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4th Programme Review
Agenda & progress made in meeting agreed targets

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Heads of troika missions to arrive in Athens next week for the 4th programme review
A technical team of troika officials arrived in Athens earlier this week to prepare the ground for the upcoming discussions with Greek authorities in the context of the 4th adjustment programme review. The heads of the EC/ECB/IMF mission are reportedly expected to arrive on June 11 and, according to the current plan, they will stay in Athens for a couple of weeks. As per a number of press reports, the issues expected to dominate the agenda include, among others; (i) the progress made so far in public administration reform; (ii) observance of the agreed privatization targets; (iii) the size of a possible government borrowing gap in 2015-2016; (iv) the domestic bank recapitalization programme; (v) a review of the current framework of indirect taxes; and (vi) progress towards removing restrictions to the access and exercise of regulated professions.

Key issues to dominate the agenda in the upcoming discussions with the troika
In what follows, we provide a more detailed analysis of the key issues to be reportedly discussed between the government and the troika in the context of the 4th programme review.

I. Progress in public administration reform

According to the local press, the Greek Ministry of Administrative Reform and E-Governance has to report the progress made so far in fulfilling the following agreed prior actions:

i) Transfer to the *so-called* mobility scheme of 12.5k public employees by June 2013 and 25k cumulatively by the end of 2013. Under the said scheme, transferred civil servants will be receiving 75% of their basic monthly salary for a year before being subject to permanent separation, in case they fail to be reappointed in the broader public sector to fill in vacant positions. This is part of a broader commitment to reduce public sector employment by 150k over the period 2010-2015. According to official data, the overall public sector workforce is falling faster than expected earlier, mainly thanks to natural attrition, early retirements, the non-renewal of fixed-term contracts and the application of a 1:5 (and, in some cases, 1:10) hiring rule in the broader public sector. Specifically, total public sector workforce stood at around 668k in late 2012, having declined by ca 80k in the past 1½ year.

ii) Mandatory exit of 2k public employees by end Q3 2013 (and 4k by the end of the current year), so as to create the space needed for the hiring of new staff, particular young and highly qualified in several priority areas, *e.g.* tax administration, where half of the staff (estimated at about 14k) is over the age of 50 and a quarter over 55. An addition 11k will have to be removed by the end of 2014. Each dismissed employee will be replaced by a new recruit, through a totally meritotacratic process. As laid out in the updated MoU, the 1:1 hiring rate will have to be reduced in due course, should it risk violating the agreed target for a 150k reduction in the public sector workforce in the period 2010-2015. For all other exits (*e.g.* via natural attrition), the hiring ratio will remain 1:5, as envisioned in the current programme. As agreed with official lenders in the context of the 3rd programme review, mandatory exits will mainly come from the following pools:

- public employees transferred to the mobility scheme who fail to be reappointed after the expiration of the 12-month period;
- public employees who are found guilty of breaching the code of conduct, upon completion of legal procedures. According to local press, in the period between July 2012 and March 2013, only 99 perjurer employees have been removed, while criminal charges against another 2,127 civil servants are currently under investigation;
- merged and closed-down public organizations and private-law legal entities resulting in redundant positions. The first list of state bodies that are to be merged and/or abolished was made public earlier this month, featuring 17 public organizations and 46 public libraries, research centers and academies, employing a total of 416 staff. Out of these employees, at least 216 are reportedly expected to join the list of the 2k planned layoffs for Q3 2013. Selection of other state organizations that will merge or close-down to provide the main bulk of mandatory exits, will reportedly dominate the agenda of the upcoming official discussions;
- employees who will score poorly in upcoming evaluation tests (expected be completed by end-2013);
- voluntary early retirements of public employees (excluding public employees who are within up to three years of retirement);
- employees who have been appointed with false documentation or/and have been unjustifiably absent from their work for a protracted period of time.

Looking further ahead, as a prior action to the 5th programme review, the Greek side will have to provide completed staffing plans involving cumulatively 450k employees (including those employed in decentralized entities supervised by the line ministries). Staffing plans for the broader public sector will need to be completed by the end of the current year.

