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Focus notes: Greece

Latest macro & market developments

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Joint EC/ECB/IMF mission to Greece concludes 4th programme review

The joint EC/ECB/IMF mission to Greece announced on June 3rd the successful conclusion of the 4th Review of the country's existing EU/IMF-financed adjustment programme. In a statement released late on Friday, official lenders noted that significant progress was made so far in implementing the programme, but a reinvigoration of fiscal and broader structural reforms is required to further reduce the deficit and achieve the critical mass of reforms needed to improve the business climate and pave the way for sustainable economic recovery. The positive conclusion of the 4th Review effectively opens the door for the disbursement of the 5th tranche of the existing EU/IMF loan, most likely by early July 2011.

Speculation mounts over a new rescue package for Greece

The European Economic and Financial

Committee of deputy ministers and senior officials has reportedly agreed in principle to a new support package for Greece, which will run till mid-2014, a year after the existing EU/IMF support scheme expires. According to a number of press reports, the new aid package would total €85bn, an amount that is deemed adequate to fully cover the country's borrowing requirement for the following two years, assuming that Greece will not probably be able to access international markets until 2013.

According to a number of reports circulated in the local and international press over the last couple of days, the new aid package for Greece will come in the form of:

- i) ca €40-45bn in new bilateral loans from other EU States or in the form of funding from the European Financial Stability Facility (EFSF)
- ii) €25bn from Greece's privatization and real estate development programme. According to an outline of the

government's Medium-Term Fiscal Strategy (MTFS) released last month, projected revenues from privatizations and the better utilization of state assets have been revised upwards to between €4.0-€6.0bn in 2012 and €4.5-€5.5bn in 2013, following expected receipts of €3.5-€5.5bn this year.

- iii) €20bn via the voluntary rollover of private sector exposures *i.e.*, some sort of a Vienna-style initiative. Reportedly, the new plan will involve participation of private sector bondholders, albeit in a limited way so as to avoid the risk of triggering a "credit event".

With respect to the later, a number of press leaks suggest that private creditors would be encouraged to roll their holdings of Greek sovereign paper maturing between 2012 and 2014 with new 10-15 year bonds. To facilitate the process, the government could reportedly provide some form of sweeteners, so as to enhance the appeal of the new instruments. According to a Bloomberg report (June 1st) quoting unnamed official sources this could be achieved via offering preferred status, higher coupon payments or collateral as inducements to buy the new bonds. The ECB could also lower the attractiveness of the old debt instruments by no longer accepting them as collateral in its refinancing operations, *though it remains unclear to us whether this (or any of the alternatives noted above) would indeed qualify as a no credit event-triggering scheme.*

While the ECB remains adamant against an outright restructuring of Greek debt, a number of central bank officials have lately indicated that they are open to a Vienna-type arrangement, provided that this would not trigger a credit event. Among them, ECB Executive Board member Jose Manuel-Gonzalez-Paramo said recently that a voluntary debt rollover agreement for Greece could be "positive", even as it would only be part of the solution to the country's fiscal problems. Furthermore, the prevailing political mood in a number of core Eurozone countries, including Germany, Netherlands and Finland, is such that some form of private sector involvement is deemed necessary for national parliaments to agree on a new rescue package for Greece.

The Vienna Initiative was launched in January 2009, at the height of the financial crisis triggered by the collapse of investment bank Lehman Brothers. It took the form of a "gentlemen's agreement" between the ECB, the European Bank for Reconstruction and Development, the IMF, regulators and

banks with subsidies in Central and Eastern Europe. Under the plan, parent bank groups were publicly committed to maintain their earlier exposures in a number of CESEE countries – including, among others, Hungary, Latvia and Romania – and recapitalize their subsidiaries so as to secure continued financing from the official lenders.

