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

GREECE MACRO MONITOR

September 20, 2012

Focus notes: Greece

Theodosios Sampaniotis
Senior Economic Analyst
tsabaniotis@eurobank.gr

EU Structural Funds in Greece: high risks and enormous potential

- Approximately €14bn of public (EU + national) funds or 1.9% of projected GDP are available and 3.5 years left to utilize them.
- Greece is close to the EU average in absorption rates. Yet, MoU targets concerning EU funds absorption for 2012 are at risk.
- Delays are caused by liquidity problems and bureaucratic obstacles.
- The disbursement of the pending installment of the Greek economic adjustment program and the recapitalization of Greek banks plus a series of administrative measures will give a boost.
- Negotiations for EU structural funding during the 2014-2020 programming period are under way. A critical issue for Greece is whether or not the consequences of the recent severe economic crisis on Greek regional GDP will be taken into account in calculating relative living standards across EU-27.

Increase in the co financing rate

The National Strategic Reference Framework (NSRF) 2007 – 2013, the program under which EU structural funding is implemented in Greece, is in its 6th programming year. The execution of the program is of critical importance both for the smooth implementation of the budget, as well as for boosting private investments, especially during the current severe economic and fiscal crisis. Projects under the NSRF are co-financed with EU and national funds. Securing the necessary national funds has become very difficult.

The December 2011 EU Council decided to temporarily raise the EU co-financing rate (which had already been raised to 85%[1]) by a further 10% for member states under financial difficulties. This means that for Greece the new co financing rates will be 95% EU funds and 5% national public funds.

The new rates do not imply an increase in EU funds, just a decrease in the necessary national public funds. This arrangement will be applied retroactively from 1/1/2010 and it will hold until the end of 2013. Based on payment claims already submitted by the Greek authorities to the EU, Greece will receive €958mn from the EU for expenditure that was covered by national public funds. The increase to the 85% co financing rate accounts for €409bn and the supplementary increase to 95% accounts for another €549mn.

Execution of the NSRF 2007 - 2013

The latest available data for the execution of the NSRF are based on the 85% co-financing rate: €20.2bn of EU funds plus €3.8bn of national public funds for a total of €24bn public funds[2].

[1] Previously the maximum co financing rate ranged from 50% to 85% depending on the objective of each project and on which EU structural fund co financed it.

[2] Based on the 95% co financing rate, national public funds should be around €2bn. According to the initial (2006) NSRF financing plan, national public funds were supposed to be €11.5bn plus €7.5bn of private sector funds.

Nevertheless they give a clear picture of the progress made. These figures do not include the €0.34bn of public funds available for the Cross-border cooperation programs.

An important stage in the execution of the program is the *signing of a binding legal contract* for a specific project. According to September 17th data, €17bn worth of contracts have been signed or 70.7% of available public funds. For sectoral and regional programs the numbers are 67.9% and 75.9% respectively.

The most important stage is *the actual spending of the funds*. That means that part of or a whole project was delivered and the national authorities paid the contractor or the beneficiaries. By September 17th, 38.8% or €9.3bn of the total €24bn 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. Expenditure has reached 36.1% of available public (EU and national) funds on sectoral programs and 43.5% on regional programs.

Since, according to EU regulations, expenditure on projects is possible until the end of 2015 when projects should be completed, the Greek authorities have 3.5 years to spend the remaining €14.7bn. If we take into account the increase of the EU co financing rate we estimate total available public funds to be €14bn, or 1.9% of projected GDP for the period mid 2012 - end 2015.

In Table 1 more detailed data are presented per Operational Program (OP). Regional programs on average appear to be in better shape than Sectoral programs.

The progress of the Cross-border Cooperation Programs is presented in Table 2, with end of July 2012 data.

Public expenditure is not the final stage of the procedure. The Greek authorities have to submit payment claims to the European Commission in order to collect the EU funds. Actually one of the conditionalities of the Memorandum of Understanding signed with the IMF and the European Commission in May 2010 is the proper and timely execution of the NSRF. The Greek government has to meet specific targets