II. Observance of the agreed privatization targets

- As per the latest European Commission report on Greece[1], significant efforts have been made in recent months in preparing assets for privatization. More specifically: (i) 3,150 real estate properties have been preselected and pre-valued by the Hellenic Republic Asset Development Fund (TAIPED) in order to provide the basis for sales over the next 2-3 years; and (ii) preparatory steps have already been taken for the transfer of 1,000 commercially-viable real estate assets to the by the end of 2013, targeting 250 transfers per quarter to the Greek privatization agency. The first cluster of ca 290 real estate assets is reportedly expected to be transferred to TAIPED portfolio by end-June 2013, including among others, the Peace and Friendship Stadium in Piraeus, real estate assets in Attica, the old royal estate at Tatoi, the Prasonis island near Rhodes and a ski center in Macedonia.

- Yet, the overall speed of the privatization process is considered as being far from satisfactory, due to a multitude of implementation hurdles, including among others, serious administrative, bureaucratic and legal complexities. To this end, authorities have committed to develop a plan aiming to transfer gradually to TAIPED all preselected for exploitation real estate assets that are currently under the management of line ministries and the Public Properties Company (some 80k pieces). A final report is expected by December 2013, while the first progress report is due by end-June 2013 (prior action for the 5th programme review).

[1]European Commission, Occasional Papers 148/May 2013, "The Second Economic Adjustment Programme for Greece, Second Review- May 2013", http://ec.europa.eu/67F3A53E-736D-4AC5-942B-671589E6142F/FinalDownload/DownloadId-68AC4B418945651CFD5241DEE943B4FD/67F3A53E-736D-4AC5-942B 671589E6142F/economy_finance/publications/occasional_paper/2013/pdf/ocp148_en.pdf

- In the latest European Commission report, expected privatization proceeds over the period 2013-2020 were left unchanged compared to these envisaged in the previous review. Cumulative proceeds expected by the end of this year remained at €2.6bn (excluding ca €1.6bn generated over the period June 2011-December 2012), €4.5bn by end-2014, €6.5bn by end-2015, €8.5bn by 2016 and €22bn by 2020 with the main bulk expected to be raised from concession contracts on public sector property. The earlier-envisaged amount of €50bn in privatization revenue remains valid, though, it is now expected to take longer than initially expected to be realized. Privatization proceeds are paid directly to a special segregated account held in the Bank of Greece. Disbursements to this account cannot be used for any other purposes than debt servicing to official creditors (law 4063/2012).

- In case of a shortfall in privatization proceeds (relative to programme targets) for two consecutive quarters, the pace of the fiscal adjustment will need to accelerate. That is, in case no other adjustments are agreed with official lenders- According to the agreed *fiscal policy reaction mechanism*, the primary surplus target would need to be raised by an amount equivalent to 50% of the shortfall in proceeds and the required incremental adjustment will have to be achieved via additional expenditure cuts. The adjustment within any year will be capped at €1bn.

- Repeated postponements and sluggishness in the licensing progress and in the approval of contracts have altered the implementation timetable of several privatization projects this year. Against this background, local press suggested that the privatization revenue target for this year may be revised lower in the context of the 4th programme review (to ca €2bn from €2.6bn, currently). According to TAIPED's Q1 economic report released earlier this month, privatization proceeds stood at just €60mn, generated from the concession of the International Broadcasting Center (IBC) to Lamda Development last summer. Fuelling market concerns that the FY-2013 private revenue target may be underperformed, TAIPED has penciled additional revenues of just €41mn by end-June, from the sale of four State properties abroad (London, Nicosia, Brussels and Belgrade), provided that the related contracts will be approved on time.

- One of the most important projects of the entire privatization programme was completed in May with the sale of the 33% stake in gambling company OPAP (Hellenic Football Prognostics Organisation) to Emma Delta Fund. The Fund will pay €652mn for the stale and an addition €60mn in 2012 dividends (the latter amount will be paid in three installments over a 30-year period). Yet, the State is not expected to receive any receipts from this sale before the completion of a review by Greece's Court of Auditors. That said, the successful and timely completion of the privatization of DEPA (Public Gas Corporation)//DESFA (National Natural Gas Transmission Network Operator) is highly important for this year's programme. According to TAPED, the deadline for submitting binding offers has been pushed back to June 7 (from early April envisaged initially), with the winning bids expected to be chosen in early summer. So far, the gas companies have drawn interest from five investors but it remains unclear how many of them will submit final offers. DEPA planned sell-off is reportedly expected to yield ca €1bn an amount equal to ca 40% of the projected privatization proceeds for FY-2013.

