

## Greece: 2017 Budget Assessment

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The Greek Government submitted in Parliament the 2017 Budget. The 2017 Budget is to be voted by Parliament until December 10<sup>th</sup> 2016. Below we present a brief review of the basic 2017 Budget items:

- **Macroeconomic assumptions:** The new budget is framed on an improved macroeconomic environment, envisaging real GDP growth of -0.3% and 2.7% for 2016 and 2017 (Table 1) respectively. That is, assuming swift implementation of the fiscal and structural reforms agenda agreed with official creditors in the context of the 3rd bailout programme. In more detail, the expected performance for 2016 is attributed mainly to investment. Both private and public consumption are expected to remain on a negative territory. For 2017, private consumption is expected to return on a positive territory (public consumption will remain negative at -0.3%) while investment will continue the positive contribution and net exports will rebound mainly on the back of an expected improvement in disposable incomes amid a further increase in employment, a rebound in consumer confidence, the anticipated improvement on credit conditions, the continuation of strong rates of absorption of EU structural funds, and the further relaxation of capital controls. Elsewhere, unemployment is projected to remain in a declining path for the fourth year in a row (22.6% in 2017 vs. 23.7% in 2016), while HICP inflation is expected to turn positive for the first time since 2012 (+0.6% in 2017 vs. 0.0% in 2016), supported by higher oil prices and the recovery of domestic demand.
- **Fiscal targets for 2016 and 2017:** The primary balance in programme terms for 2016 and 2017 is expected at €1.91 bn or 1.1% and at €3.69 bn or 2.0% higher compared to the official targets of the 3rd MoU. i.e. 0.5% and 1.75% for 2016 and 2017 respectively (Table 2). Ordinary budget balance revenue is expected to increase by 2.9% and 4.7% on an annual basis in 2016 and 2017 respectively. On the other hand, ordinary budget expenditure is expected to change by 3.0% and -2.9% on an annual basis in 2016 and 2017 respectively. These targets are on the back of the total expenditure and revenue measures of €1.42 bn and €2.60 bn for 2016 and 2017 respectively (Table 3) that were agreed in May – June 2016 (1<sup>st</sup> Review of the 3<sup>rd</sup> Economic Adjustment Programme). The expected over performance (0.6%) of the 2016 primary surplus target compared to the respective programme figure is mainly due to:
  1. An expected improvement by ca €0.36 bn of the net state budget revenue in ESA2010 terms which comes as a result of an expected increase of certain items in recurring revenue (direct, indirect taxes, and non-tax revenue).
  2. An expected improvement of €0.84 bn in the balance (deficit) of the Social Security Funds relative to the respective 2015 figure, as a result of an expected significant reduction of the social security funds cash balances and the reduction of the respective national accounts adjustment due to the activation of the new social security fund (EFKA) that will incorporate the existing funds.
  3. An expected decrease in General Government net interest payments by €0.80 bn due to lower current interest rates and lower nominal debt levels compared with the respective 2016 Budget figure. The 2016 General Government Debt was expected at €327.60 bn in the 2016 Budget while the respective 2017 Budget figure is expected at €315.4 bn mainly as a result of the lower bank recapitalization needs.
  4. The lower forecast for the 2016 nominal GDP that was due to the base effect created by the recently revised nominal 2015 GDP (ELSTAT revision of October 14<sup>th</sup> 2016).
 In addition, for 2017 the achievement of the expected primary balance target is attributed – besides the fiscal interventions in revenue and expenditure, the real growth rate of 2.7% and the base effect due to the revised 2015 nominal GDP mentioned above – to a further streamlining of the cash balances of the various central and general government entities and to an expected decrease in General Government net interest payments by -1.3% on an annual basis. Finally, the implementation of the Unified Solidarity Income scheme for 2017 will create a cost of €0.7 bn for the 2017 Budget.
- **Gross public debt:** General Government gross public debt is expected at €315.4 bn (or 180.3% of GDP) and at €319.20 bn (or 176.5% of GDP) for 2016 and 2017 respectively. These figures are lower than the respective European Commission forecasts (€317.5 bn or 181.6% and €324.4 bn or 179.1% for 2016 and 2017 respectively). Note that total debt financing needs for 2017 are expected at €15.3 bn according to the 3<sup>rd</sup> Economic Adjustment Programme (June 2016).