Table 1

NSRF 2007 -2013

Available funds (85% co-financing rate) & execution progress

	Operational Program	**Public Funds (EU + national) (€ bn)**	**EU Funds (€ bn)**	**Signed Contracts* (% of public funds)**	**Public Expenditure (% of public funds)**
1	Environment - Sustainable Development	2.1	1.8	49.3	28.4
2	Accessibility Improvement	4.4	3.7	80.5	38.2
3	Competitiveness & Enterpreneurship	1.5	1.3	111.2	66.5
4	Digital Convergence	1.0	0.9	32.1	23.1
5	Human Resources Development	2.7	2.3	57.4	35.8
6	Education & Lifelong Learning	1.7	1.4	66.2	29.4
7	Public Administration Reform	0.6	0.5	36.1	13.4
8	Techincal Support for Implementation	0.2	0.19	89.0	33.5
	Total Sectoral Programs (1-8)	**14.2**	**12.0**	**67.9**	**36.1**
9	*National Contingency Reserve*	*0.19*	*0.16*	*18.3*	*2.1*
10	Macedonia - Thrace	3.1	2.7	82.5	43.5
11	Western Greece – Peloponnese – Ionian islands	1.1	0.9	58.3	38.3
12	Crete and Aegean islands	1.1	0.9	85.2	46.5
13	Thessaly - Mainland Greece – Epirus	1.4	1.1	102.4	60.6
14	Attica	2.9	2.4	58.5	36.0
	Total Regional Programs (10-14)	**9.6**	**8.0**	**75.9**	**43.5**
	Total NSRF (1-14)	**24.0**	**20.2**	**70.7**	**38.8**

* Signed contracts in terms of public expenditure appear in some programs to exceed available public funds. This is done in order to ensure a pool of eligible for EU funding projects. If there are problems or delays in the actual execution of any project it will be easily replaced.

Source: Ministry for Development, Competitiveness, Infrastructure, Transport and Networks

Table 2
Cross-border Programs

	Operational Program	Public Funds (EU + national) (€ bn)	EU Funds (€ bn)	Signed Contracts (% of public funds)	Public Expenditure (% of public funds)
1	Greece-Cyprus	0.06	0.05	65.8	13.2
2	Greece-Bulgaria	0.14	0.11	94.1	11.2
3	Greece-Italy	0.12	0.09	64.7	6.9
4	Greece-FYROM	0.01	0.01	29.7	0
5	Greece-Albania	0.01	0.008	10.0	--
	Total Cross-border Programs (1-5)	**0.34**	**0.27**	**73.8**	**9.3**

Source: Ministry for Development, Competitiveness, Infrastructure, Transport and Networks

Table 3
MoU Targets & Actual Absorption
(Payment claims to be submitted between 2010 and 2013)

(in € mn)	2010	2011	2012	2013
European Regional Fund and Cohesion Fund	2,330	2,600	2,850	3,000
European Social Fund	420	750	880	890
Target of first half of the year		1,105	1,231	1,284
Target of second half of the year		2,245	2,499	2,606
Total annual absorption target	**2,750**	**3,350**	**3,730**	**3,890**
Absorption	**2,820**	**3,390**	**877**	

Sources: Ministry for Development, Competitiveness, Infrastructure, Transport and Networks (September 17th, 2012 data), Greece: Memorandum of Understanding on specific economic policy conditionality (May 2010).

for payment claims to the EU concerning the absorption of Structural and Cohesion Funds (see Table 3). The Greek government makes three payment applications per year to the Commission, usually in July, October and December. According to Ministry for Development data the target for 2010 and 2011 was met and for 2012 until September 17, payment claims of €877mn were made to the Commission.

EU member states absorption rates

According to European Commission's end of July 2012 data, from the total amount of €20.2bn of EU funds available for Greece, €8.4bn have been collected by the Greek government or 41.4%. This is close to the average EU absorption rate of 41.5%. Recipient Member State's absorption rates of cohesion policy funds are presented in Graph 1.

Absorption rates are low for European Social Fund (ESF)[3] co-financed programs. The ESF provides app. 1/5 of total EU funds for Greece. According to end August 2012 data, Greece has received 36.8% of available ESF funds compared to an EU average of 44.9%.

[3] EU structural funding for the NSRF comes from three EU funds: the European Regional Development Fund (ERDF) 60.5% of total EU funds, the European Social Fund (ESF) 21.4% of total EU funds and the Cohesion Fund (CF) 18.1% of total EU funds.