III. Projected government funding gap in 2015-2016

- The size of an expected borrowing gap in general government finances over the period 2015-2016 will be high in the agenda of official discussions. As per the revised MoU, concrete measures for bridging the gap will need to be identified during the 5th programme review (August 2013). By that time, new macroeconomic data will provide a clearer view about the pace of this year's GDP contraction as well as the progress made in key structural reform targets, including tax administration and the privatization programme. According to the revised MoU, the general government primary account targets a balanced position in 2013 and the generation of a 4.5%-of-GDP surplus in 2016, following a gradual pace of improvement (to the tune of 1.5ppts-of-GDP/annum) over the period 2013-2016. As per the latest European Commission report on Greece, the general government borrowing gaps are currently estimated at about 1.7%-of-GDP in 2015 and 2.1%-of-GDP in 2016, based on the new baseline macroeconomic scenario. Reacting to this announcement, Greek Minister of Finance Yiannis Stournaras insisted that the fiscal gap for 2015-2016 will be contained to ca €4bn and will likely be covered by the improved fiscal performance in 2013-2014, rather than through new fiscal measures. The latest Greek FInMin data on the execution of the State Budget in January-April 2013 revealed a primary deficit of €306mn compared to a targeted shortfall of €3,613mn and a deficit of €1,729mn recorded in the same period of last year. For the year 2013 as a whole, we expect a small primary surplus, while we deem the 4.5%-of-GDP surplus target by 2016 as perfectly attainable, judging from past experience and the extent of the fiscal effort currently underway. Note that in the seven-year period (1994-2000) ahead of the country's entry to the euro area, the general government primary balance recorded an average annual primary surplus of 3.6%-of-GDP.

IV. Domestic bank recapitalization

- **Alpha Bank** was the first out of the four systemic domestic banks confirming earlier this week the completion of its recapitalization process. In an official statement, the bank said that it succeeded to secure 12% of private investment in the capital increase process, outperforming the minimum requirement of 10%. In more detail, out of a total recapitalization need of €4,571mn[2], 10% of the issue was raised through existing shareholders and €92.9mn through a private placement to institutional and other private investors (2% of issue). The remaining €4,020mn will be covered by the HFSF in exchange for new shares with restrictive voting rights.[3] With private investors covering 12% of the common equity capital increase, 7.33 warrants will be issued for each common share, enabling private investors to purchase the remaining common shares from the HFSF at a future time. As per the bank recap terms, warrants may be exercised every six months; the exercise period commences six months post their issue date and spans over the subsequent 54 months. Post recapitalization, Alpha Bank's Core Tier 1 ratio was boosted at 13.7%, well above the BoG's 9% threshold, applied as of end-March 2013.

- The recapitalization scheme for **National Bank of Greece** has entered its final stage. According to an official announcement, the bank will aim to secure 12% (or €1,170mn) of its total recap need of €9,756mn via private participation. This is planned to be achieved through a 2.2:1 rights issue at €4.29 per share following the completion of a 1:10 share reverse split. The remaining amount ca €8,586mn will be covered by the HFSF. Should the target of 12% be attained, the bank will not have to resort to the issue of convertible bonds CoCos[4]. The trading period of rights will take place between May 30 and June 7 and the exercise period ends on June 13 while the new shares are expected to begin trading on June 25.

- **Piraeus Bank's** recapitalization program is also nearing completion. The bank's total capital needs stand at €8,429mn, taking into account the €1,04 capital increase covered by the HFSF following the acquisitions of the good part of ATE and the Greek operations of 3 Cypriot banks (€570mn and €524mn, respectively). With regards to the remaining €7,335mn capital need, the bank has decided some €400mn to be offered via a private placement, leaving €6,935mn to be covered through a rights issue to existing shareholders. Given that the bank has already secured total strategic investment of €570mn (€400mn from Millennium BCP and €170mn from Societé General), the actual amount required from private investors stands at €163mn. In practice, Piraeus Bank will try to tap the market and secure the 10% required threshold for private participation, thus avoiding issuance of convertible bonds (Cocos). Rights will trade from June 11 to June 18 and the subscription period for the offering will run from June 11- 25 ahead of the official announcement of bank recap results on June 28. As per the current timetable, new shares and associated warrants are expected to begin trading on July 4.

