities are committed to providing a new tranche of government guarantees for bank bonds in the amount of €25 billion. The Financial Stability Fund law has been approved, by Parliament, providing a facility for a sound level of bank equity. The Greek authorities have requested a preliminary due diligence and, following the outcome of this study, they will formulate a program to enhance financial stability and efficiency in the banking system.

Structural Policies and Competitiveness

The Greek authorities have demonstrated their commitment to implementing far-reaching structural reforms in order to regain competitiveness and restore growth. In fact, crucial new legislation has been introduced, notably to ease employment protection legislation and collective dismissals, reform minimum wages, and allow firm-level agreements to prevail over other levels. Moreover, reforms in public employment to reduce labor-market distortions have been implemented. Further measures will be taken to reform collection bargaining, including the elimination of the automatic extension of sectoral agreements to those not represented in the negotiation and the adoption of legislation to introduce symmetry in the arbitration system.

An important development is the three-year national general collective wage agreement signed by the social partners on July 15th. These provisions yield average annual increases of minimum wages equal to 1.7 percent in 2010 (exclusively because of 2009 carryover), 0.8 percent in 2011, and 1.5 percent in 2012. In real terms, these developments result in a bigger wage cut than that assumed in the MoU. More importantly, the agreement signals the social partners' awareness of the gravity of the situation as well as their broad acceptance of current economic policy goals.

As a result of the new policies, the Bank of Greece estimates that the unit labor cost growth in the total economy will actually turn negative (-1.7 to -2.0 percent) in 2010, taking into account a fall of 12.8 percent in average earnings of government employees and 9.3 percent in average pensions of government pensioners. In 2011, average earnings and compensation per employee in the total economy are expected to decline further.

The Greek authorities decided to fully implement the EU Services Directive, to liberalize the wholesale electricity market, to facilitate start-ups, and to accelerate the authorization of several economic activities. A task force has been established to enhance the growth impact of EU structural funds. Finally, the Greek authorities are taking measures to facilitate FDI and investments in innovation and public-private partnerships. The Greek authorities are committed to eliminating restrictions (licensing requirements, geographic restrictions, regulated tariffs, etc) for entry into a number of professions (pharmacy, notary, architecture, engineering, etc.).

The conclusion of the SBA's first review is a major achievement. Looking forward, the Greek authorities are fully aware that continued effort is necessary, with the ultimate objectives of regaining market confidence and restoring sustained growth. They are fully committed to implementing all the measures needed to fully meet the program's targets.