New official funding to come with strict conditionality

Reportedly, the new rescue plan will come with stricter conditionality that would likely involve a closer monitoring of reforms implementation as well as more austerity measures and an ambitious privatisation plan as laid out in the country's soon-to-be-unveiled Medium-Term Fiscal Strategy. The latter was presented by Greek Prime Minister George Papandreou to Eurogroup President Jean-Claude Juncker on Friday and includes **i)** additional fiscal measures worth €6.4bn (~2.8%-of-GDP), aiming to ensure fulfillment of this year's 7.5%-of-GDP fiscal deficit target, **ii)** a further €22bn of fiscal measures for 2012-2015, aiming to eliminate the excessive deficit and facilitate the generation of primary surpluses from 2012 and **iii)** an ambitious privatization and state assets management programme, aiming to generate additional revenues of €15bn until 2013 and a total of €50bn by 2015. Reportedly, the programme of privatization will be subject to strict rules regarding the timetables set and the composition of the board of a sovereign wealth agency that will manage the state-asset sales.

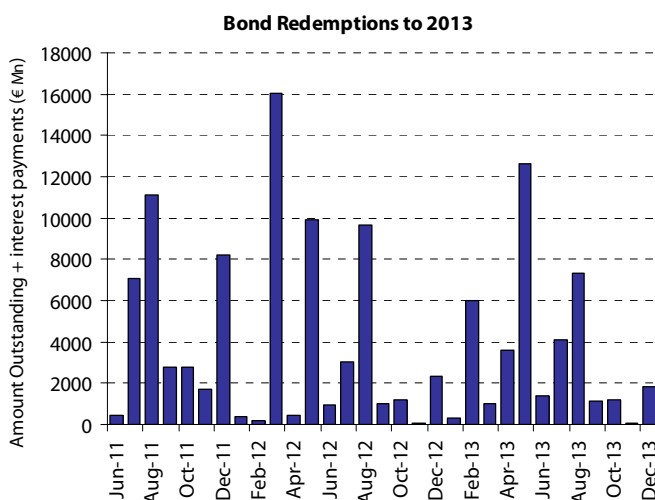
Reportedly, a more challenging precondition to a second EU/IMF aid package for Greece is a broader political consensus for the new austerity measures and the privatization programme. Greek Prime Minister George Papandreou failed last week to win cross-party agreement. The leader of the main conservative opposition New Democracy party, Antonis Samaras who is not in principle opposed the 2011-2015 privatization programme, refused to back the new fiscal measures. Instead, the leader of the main opposition demanded lower taxes to help the economy rebound and called for the renegotiation of the EU/IMF bailout terms. However, Prime Minister, George Papandreou, highlighted earlier this week that the government will continue its efforts to reach a form of consensus, raising hopes that a deal will be finally sealed. Adding to hopes for a broader political consensus, an unnamed official in Germany's ruling coalition claimed this week that the joint team of EU/IMF/ECB inspectors who just completed the country's fourth programme review, agreed to a three pps reduction in VAT rates applied to the retail prices of a number of goods and services, though no official conformation on the latter has been provided yet.

Estimating the government's financing gap in 2012-2013

The March 2011 update of the EU/IMF programme envisioned that Greece would be able to return to the international capital markets by Q1 2012, a scenario that seems increasingly unlikely by now. Back then, official lenders estimated the government's gross borrowing requirement at €66.6bn in 2012 and €60.9bn for 2013. Out of these amounts, €32bn would be covered by EU/IMF bilateral loans under the existing financial support scheme (€24bn in 2012 plus €8bn in 2013). An additional amount of €6bn would need to be raised via privatization; €3bn in each of the next two years.

The remaining amounts required to cover fully the 2012-2013 borrowing needs (~€40.3bn and ~€51.5bn respectively) were projected to be raised via the issuance of government securities; short-term T-bill sales (€27.2bn cumulatively for both years) and medium- and longer-term notes and bonds (€64.6bn in total for the two years). But again, with Greek borrowing rates remaining in a steep upward trend, access to international bond markets as soon as early next year, is increasingly doubtful. Consequently, unless domestic macro and market conditions improve markedly in the coming months, the present EU/IMF funding programme – due for expiration end Q2-2013 – will probably run into a cumulative funding gap of ca €65bn in the course of 2012-2013. (The latter will reportedly be bridged by a new EU/IMF aid package for Greece, the rumored components of which are presented in the first paragraph of this report).