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[2]As per the BoG exercise "*Report on the Recapitalisation and Restructuring of the Greek Banking Sector*" published in December 2012, the capital needs for the four biggest domestic lenders were estimated at €27.5bn with the following allocation: National Bank of Greece: 9,756mn; Eurobank: €5,839mn; Alfa Bank: €4,571mn; and Piraeus Bank: €7,335mn.

[3] Under a ministerial cabinet act issued in early November 2012, Greek banks should meet a Core Tier 1 capital ratio of at least 6% through the *exclusive* issue of common shares. Private shareholders will be required to cover at least 10% of new common equity capital so as to keep credit institutions privately run. Should this be the case, the remaining 90% will be covered through the issue of common shares to the Hellenic Financial Stability Fund (HFSF) with restrictive voting rights. Yet, should the Fund's participation exceeds 90% of the common equity capital increase, the HFSF shares will carry full voting rights.

[4]According to the bank recapitalization terms, contingent convertibles will bear an annual coupon of 7% plus a 50bps step-up per year. The said interest has to be paid in cash on an annual basis, provided that capital adequacy requirements are fulfilled. Yet, interest payment could be paid via the issue of common shares in case that a cash payment would result in a fall of the Core Tier 1 ratio below the minimum acceptable threshold. Common shares would then be issued at a price equal to the 50% of the bank stock weighed average price over the 50 trading days preceding the interest payment.

- **Eurobank** became the first systemic fully-recapitalized Greek bank after its Board decided in late April the €5.8bn capital requirement to be fully subscribed by the HFSF. In an official statement issued by Eurobank's Board of Directors, the reasons behind its decision included: (i) uncertainty regarding the completion or not of its merger with National Bank of Greece (NBG) and the ensuing inability of properly assessing the relevant investment proposal; and (ii) the absence of tens of thousands of Eurobank's traditional shareholders who were substituted - through the recent Voluntary Tender Offer -by NBG's stake of approximately 85% in the bank's capital. Based on this decision, Eurobank announced that it intends to actively engage in the strategic restructuring of the Greek banking system through the integration of smaller non-systemic banks. Furthermore, if the relevant authorities finally decide not to conclude the merger with NBG, Eurobank will submit, as required, a comprehensive business plan aiming to attract private and institutional investors from Greece and abroad as soon as possible, according to the provisions of the current legal framework. The objective will be to further enhance the bank's capital, align the bank to the new circumstances and requirements of the domestic and international markets, as well as preserve and increase corporate value to the benefit of the Greek economy.

- Regarding non-core banks, Emporiki Bank has already been absorbed by Alpha Bank. Geniki Bank, ATEbank and Millennium have been acquired by Piraeus Bank, while the so-called *good part* of First Business Bank (FBB) has been absorbed by National Bank of Greece. As regards New Proton bank, the HEFSF is currently taking actions to make major reductions in its operating costs, with the objective of making it attractive to potential buyers and concluding its sale by July 15, 2013 (structural benchmark). Concerning Hellenic Post Bank, following the bank's resolution in July 2012, the deadline for the sale of its good part has been shifted from May to July 15, 2013. The remaining non-core banks, Attica Bank, Probank and Panellinia Bank need to secure their capital requirement fully from private sources and their capitalization programme has to be completed by June 24, 2013. According to the revised MoU, for those non-core banks that will not finally meet the capital requirements, the BoG in coordination with the HFSF will assess by end-June 2013 alternatives aimed at minimizing the cost to taxpayers, including Purchase and Assumption transactions (P&A) by any of the four systemic banks, while guaranteeing the security of depositors.

