Eurobank Research
www.eurobank.gr/research
research@eurobank.gr

Eurobank EFG

GREECE MACRO MONITOR

December 22, 2011

Focus notes: Greece

Written By:

Theodosios Sampaniotis
Senior Economic Analyst
tsabaniotis@eurobank.gr

Edited by:

Tasos Anastasatos
Senior Economist
tanastasatos@eurobank.gr

EU Structural Funds in Greece: more necessary than ever

- EU structural funds are critical for boosting growth, especially during the current crisis
- The absorption of EU funds under the NSRF 2007 -2013 got a boost after the decision to increase the EU co-financing rate to 95%;
- MoU targets appear feasible
- Risks remain and further measures are needed for securing the future smooth execution of the program.

EU structural funds[1] were always important for improving the performance of the Greek economy in terms of GDP, employment, productivity, investment and the trade balance. Now, with Greece in the middle of an unprecedented fiscal and economic crisis, EU structural funding is more critical than ever. Given limited access of both the State and the private sector to international capital markets and the negative business climate, EU structural funds are an indispensable tool for boosting economic growth without causing extra fiscal burden.

According to the BoG's Balance of Payments data, in the period 2000 – 2010, Net Transfers (receipts minus payments) from the EU to Greece were on average 2.15% of GDP. These transfers include not only structural funds but also agricultural subsidies.

The largest part of these funds is channeled to public investment. Despite their small size compared to private investments, the size of the fiscal multiplier of public investments is large[2]. Liquidity constraints, both for the public and the private sector, have put the execution of the Public Investments Budget (PIB) under severe pressure. In 2012, in an effort to boost growth, the PIB is projected to increase by 11.8% to €7.7bn (3.6% of GDP). It should be noted though, that both in 2010 and 2011 the PIB was the first to be sacrificed in order to meet fiscal targets.

The inability to secure national funds for public investments means that projects co-financed by the EU have been given priority since 2008. Almost 80% of the 2012 PIB is dedicated to co-financed projects, compared to 50-55% ten years ago. In 2012, €6.0bn of public funds (€4.55bn of them are EU funds) are earmarked for EU co-financed projects (2011: €5.5bn) and €1.7bn for exclusively nationally funded projects (2011: €1.4bn).

The importance of EU structural funds for the Greek economy

The impact of EU funding on GDP is difficult to measure. The European Commission has published periodic reports on the effect of cohesion policy. The latest available[3] includes an

[1] European Regional Development Fund (ERDF), European Social Fund (ESF), Cohesion Fund.

[2] The Foundation of Economic and Industrial Research (IOBE) estimates the multiplier to be [5].

[3] Investing in Europe's future, Fifth report on economic, social and territorial cohesion, Report from the Commission, November 2010.

assessment of the macroeconomic impact of structural funding utilizing two macroeconomic models, HERMIN and QUEST[4]. It focuses on the impact of the 3rd Community Support Framework (2000 – 2006) and estimates the impact of its successor National Strategic Reference Framework (2007 – 2013).

According to the report, actual expenditure funded by EU structural funds (EU contribution) averaged in Greece ca. 1.22% of GDP annually in the period 2000 – 2009[5]. This was the second largest direct contribution after Portugal. Spain, Portugal, Greece, Ireland and East German and Southern Italy regions were the main recipients during this time period. The situation is different for the period 2007 – 2016[6], when the average annual expenditure in Greece falls to ca. 0.76% of GDP, the 13th largest direct expenditure. Reasons include the increase in the Greek regions' GDP, which reduced eligibility for allocating funds, as well as the entry of poorer countries in the EU (EU-10 in 2004, Romania and Bulgaria in 2007). The new member states account for just over half of the cohesion policy expenditure in 2007 – 2013. Portugal is the only one of the old EU-15 member states whose structural funding from the EU remained relatively stable.

The macroeconomic impact of the 2000 – 2006 programs is significant. GDP in Greece increased by an average 1.6% higher each year, over the course of the spending period (2000 – 2009), than it would otherwise have without EU funding (EU average: 1.2%). These effects are cumulative, so that by 2009, GDP in Greece is estimated to have been around 16% higher than what would be the case without EU funding. The effects for Greece are the 3rd largest in the EU.

The macroeconomic impact of the 2007 – 2013 programs is estimated to be smaller. GDP is estimated to increase by an average 1% higher each year above the baseline scenario (without EU funding). The effects for Greece are the 12th largest in the EU.