The graph below exhibits Greece's monthly redemption payments, including interest payments, until end 2013; the next hurdle in terms of debt repayments is August 2011 when the 3.9% August 2011 redeems for €6,61bn.



Counting down to a new bailout plan

The next major steps that need to be taken before an agreement on a new rescue package for Greece is sealed include:

- i) The privatization programme as well as the additional fiscal tightening measures for 2011 and the period 2012-2015 (Medium-Term Fiscal Strategy) need to be submitted and approved by parliament. Reportedly, the medium-term plan will be submitted within the next 10 days as one article rather than in an article-by-article form in order to speed up the voting process. No specific parliament vote date has been announced yet, but this should be ahead of the next EU Council on June 23/24. Even in the absence of a cross-party agreement, the government would still likely be able to push the new austerity measures through parliament on the back of its six-seat majority.
- ii) Eurozone finance ministers need to express their support to Greece's medium-term fiscal plan at their upcoming meeting on June 20 (pushed back from June 13, scheduled initially) and underline the main axes of a new aid program that will aim to help cover Greece's 2012/2013 expected funding shortfall. The 23/24 June EU Council would then need to endorse the agreement struck by the Eurozone finance ministers. In addition, the EU Council agenda is also expected to include i) an endorsement of the March 11 EU Council meeting agreement on improved EU loan terms for Greece and ii) the finalization of the EFM reforms, including a) the extension of its power to exceptionally intervene in the primary sovereign bond markets and b) the way the additional burden of the enlarged fund -to €440bn from €225bn previously- will be shared among eurozone member states.
- iii) Once an EU commitment is provided with respect to the coverage of Greece's 2012 funding need, the IMF Board will likely approve the release of the Fund's contribution to the 5th fifth tranche (€12bn) of financial assistance to Greece under the existing EU/IMF aid programme. The release date was initially scheduled for June 29, but the last EC/ECB/IMF mission to Greece said that this will be probably delayed to early July. Note that the IMF threatened early last week to withhold its share from the next installment of funds under the €110bn EU/IMF bailout package, worth

€3.3bn, unless the EU guarantees fulfillment of the country's funding needs over a 12-month period ahead. Given IMF internal rules, the Fund cannot continue to disburse programme payments without assurances on a country's funding sources for the next 12 months.

Roadmap to the new deal for Greece

Date	Event
9-Jun	ECB meeting & press conference
13-17-Jun	Greek Parliament to approve the medium-term fiscal plan
20-Jun	Eurogroup meeting
21-Jun	Ecofin meeting
23/24 Jun	Summit of EU heads of state and government in Brussels