- Upon completion of the domestic banking system's recapitalization and restructuring programme, Greek authorities in cooperation with the EC/ECB/IMF staff will prepare by mid-July 2013 a comprehensive banking sector strategy (structural benchmark) addressing, among others, options and operating steps for the HFSF to prompty proceed with the disposal to the private sector the shares of the core banks that will not be able to remain under private control. Only upon completion of the banking sector strategy, any consolidation in the form of possible further mergers among the four systemic banks may be considered. In the meantime, all four pillar banks will be able to continue to act as integrators of smaller domestic banks. Moreover, Greek authorities, in coordination with the troika staff, will have to finalise by end-July 2013 a stress testing methodology for the domestic banking system, with the relevant stress tests to be completed by the end of this year.

V. Review of the current framework of indirect taxes

- According to the latest European Commission report, the Greek government's proposal for a reduction in the VAT rate for restaurants and catering will be reassessed in the context of the 4th programme review. The proposed VAT rate reduction (to 13% from 23%, currently) was rejected by the troika during the previous round of official discussion amid worries that it could jeopardize the agreed fiscal targets. As per a study published recently by the Association of Hellenic Tourism Enterprises (SETE), the VAT hike has led to a 40% drop in the sector's turnover over the period 2011-2012, while some 40k enterprises have closed down and more than 30k jobs have been lost. Yet, the issue is reportedly likely to meet again strong resistance from the troika. As per the last IMF report on Greece[5], easing some of the currently applied adjustment measures (including VAT on restaurant) would entail the risk of creating a significant fiscal shortfall, especially in view of lingering uncertainty over the effectiveness of tax administration reforms.

[5] IMF Country Report No. 13/153, "Greece: Third Reviews Under the Extended Arrangement Under the Extended Fund Facility —Staff Report; Staff Supplement; Press Release; and Statement by the Executive Director for Greece", June 2013

- In relation to the aforementioned, note that the latest Greek FinMin data on the execution of the State budget on a modified cash basis showed that central government net revenues in the period January-April 2013 amounted to €15,743mn, 5.3% or €786mn higher than the corresponding target. This was mainly thanks to higher than expected receipts from personal income tax and property taxation, which exceeded monthly targets by €54mn and €69mn respectively. Yet, revenues from VAT and consumption taxes came in short of monthly targets by €265mn and €325mn, respectively.

VI. Progress in removing restrictions to the access and exercise of regulated professions

- Greece has already undertaken a number of steps towards removing restrictions on entry, minimum prices and mandatory use for a number of regulated professions and economic activities (e.g. bake-off installations, welfare units, outdoor trading and tourist guides). However, some key professions/activities (e.g. engineering and lawyers) have yet to be fully liberalized. Aiming to address this issue, the Greek government has committed under the current programme to, among others, adopt a new Code of Lawyers by end-June 2013 and remove restrictions for the engineering professions by the end of this year. Moreover, a study of the 20 economically most-important professions has to be completed by end-July 2013. The study will assess the degree to which they have been liberalized and address any remaining restrictions. According to recent comments by the Greek Finance Minister, some 247 regulated professions (out of a total of 343) have already been liberalized.

June 13, 2013 Euro Working Group expected to approve release of the next EFSF loan tranche to Greece

The Euro Working Group is broadly expected to approve on June 13 the release of the next EFSF loan tranche to Greece (€3.3bn), provided that the Greek side will proceed with the timely implementation of the agreed prior actions:

(i) appointment of a national coordinator for anti-corruption, a coordination committee and its chairman, an advisory committee and eight staff members provided for by the law;
(ii) authorities to present to the EU Commission Services for consultation a detailed action plan with identified time bound steps for the restructuring of PPC with a view to prepare the company for privatization and thus to establish the required conditions for a liberalized electricity market; and
(iii) facilitate the resolution of unsustainable household debt by passing legislation to parliament introducing; (a) a new "Facilitation programme" for heavily indebted households and; (b) revising law 3869/10 (budded as Katseli law) to address the implementation shortfalls identified during its first three years of enactment.