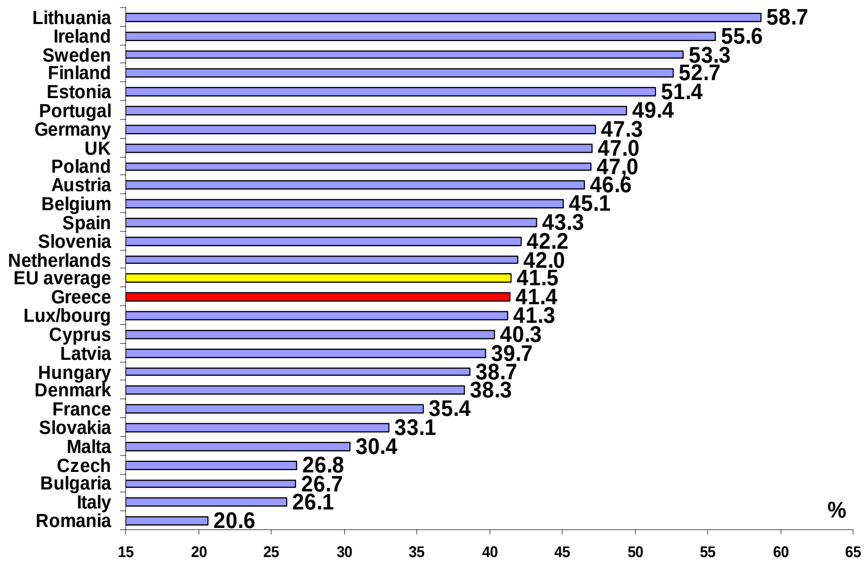
Risks

There are serious risks to the smooth absorption of EU structural funds, not only for the programming period 2007-2013 (NSRF) but for funds from the previous[4] programming period 2000-2006[5]. These risks are associated both to the severe economic and financial crisis and to administration mechanism problems.

The problems faced due to the economic crisis and the subsequent liquidity shortage and fiscal slippages are evident in the execution of the Public Investment Budget (PIB). 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. The initial 2012 PIB was €7.7bn; €6.0bn of public funds were earmarked for EU co-financed projects (of which €4.55bn are EU funds), and €1.7bn for exclusively nationally funded projects (respective figures for 2011: €5.5bn for co-financed projects and €1.4bn for exclusively nationally funded projects). The execution of the PIB is under severe pressure. As in 2010 and 2011, the PIB was the first to be

[4] 3rd Community Support Framework. For more details on the size and the implementation of the 3rd CSF see previous issues of our Greece Macro Monitor: March 2010, July 2008, and October 2007.
[5] According to EU regulations these projects should have been completed by the end of 2008, but in order to facilitate the smooth transition from the 3rd CSF to the NSRF, EU authorities gave further extensions and some projects were even financed by both programs.

Graph 1
EU Member States absorption rates
(% of funds allocated per MS paid by the Commission)



Source: EU Commission

sacrificed in order to meet fiscal targets. Already in February 2012 the PIB was cut by €400mn to €7.3bn when the Supplementary Budget was adopted. The fiscal slippages in the revenue side and the inability to reduce spending in other sectors were dealt with partly by cutting down on PIB spending. According to the preliminary state budget execution data for the January – August 2012 period, the expenditure of the PIB was only €2.6bn instead of €4.8bn which was the revised target. That's a difference of €2.2bn or 46% less expenditure on public investment. The timely execution of the NSRF co financed projects is at question.

According to the Task Force for Greece, March 2012 Second Quarterly Report, 872 projects from the previous programming period of EU structural funds (3rd CSF) remain uncompleted. The deadline for around half of them is September 2012 and for the rest is 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 €3bn.

As for the NSRF, press articles[6] mention a recent Ministry for Development internal report that identifies projects at risk to be uncompleted by the end of 2015. These projects have a budget of €7.5bn or almost 1/3 of total available public funds, EU and national. The NSRF ends in 2013 but under EU regulations a project financed under the NSRF will have to be completed by the end of 2015. If a project fails to meet this deadline its cost will have to be covered exclusively by national funds i.e. no further payments of EU funds will be done and any EU funds spent will have to be recovered[7].

Serious problems are faced by the Accessibility Improvement program, dealing with the construction and upgrade of road axes, railway network, port facilities and airports. Even though it has the second highest expenditure rate among sectoral programs, liquidity problems due to the economic crisis have interrupted private sector financing[8]. Construction in concession projects, such as highways has stopped. There are five motorway concessions (1,400 km of the Trans-European-Network) with a budget of €3.2bn of public funds. Construction in four of them has stopped.

The Competitiveness & Entrepreneurship program, which among other things funds SME's modernization and investment plans, has managed to spent more than 2/3 of its budget with the use of special financing tools for SMEs, such as the JEREMIE initiative. That does not mean, however, that the funds used as capital for some of these financing tools have been actually spent, i.e. reached SMEs. Implementation risks remain high due to liquidity problems, since these tools are intended to provide co-financing with commercial banks, and administrative problems, associated

[6] Kathimerini 12/9/2012

[7] During the execution of a project national public funds are disbursed as payments. EU authorities release EU funds to cover EU's share of the cost after the whole project or a sub-project is completed, contingent on the co-funded projects' compliance with the relevant EU regulations.