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See next page

**Key takeaway**

The achievement of the 2016 primary surplus target of 1.1% of GDP of the 2017 Budget, is attainable conditional on no major negative surprises on the revenue and / or the expenditure side of the budget. According to the State Budget execution for the January – October 2016 period, on a modified cash basis, the primary balance was at €6.50 bn which was due primarily to the over performance of the ordinary budget net revenue and to a lesser extend to the under execution of expenditure. The Eurobank Research adjusted primary balance (APS) was at €3.95 bn. The APS was calculated under the working assumptions that: a) ordinary budget revenue was at its realized level, and b) tax refunds, budget expenditure and PIB revenue and expenditure were at their target levels. At the same time, the ELSTAT's flash estimate of the 3<sup>rd</sup> quarter of 2016 was at 1.5%yoy, thus signaling at least the attainability of the 2016 real growth forecast of -0.3%. On the other hand, the attainability of the 2017 primary surplus target is subject to the achievement of the 2.7% real growth forecast. Currently, the market consensus supports a real growth rate at the vicinity of 1.3% for 2017. Realization of such an adverse scenario will create – at least - a significant revenue shortfall for 2017. The baseline scenario of 2.7%, in our view, is conditional on:

1. the timely conclusion of 2<sup>nd</sup> review of the 3<sup>rd</sup> Economic Adjustment Programme;
2. the continuation of official discussions on debt relief for Greece on the basis of the short and medium term measures agreed in May 2016 (assuming a timely completion of the 2<sup>nd</sup> programme review, we expect further specification and gradual implementation of the short-term debt relief framework before year end);
3. the inclusion of Greece in the ECB's quantitative easing program (PSPP);
4. the measurable progress in dealing with NPLs, which along with a further relaxation/removal of capital controls could notably improve the outlook for domestic credit;
5. the significant pick-up in domestic sentiment, investment and export activity;
6. the speedy absorption of EU structural funds (>€35bn committed for Greece in the EU budget for 2014-2020) and the utilization of available resources and possibilities provided by the European Commission's Investment Plan for Europe;
7. the continuation of product and labor market reforms aiming to create a more business friendly environment, enhance competitiveness and boost extroversion;
8. the implementation of reforms to increase efficiency in the public sector and the judiciary system;
9. the further relaxation / removal of capital controls, with a view to boost depositor confidence and ease lingering investor worries over the safety of their cash-flows;
10. the absence of a major external shock emanating from e.g. the refugee crisis, the change of government in the US, Brexit negotiations and the upcoming round of elections/referendums in a number of euro area countries in the months and quarters ahead.

<b>Table 1: 2017 Draft Budget- Main macroeconomic aggregates (realisation and forecasts, % YoY)</b>			
	<b>2015</b>	<b>2016 (f)</b>	<b>2017 (f)</b>
<b>Real GDP</b>	-0.2	-0.3	2.7
<b>Private consumption</b>	-0.2	-0.6	1.8
<b>Public consumption</b>	0.0	-1.5	-0.3
<b>Investment</b>	-0.2	3.3	9.1
<b>Exports of goods &amp; services</b>	3.4	0.8	5.3
<b>Imports of goods &amp; services</b>	0.3	2.7	3.2
<b>GDP deflator</b>	-1	-0.2	0.7
<b>Harmonized CPI</b>	-1.1	0.0	0.6
<b>Employment*</b>	0.5	1.0	2.0
<b>Unemployment** (f)</b>	22.9	21.8	20.6
<b>Unemployment*** (f)</b>	24.9	23.7	22.6