As a reminder, the May 13, 2013 Eurogroup gave the green light for the release of €7.5bn in new EFSF funding to Greece, following the successful completion of the 3rd programme review. (*Table 1* in the Annex section depicts the full (revised) schedule of troika loans to Greece under the present adjusted programme). Note that the first sub-tranche (€4.2bn) of the €7.5bn EFSF loan installment arrived in State coffers on May 17, following the parliamentary endorsement of a multi-bill for the legislation of a number of prior actions. The release of the 2nd sub-tranche is scheduled for June, upon completion of all required MoU milestones. On its part, the IMF Board met on May 31 and decided to release its contribution (€1.8bn) to the loan tranche scheduled for Q2 2013. So far, the total amount of official loans to Greece disbursed under both the 1st and the 2nd bailout programmes is €205.1bn (*Table 2* in Annex).

Annex

Table 1- Programme of EFSF/IMF official assistance disbursments under the 2nd bailout programme (2012-2014)

(in € bn)	2012				2013				2014				(Total)
	Q1*	Q2	Q3	Q4**	Q1***	Q2	Q3	Q4	Q1	Q2	Q3	Q4	
EFSF disburmsents	40.4	33.6	0.0	34.3	12.0	10.3	3.0	2.6	5.7	2.9	0.0	0.0	***144.8***
IMF disburmsents	1.65	0	0	0	3.3	1.8	1.8	1.8	3.5	1.8	1.8	1.8	***19.1***
Source: European Commission (May 2013)													***163.9***

(*) including the 1st tranche for the domestic bank recapitalization program (€25bn)
(**) including part of the 2nd (and final) installment for the domestic bank recapitalization program (€16bn)
(***) including part of the 2nd (and final) installment for the domestic bank recapitalization program (€7.2bn)

Table 2- Disbursements alerady made under the Greek adjustment programmes (EUR bn)

1st programme		**Euro-area Member States**		**IMF**		**Total**
1st disbursement		18 May 2010	14.5	20 May 2010	5.5	20.0
2nd disbursement		13 September 2010	6.5	14 September 2010	2.5	9.0
3rd disbursement		19 January 2011	6.5	21 December 2010	2.5	9.0
4th disbursement		16 March 2011	10.9	16 March 2011	4.1	15.0
5th disbursement		15 July 2011	8.7	13 July 2011	3.3	12.0
6th disbursement		14 December 2011	5.8	7 December 2011	2.2	8.0
1st programme- Total disbursments			**52.9**		**20.1**	**73.0**
2nd programme		**EFSF**		**IMF**		
1st disbursement	1st tranche	12 March, 10 April, 25 April 2012	29.7	19 March 2012	1.6	
	2nd tranche	12 March, 10 April, 25 April 2012	4.9			
	3rd tranche	19 March 2012	5.9			
	4th tranche	10 April 2012	3.3			
	5th tranche	19 April 2012	25.0			
	6th tranche	10 May 2012	4.2			
	7th tranche	28 June 2012	1.0			
2nd disbursement	1st tranche	20-Dec-2012	34.3			
	2nd tranche	31-Jan-2013	9.2	16 January 2013	3.24	
	3rd tranche	28 February 2013	2.8			
	4th tranche	3 May 2013	2.8			
3rd disbursement	1st tranche	17 May 2013	4.2			
2nd programme- Total disbursements			**127.3**		**4.84**	**132.14**
1st & 2nd programme -Total Disbursements already released till mid-May 2013 (EUR bn)			**180.2**		**24.94**	**205.1**
Scheduled EFSF/IMF loan disbursements yet to be released under the 2nd programme, upon fulfillment of related MoU milestones						
		EFSF		**IMF**		
		3rd disbursement, 2nd tranche	3.3	Q2 2013	1.8	
		Q3 2013	3.0	Q3 2013	1.8	
		Q4 2013	2.6	Q4 2013	1.8	
		Q1 2014	5.7	Q1 2014	3.5	
		Q2 2014	2.9	Q2 2014	1.8	
				Q3 2014	1.8	
				Q4 2014	1.8	
				Q1 2015	1.8	
				Q2 2015	1.8	
				Q3 2015	1.8	
				Q4 2015	1.8	
				Q1 2016	1.8	
Total EFSF/IMF loan disbursements yet to be released under the 2nd programme			***17.5***		***23.1***	***0.0***
Total EFSF/IMF loan disbursements agreed under the 2nd Greek adjustment programm			***144.8***		***27.9***	***172.7***
Source: European Commission (May 2013), Eurobank Research						

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