Another interesting finding is that cohesion policy also affects positively countries which are net contributors, i.e. countries like Germany and France. These advanced economies produce the bulk of capital goods and services that are required by the net recipient countries as they develop. The burden of needing to raise the necessary funds is mitigated by their increased exports. The effect differs from country to country depending on trade relations.

EU structural funding in Greece 2007 – 2013

The NSRF is in its 5th programming year. The fiscal and economic crisis, which started in 2009, made the execution of the program of critical importance both for the smooth implementation of the budget, as well as for boosting private investments. However, it also made securing the necessary national funds almost impossible. In an effort to safeguard the much needed EU funds, the EU came to the rescue once again[7].

The initial program amounted to €26.2bn of available public funds[8]: €20.5bn of EU funds and €5.7bn of national funds. The co-financing rates were 78% EU funds and 22% national public funds. In July 2011, the Greek government reached an agreement with the Commission to reduce the national funds required fro the execution of the program. According to the agreement, EU funds will cover 85% of public funds and only 15% will be national public funds. That means that the absolute level of EU funds remains the same but total available public funds (EU + national) were reduced. Furthermore, the new co-financing rates apply retroactively from the beginning of the program (1/1/2007), meaning that the EU will return to Greece public national funds of €771mn already spent. Until 2013, a total of €1.8bn will be saved. Under this agreement, the revised figures are €24.3bn of total public funds: €20.5bn EU funds and €3.8bn national funds.

In December 12th the EU Council decided to temporarily reduce the co-financing rates for member states under financial difficulties (Greece, Ireland, Portugal, Hungary, Latvia and Romania) by ten percentage points above the usual co-financing rates. That means that for Greece the new co-financing rates will be 95% EU funds and 5% national public funds. As before, the new rates do not imply an increase in EU funds, just a decrease in the necessary national public funds. We estimate the available public funds to be: €20.5bn EU funds and €1.6bn national funds, a total €22.1bn of public funds. This arrangement will be applied retroactively from 1/1/2010 and it will hold until 31/12/2013. According to the BoG[9], this translates into a return of ca. €880mn of national public funds already spent.

One of the conditionalities of the Memorandum of Understanding signed with the IMF and the European Commission is the proper and timely execution of the NSRF. The Greek government has to meet specific targets for payment claims to the EU concerning the absorption of Structural and Cohesion Funds. For 2011 the target

4 For a description of the models and results see: http://ec.europa.eu/regional_policy/sources/docgener/evaluation/pdf/expost2006/wp3_hermin_aggregate.pdf and http://ec.europa.eu/economy_finance/publications/economic_paper/2010/index_en.htm

5 For the 2000–2006 programs, the implementation period lasted until the end of 2009.

6 For the 2007–2013 programs, the implementation period was scheduled to last until the end of 2016.

7 See Eurobank EFG Research previous publications: Greece Macro Monitor July 2006, October 2007 and July 2008 for EU measures that helped boost execution and absorption rates of the 3rd CSF.

8 Initially the program was advertised to amount to €32bn of available public funds: €20.5bn of EU funds, €11.5bn of national public funds. Another €7.5bn of private funds were added for a total of €39.5bn.

9 Monetary Policy, Interim Report 2011, November 2011, pages 162 – 165.

was €3.35bn. According to the latest available data[10] for the execution of the NSRF, at the beginning of December 2011 (4/12/2011) public spending of EU funds in 2011 had reached €2.3bn (68.3%). The Greek authorities believe that they will achieve the target since €800mn of public funds have already been spent and payment claims will be sent to the EC before the end of December and. In addition, operational program's management authorities estimate that an extra €400mn of public spending will take place before year end. For 2012 the target is €3.73bn and for 2013 €3.89bn.

The latest available data for the execution of the NSRF are based on the 85% co-financing rate, but they give a clear picture of the progress made.

A critical stage in the execution of the program is the signing of a binding legal contract. According to December 4th data, €13.4bn worth of contracts have been signed or 55.1% of public funds. For sectoral and regional programs the numbers are 50.8% and 63.2% respectively.

By December 4th, 28.05% or €6.8bn of the total €24.3bn of public (i.e. EU + national) funds was spent, in comparison to 18% at the end of 2010 and just 3.1% at the end of 2009. Public expenditure has reached 25.2% of available public funds on sectoral programs and 29.6% on regional programs.

Public expenditure is not the final stage of the procedure. The Greek government makes three payment applications per year to the Commission, usually in July, October and December. From the total amount of €20.2bn of available EU funds (excluding cross-border programs), €6.7bn have been collected by the Greek government or 33.3%. Since this amount includes €1.5bn in down payments made by the EU Commission on approval of the operational programs in the beginning of the NSRF, which do not correspond to actual expenditure on projects, the real absorption rate of EU funds is 25.8%. According to the Greek authorities this is close to the EU average absorption rate.