\*national accounts basis

\*\* Domestic Forecasts

\*\*\* Labor Force Survey

Source: Ministry of Finance

See next page

	2015	2016		2017 Budget forecasts
		2016 Budget projection	2017 Budget Forecast	
<b>I. Central government revenue (a+b+c+d+e+f)</b>	<b>51.59</b>	<b>53.65</b>	<b>52.48</b>	<b>54.53</b>
a. Ordinary budget net revenue	46.76	49.23	48.10	50.37
a.1. Recurring Revenue	47.79	48.43	50.48	51.00
a.1.1 Direct taxes	19.94	20.03	20.71	20.42
a.1.2 Indirect taxes	23.78	24.74	25.11	26.44
a.1.3 Drawings from EU	0.43	0.33	0.40	0.52
a.1.4 Non-Tax revenue	3.65	3.34	4.26	3.62
b. Non-recurring Revenue	1.53	0.58	0.42	0.27
c. Tax refunds	3.11	3.27	3.29	3.29
d. Privatization Proceeds	0.25	1.80	0.12	2.04
e. ANFA&SMP Revenue	0.29	1.69	0.38	0.35
f. Public Investment Budget (PIB) revenue	4.83	4.42	4.38	4.16
<b>II. Central government expenditure (a+b)</b>	<b>55.92</b>	<b>57.18</b>	<b>57.77</b>	<b>56.29</b>
a. Ordinary budget expenditure	49.54	50.43	51.02	49.54
a.1. Primary expenditure	43.74	44.50	45.42	43.99
a.2. Net interest payments	5.80	5.93	5.60	5.55
b. Public Investment Budget (PIB) outlays	6.38	6.75	6.75	6.75
<b>III. State Budget Balance- Modified cash basis</b>	<b>-4.33</b>	<b>-3.53</b>	<b>-5.29</b>	<b>-1.76</b>
% GDP	-2.5%	-2.0%	-3.0%	-1.0%
<b>State Budget Primary Balance-Modified cash basis</b>	<b>1.47</b>	<b>2.40</b>	<b>0.31</b>	<b>3.79</b>
% GDP	0.8%	1.4%	0.2%	2.1%
<b>IV. National accounts adjustments</b>	<b>-4.45</b>	<b>-2.85</b>	<b>-1.77</b>	<b>-2.06</b>
National accounts adjustments - Revenue	-3.21	-2.70	-1.17	-1.93
National accounts adjustments - Expenditure	-1.24	-0.14	-0.61	-0.14
<b>IV. State Budget Revenue - ESA 2010</b>	<b>48.38</b>	<b>50.95</b>	<b>51.31</b>	<b>52.60</b>
<b>State Budget Expenditure - ESA 2010</b>	<b>57.16</b>	<b>57.32</b>	<b>58.37</b>	<b>56.42</b>
<b>V. State Budget Balance- ESA 2010</b>	<b>-8.78</b>	<b>-6.37</b>	<b>-7.06</b>	<b>-3.82</b>
% GDP	-5.0%	-3.7%	-4.0%	-2.1%
<b>State Budget Primary Balance-ESA 2010</b>	<b>-1.97</b>	<b>0.56</b>	<b>-0.71</b>	<b>2.43</b>
% GDP	-1.1%	0.3%	-0.4%	1.3%
<b>VI. Central Government Balance - ESA 2010</b>	<b>-13.13</b>	<b>-2.97</b>	<b>-3.85</b>	<b>-1.28</b>
<b>VII. General Government Balance - ESA 2010</b>	<b>-13.23</b>	<b>-3.69</b>	<b>-3.77</b>	<b>-1.46</b>
% GDP	-7.5%	-2.1%	-2.2%	-0.8%
<b>VIII. General Government Interest payments</b>	<b>6.33</b>	<b>6.82</b>	<b>6.02</b>	<b>5.94</b>
% GDP	3.6%	3.9%	3.4%	3.3%
<b>IX. General Government Primary Balance-ESA 2010</b>	<b>-6.91</b>	<b>3.13</b>	<b>2.25</b>	<b>4.48</b>
% GDP	-3.9%	1.8%	1.3%	2.5%
<b>X. Primary balance adjustments - Programme terms</b>	<b>7.35</b>	<b>-2.21</b>	<b>-0.35</b>	<b>-0.79</b>
<b>XI. General Government Primary Balance-Programme terms</b>	<b>0.44</b>	<b>0.92</b>	<b>1.91</b>	<b>3.69</b>
% GDP	0.3%	0.5%	1.1%	2.0%
<b>XII.. Public Debt</b>	<b>311.67</b>	<b>327.60</b>	<b>315.40</b>	<b>319.20</b>
% GDP	176.90	176.90	178.90	174.80
<i>GDP</i>	175.70	174.44	174.91	180.82

Source: Ministry of Finance

See next page

Table 3: Budget 2017: Fiscal Measures (annual basis basis, € bn)			
	2016	2017	Total measures (2017-2017)
<b>Total Measures</b>	<b>1.42</b>	<b>2.60</b>	<b>4.01</b>
Interventions on Wages and non wage Comensation	0.01	0.08	0.08
Interventions on Pensions	0.15	0.56	0.72
Interventions on Social Security Contributions and related allowances	0.65	-0.59	0.06
Interventions on Ministry of Dence Expenditure	0.01	0.09	0.09
Revenues of the General Government entities	0.00	0.01	0.01
Revenues - State Government (Taxes)	0.60	2.45	3.05

Source: Ministry of Finance

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