[8] Private funding is necessary to co-finance infrastructure and productive investment projects which can only be part-financed by public funds, such as infrastructure projects which generate net revenues, e.g. tolled motorways.

with the approval of investment proposals, monitoring and the timely completion of the projects.

The Public Administration Reform program is also a major concern since it has made the least progress. Even though the restructuring of the public sector is a top priority under the Greek Economic Adjustment Program agreed with the EU, the IMF and the ECB, little have been done.

Measures to expedite the absorption of EU structural funds

During the past five years a number of measures have been taken in order to facilitate the absorption of EU structural funds[9]. The most important undoubtedly were the two EU decisions that raised the EU co-financing rate for Greece to 95% and the list of 181 priority high impact projects, accounting for 56% of available funding, which will be the focus of intensive monitoring and support. Since EU structural funds' timely absorption is also a MoU target, a set of relevant measures and actions are part of the conditionalities of the Greek economic adjustment program.

In this context, the new government has announced a series of measures to be implemented as soon as possible. There will be a new restructuring of the program based on the new economic and social conditions and a reallocation of funds from programs running behind schedule to programs in a more advance stage of implementation. Such restructurings have occurred in the past and have given a boost to the execution of the program.

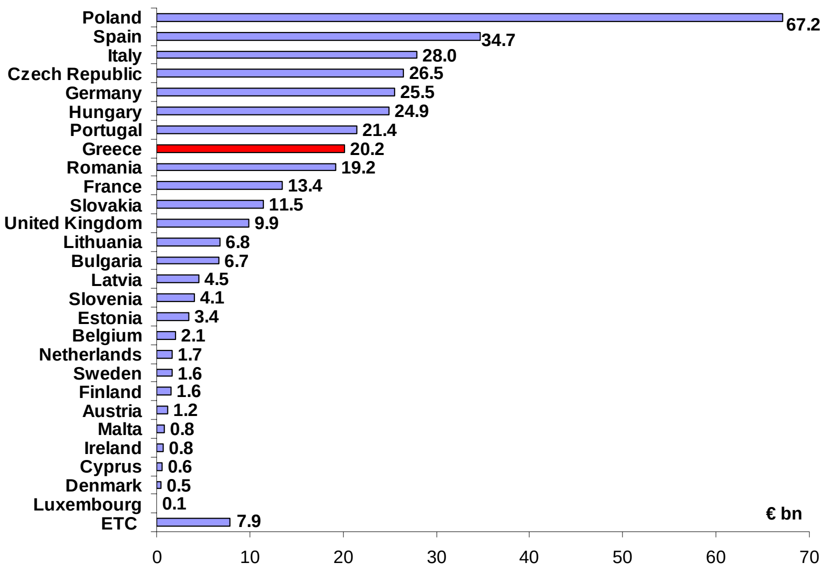
Special attention will be given in the simplification of the entire implementation process:

- legislation to shorten deadlines for contract awarding will be introduced
- legislation was adopted for simplifying and accelerating land expropriation procedures and rationalize the cost
- measures will be taken to remove unnecessary bureaucratic steps and simplify the criteria in order for a project to be selected for co-financing by the NSRF

As described above, one of the main problems concerns delays in the implementation of infrastructure projects, especially concession projects. Highway concessions face the most serious problems. Their financing is roughly 1/3 NSRF funds, 1/3 toll income and 1/3 private (bank loans and contractor's capital). The government is in negotiations to revise existing contracts in order to ensure the financial viability of the projects. Liquidity problems though will not be solved until the fate of the recapitalization of Greek banks and the disbursement of the pending €31bn installment of the financial aid accompanying the Greek economic adjustment program is decided. The European Commission has proposed the creation of a Risk Sharing Instrument (RSI) that will provide capital provisioning to the European Investment Bank (EIB) to enable it to provide loans or

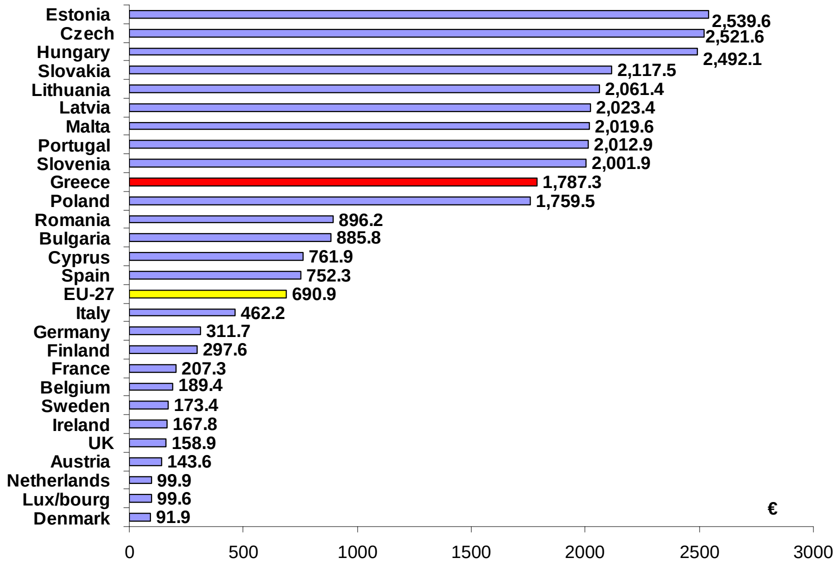
[9] For more details see previous issues of Greece Macro Monitor: December 2011 and March 2010