In Table 1 more detailed data are presented per program, including Cross-border programs.

According to the Greek authorities no EU funds are in danger due to the application of the n+3 rule[11] for 2011 and most of the targets for 2012 have already been achieved.

Measures to expedite the absorption of EU structural funds

Despite the progress made so far and the adjustment of the co-financing rate to 95%, the need for accelerating the execution of the NSRF is obvious. A number of measures have been decided with the cooperation of EU authorities.

i. A list of 181 priority projects was established with a budget of €11.5bn. These projects will have a significant impact on cohesion, growth and employment. 166 of these projects are co-financed by the ERDF and the Cohesion Fund (energy, transportation, environment, SMEs), the remaining 15 are co-financed by the ESF (education, public administration, employment).
ii. Administrative procedures are being simplified: a new law for environmental licenses, new measures to expedite procedures relating to archaeological findings (respective procedure to be shortened to an average of 41 days from 110 previously), a new law reducing the time for expropriations of land (from 33 to 19 months).
iii. New funding tools: JEREMIE initiative for SMEs (€250mn), JESSICA initiative for urban development programs (€260mn through the EIB), the creation of a guarantee fund for SMEs in order to be able to borrow from commercial banks (€500mn from the NSRF and €500mn from the EIB).
iv. A new web-based monitoring tool of procedures for the approval of project proposals and for the implementation of public projects.
v. The elimination of inactive / sleeping projects[12] and the increase in flexibility of the managing authorities to transfer resources between projects. According to data released from the Greek authorities, from ca. 7.500 projects approved for funding from the NSRF, 4.700 with a budget of €5.5bn were sleeping projects. They have been reduced by 39%, mostly by succeeding to move them to the next stage, i.e. signing of a contract.
vi. In the June 2011 EU Summit it was decided to form a Task Force to help the Greek authorities, among other things, with the execution of the NSRF. The Task Force will issue quarterly progress reports.

Risks for the smooth execution of the NSRF

The measures taken above and the reduction of the co-financing rate do not eliminate all the risks for the proper and timely execution of the program. These risks include but are not limited to:

i. The increase in the co-financing rate results in a decrease in total available public funds, as mentioned above. This limits drastically the ability to finance new projects and the authorities need to be very conservative in the allocation and especially the reallocation of funds between projects in order to boost absorption rates.

[10] Source: Monitoring Information System (M.I.S.)

[11] The n+3 rule states that after the signing of a contract for the execution of a project the public funds committed to this project will have to be spent, no latter than the end of the third calendar year, after the year the contract was signed. Hence, if a contract was signed in 2010, funds will have to be spent by the end of 2013.

[12] Projects already approved in the operational programmes but not yet contracted within the appropriate timeframes (6 months to 2 years).

Table 1
NSRF 2007 -2013
Available funds (85% co-financing rate) & execution progress

Operational Program	Public Funds (€ bn)	EU Funds (€ bn)	Signed Contracts (% of public funds)	Public Expenditure (% of public funds)	Absorption Rate (% of EU funds w/o down payments)
Environment - Sustainable Development	2.1	1.8	33.5	19.6	18.3
Accesibility Improvement	4.3	3.7	62.4	27.8	26.5
Competitiveness & Enterpreneurship	1.5	1.3	87.1	52.6	51.9
Digital Convergence	1.0	0.9	26.2	18.2	16.2
Human Resources Development	2.7	2.3	36.3	21.9	21.7
Education & Lifelong Learning	1.7	1.4	54.5	21.4	20.4
Public Administration Reform	0.6	0.5	18.2	9.7	9.7
Techincal Support for Implementation	0.2	0.19	86.7	27.6	27.4
Total Sectoral Programs (1-8)	**14.2**	**12.0**	**50.8**	**25.9**	**24.9**
National Contingency Reserve	0.19	0.16	4.3	0.6	0.6
Macedonia - Thrace	3.1	2.7	68.5	33.0	28.5
Western Greece – Peloponnese – Ionian islands	1.1	0.9	51.1	27.1	23.9
Crete and Aegean islands	1.1	0.9	75.0	35.3	22.0
Thessaly - Mainland Greece – Epirus	1.4	1.1	81.9	42.7	38.0
Attica	2.9	2.4	48.2	28.5	25.4
Total Regional Programs (10-14)	**9.6**	**8.0**	**63.2**	**32.7**	**27.6**
Greece-Cyprus	0.06	0.05	41.7	3.6	
Greece-Bulgaria	0.13	0.11	51.4	0.5	
Greece-Italy	0.12	0.09	5.0	0.1	
Greece-FYROM	0.01	0.01	10.0		
Greece-Albania	0.01	0.008	10.0		
Total Cross-border Programs (15-19)	**0.33**	**0.27**	**30.3**	**0.9**	
Total NSRF (1-19)	**24.3**	**20.5**	**55.1**	**28.0**	**25.8**