Table 1: Medium Term Fiscal Plan - 2011				
	Areas of adjustment	€ bn	% of GDI	Specific Measures
1	Streamlining the Public Wage Bill	0.55	0.2	Reduction in contractual employees Introduction of part time employment Reducing wage drift Increase in working hours from 37.5 to 40 hours per week
2	Reduction in Operational Expenses	0.14	0.1	Reduction in subsidies fir newspaper distribution to remote areas Withholding of 7% of elastic operational expenses
3	Closure/Merger of Public Entities	0.45	0.2	Reduction in grants to entities outside the General Government Evaluation and reduction of spending of entities within the General Government Reduction in subsidies to remote areas Merger and closure of public entities
4	Streamlining of Health and Pharmaceutical Expenses	0.31	0.1	Digitization and monitoring of prescriptions by SSFs Expansion of list of non-prescription drugs that are not paid by SSFs New pricing policy Introduction of a fixed insurance price on pharmaceuticals that is lower than the market price Special agreement for the provision of services by hospitals to private insurance firms
5	Reduction in SSF expenditures and other social spending	0.80	0.4	Cross-checking of details of pensioners and welfare beneficiaries Introduction of tighter criteria for benefits (OAED, OEE-OEK, EKAS) Single unified regulation on the health benefits Increase in solidarity contribution on high pensions Reduction in supplementary pension from Funds running deficits Reduction in lump-sum benefits in the public sector Special contribution for pensioners under 60 years old with high pensions
6	Reducing social contribution evasion and increasing the revenues of Social Security Funds	0.38	0.2	Full implementation of single unified payroll and insurance contribution payment method Solidarity contribution for the unemployed for the public sector Increase in unemployment solidarity contribution for private sector employees and introduction of unemployment solidarity contribution to be made by public sector employees
7	Reduction in Tax Exemptions and other Tax Revenues	0.77	0.3	Increase in tax rates on yachts, pools, luxury vehicles, high-value property, evaluation and reduction of tax exemptions
8	Other Revenue	1.40	0.6	Change in the structure of tax on tobacco special consumption tax on soft drinks vehicle tax transfer of products from the 13% VAT bracket to the 23%
9	Measures that need to be identified	1.60	0.7	
	Total	6.40	2.8	

Source: Ministry of Finance

Table 2: Medium Term Fiscal Plan 2012-2015							
Areas of Adjustment		2012	2013	2014	2015	2012-2015	% GDP
1	Rationalization of the Public Wage Bill	0.57	0.28	0.25	0.10	1.19	0.5
2	Reduction in Operational Expenses	0.33	0.23	0.08	0.57	1.20	0.5
3	Closure/merger of public entities and reduction in grants	0.08	0.12	0.23	0.29	0.71	0.3
4	Restructuring of State-owned Enterprises	0.47	0.36	0.33	0.33	1.50	0.6
5	Reduction in Defence Expenditures	0.10	0.10	0.45	0.55	1.20	0.5
6	Streamlining of Health Expenditures	0.20	0.15	0.15	0.19	0.69	0.3
7	Streamlining of Pharmaceutical Spending	0.49	0.20	0.04	0.00	0.74	0.3
8	Reduction in SSF spending and other social spending	1.08	0.62	0.54	0.40	2.63	1
9	Strengthening Tax Compliance	0.35	0.70	0.80	1.15	3.00	1.2
10	Reduction in Tax Exemptions and other tax revenue	2.26	0.19	0.00	0.00	2.45	1
11	Improved SSF revenues and tackling of social contribution evasion	0.53	0.58	0.64	0.69	2.44	1
12	Increase in revenues of Local Governments	0.11	0.17	0.18	0.15	0.60	0.2
13	Other Expenditures	0.32	0.18	0.17	0.16	0.83	0.3
14	Measures to be identified					2.94	1.1
	Total	6.881	3.866	3.855	4.562	22.105	8.8