Graph 2
Structural funds allocated per member state
(€ bn)



Note: ETC stands for European Territorial Cooperation and finances a number of cross border and transnational programs. Total EU structural funding is €346.7bn or 0.4% of 2007-2013 EU-27 GDP.
Source: EU Commission

Graph 3
Structural funds allocated per member state
(€ per capita)



Source: EU Commission

guarantees as well as other financial facilities for important projects, particularly highway concessions, urban transport, energy, waste management and railways projects. An initial agreement for the creation of the RSI was reached between the Greek government and the EIB in July.

The future of EU structural funds: 2014 – 2020

Greece has been allocated[10] €20.2bn of EU structural funds for the period 2007-2013. This is the 8th largest amount (Graph 2) and the 10th largest per capita amount (Graph 3) allocated among the 27 EU member states. The accession of 12 new member states in 2004 and 2007 meant that Greece received less money per capita than in the previous programming period 2000 – 2006, since structural and cohesion funds were channeled to the new poorer regions. Still, Greece received higher per capita funding than three new member states, also being the second highest among the old 15 member states, lagging behind only Portugal.

2012 is a critical year for the negotiations for the Multiannual Financial Framework 2014-2020, involving the European Commission (EC), the Member States and the European Parliament. Part of the negotiations is the structural and cohesion funding for 2014-2020. The goal is to reach a final agreement by the end of the year. An extraordinary European Summit will take place in November, solely focusing on the MFF 2014-2020.

The Commission made a proposal in June 2011 to allocate a total of €1.25tn for spending in agricultural subsidies, cohesion policy external aid and research. There were strong reactions though from some member states calling for a smaller budget. From the €1.25tn, €376bn was earmarked for cohesion policy projects and €387bn for the Common Agricultural Policy and rural development projects.

€336bn for structural funding will be allocated to member states' regions according to their income level. €231bn or 68.7% of total funds will be allocated to less developed regions (convergence regions) with GDP per capita below 75% of the EU-27 average. €39bn or 11.6% of total funds will be allocated to transition regions with GDP per capita between 75% and 90% of the EU-27 average. €53bn or 15.8% of total funds will be allocated to more developed regions (competitiveness regions) with GDP per capita above 90% of the EU-27 average. €40bn will be allocated for the Connecting Europe facility – mainly transportation and ICT projects.

The EU authorities will use in their calculations for the allocation of funds, an average GDP of the last three years for which data will be available. According to the latest information, data for the period 2007 – 2009 will be used for GDP at the regional level. That poses a huge risk for Greece, because under these rules the effects of the ongoing crisis on these figures will not be taken into account. Greece is in the fifth year of a recession that started in 2008. The biggest losses in GDP per capita occurred after 2009.

Using the available data for regional GDP per capita, that cover the period 2006-2008, we find that from the 12 Greek

[10] Excluding Cross-border Cooperation Programs.

regions only 2 would be classified in the less developed regions – Epirus and Western Greece. 6 regions – Central and Western Macedonia, Thessaly, Peloponnese, North Aegean and the Ionian Sea – would be classified as transition regions and 4 would classify as more developed regions – Attica, Mainland Greece, South Aegean and Crete. More developed regions will receive limited funding and only for projects improving competitiveness, renewable energy sources, SMEs and innovation.

Under these conditions Greece is expected to receive much less funding than under the NSRF. A rough estimate, based on the initial EC proposal, would be around €12bn, much less compared with the €20.4bn available under the NSRF.

Research Team

Editor, Professor **Gikas Hardouvelis**
Chief Economist & Director of Research Eurobank Group

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 Gioulbaxiotis, Head of International Sales
George Petrogiannis, Head of Shipping 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 20 Amalias Av & 5 Souri Str, 10557 Athens, tel: +30.210.333 .7365, fax: +30.210.333.7687, contact email: Research@eurobank.gr