Source: 3rd Conference of the Presidents of the Monitoring Committees of the National Strategic Reference Framework, the Programme of Agricultural Development and the Operational Programme for Fishery.

ii. The new funding tools (JEREMIE etc.) are useful in helping EU funds find their way to SMEs. Still, it remains unclear if they will manage to overcome administrative problems, associated with the approval of investment proposals, monitoring and the timely completion of the projects.
iii. Many administrative problems remain unsolved. One of the goals of the EU authorities is that for any project, a single person or unit will be accountable. This has not been achieved yet for all projects. Furthermore, in many cases timelines remain unclear.
iv. Last but not least, there is a risk associated with the closure of the previous programming period of EU structural funds, the 3rd CSF 2000 – 2006. The EU authorities have warned Greece that a total of 1.000 projects remain uncompleted. According to EU rules the deadline for some of these projects expires in September 2012 and for others in March 2013. If the Greek authorities miss those deadlines EU funds spend on these projects will have to be returned to the EU. Funds at risk are estimated at €3.5bn. EU authorities estimate that €260mn of national public funds are required for the completion of these projects. According to the Greek authorities, most of the projects face administrative difficulties that will be resolved on time.

The future of EU structural funds: 2014 – 2020

The discussions and negotiations for the new programming period for EU's structural and cohesion funding, 2014 – 2020, are already under way. Greece is expected to receive much less funding than under the NSRF. The proposals of the European Commission on the new rules and procedures make clear that emphasis will be given to utilizing new funding tools and sources, such as the EIB, risk capital, risk funds, local development funds etc. Regions with GDP per capita above 90% of the EU average will receive limited funding and only for projects improving competitiveness, renewable energy sources, SMEs and innovation. For Greece, it is possible that only three from the current eight regions will be eligible for funding under the new rules. An agreement on the final allocation of funds to the regions of the 28 member states (including Croatia) will have to be reached until the end of 2012.

The EU authorities use in their calculations for the allocation of funds, an average GDP of the last three years for which data are available. According to a recent press conference by Commissioner for Regional Policy Mr. Hahn, data for the period 2007 – 2009 will be used for GDP at the regional level and data for the period 2008 – 2010 for GDP at the national level. The effects of the ongoing crisis on these figures will be taken into consideration. It is unclear whether Greece will succeed in negotiating for more funds based on the current levels of regional GDP or decisions will be based on data before the culmination of the present crisis, resulting in fewer regions being eligible for structural funding.

Research Team

Financial Markets Research Division

Platon Monokroussos: *Head of Financial Markets Research Division*
Paraskevi Petropoulou: *G10 Markets Analyst*
Galatia Phoka: *Emerging Markets Analyst*

Sales Team

Nikos Laios, Head of Sales
Vassillis Gulbaxiotis, Head of International Sales
Yiannis Seimenis, Ioannis Maggel, Corporate Sales
Stogioglou Achilleas, Private Banking Sales
Alexandra Papathanasiou, Institutional Sales

Economic Research & Forecasting Division

Dimitris Malliaropulos: *Economic Research Advisor*
Tasos Anastasatos: *Senior Economist*
Ioannis Gkionis: *Research Economist*
Vasilis Zarkos: *Economic Analyst*
Stella Kanellopoulou: *Research Economist*
Olga Kosma: *Economic Analyst*
Maria Prandeka: *Economic Analyst*
Theodosios Sampaniotis: *Senior Economic Analyst*
Theodoros Stamatiou: *Research Economist*

Eurobank EFG, 20 Amalias Av & 5 Souri Str, 10557 Athens, tel: +30.210.333 .7365, fax: +30.210.333.7687, contact email: Research@eurobank.gr

Eurobank EFG Economic Research

More research editions available at http://www.eurobank.gr/research

- **New Europe**: Economics & Strategy Monthly edition on the economies and the markets of New Europe
- **Economy & Markets**: Monthly economic research edition
- **Global Economic & Market Outlook**: Quarterly review of the international economy and financial markets

Subscribe electronically at http://www.eurobank.gr/research
Follow us on twitter: http://twitter.com/Eurobank_EFG