Source: Ministry of Finance

Table 3: Projected Transactions in 2011-2015

Year	Estimated Revenues	Firm / Organization / Real Estate / Infrastructure / License	Currently under state control (%)	% to be sold	Method	Current Status	Date of Transaction
2011	€3.5-5.5 bn	Hellenic Telecommunications Organisation	16%	up to 16	Sale of shares	-	Q2 2011
		Hellenic Postbank	34%	upt to 34	Sale of shares	-	Q2-Q4 2011
		Piraeus Port	75%	up to 75	Sale of shares	in process	Q2-Q4 2011
		Thessaloniki Port	75%	up to 75	Sale of shares	in process	Q2-Q4 2011
		Thessaloniki Water Supply and Sewage Company	74%	up to 40	Sale of shares	advisor selection process	Q2-Q4 2011
		Athens International Airport	55%		Extension of concession	in process	Q3 2011
		Hellenic Football Prognostics Organisation	34%		Extension of concession	in process	Q3 2011
		Hellenic Defence Systems (EAS)	100%	up to 66	Sale of shares	in process	Q4 2011
		State Lotteries	100%	49-66	Sale of SPV shares	in process	Q4 2011
		Public Gas Corporation (DEPA)	65%	up to 32	Sale of shares	in process	Q4 2011
		TRAI NOSE	100%	49-100	Sale of shares	advisor selection process	Q4 2011
		LARCO	55%	up to 55	Sale of shares	advisor selection process	Q4 2011
		Hellenic Horse Racing Company (ODIE)	100%	-	Sale of shares	in process	Q4 2011
		Casino Mont Parnes	49%	49%	Sale of shares	advisor selection process	Q4 2011
		Mobile Telephony Licenses	100%	-	Sale of rights	in process	Q4 2011
Hellinikon S.A I	100%	-	Sale of SPV shares	in process	Q4 2011		
Real Estate Investment -Portfolio I	100%	-	Sale of SPV shares	in process	Q4 2011		
2012	€4.0-6.0 bn	Athens International Airport	55%	up to 21	Sale of SPV shares	in process	Q1 2012
		Egnatias Odos Motorway	100%	up to 100	Sale of SPV shares	in process	Q1 2012
		Hellenic Post	90%	up to 40	Sale of shares	advisor selection process	Q1 2012
		Hellenic Football Prognostics Organization	34%	up to 34	Sale of shares	in process	Q1 2012
		Ports-Portfolio I	77-100%	43-66%	Sale of SPV shares	advisor selection process	Q1-Q4 2012
		Athens Water Supply and Sewerage Company (EYDAP)	61%	up to 27	Sale of SPV shares	advisor selection process	Q3 2012
		Hellenic Vehicle Industry S.A. (ELBO)	51%	up to 16	Sale of shares	in process	Q2 2012
		Loan and Consignment Fund	100%	up to 100	Sale of SPV shares	in process	Q2 2012
		Public Power Corporation (DEH)	51%	up to 17	Sale of Shares	-	Q4 2012
		Hellenic Motorways I	100%	-	Sale of SPV shares	-	Q1-Q4 2012
		Regional Airports -Portfolio I	100%	up to 49	Sale of SPV shares	advisor selection process	Q1-Q4 2012
		Hellinikon S.A II	100%	-	Sale of SPV shares	in process	Q1-Q4 2012
Real Estate Investment -Portfolios I and II	100%	-	Sale of SPV shares	in process	Q1-Q4 2012		
Frequency Spectrum -Digital Dividend I	100%	-	-	in process	Q1-Q4 2012		
2013	€4.5-5.5 bn	Participation in Banks (Alpha, Peiraeus, Attiki)		100%	Sale of Shares	-	Q1-Q4 2013
		Agricultural Bank of Greece	76%	up to 25	Sale of Shares	-	Q1-Q4 2013
		Regional Airports -Portfolio II	100%	up to 49	Sale of SPV shares	advisor selection process	Q1-Q4 2013
		Ports-Portfolio I	77-100%	43-66%	Sale of SPV shares	advisor selection process	Q1-Q4 2013
		Real Estate Investment -Portfolio II- III	100%	-	Sale of SPV shares	in process	Q1-Q4 2013
		Hellenic Motorways II	100%	-	-	in process	Q1-Q4 2013
Frequency Spectrum -Digital Dividend I	100%	-	Sale of SPV shares	in process	Q1-Q4 2013		

Source: Ministry of Finance

Table 4: Greece-Key Indicators				
	Last	ytd	2010	2009
Macroeconomic indicators				
GDP growth (%YoY)	-4.8 (Q1 11)	-6.6	-7.4	-2.1
CPI	3.9 (April 11)	1.8	4.7	1.2
Unemployment rate	15.9 (Feb 11)	33.1	14.8	10.2
Labor Cost (%YoY)	-4.2 (Q4 10)	-4.2	-4.2	3.6
Economic Sentiment (index level-period average)	74.0 (May 11)	76.4	75.1	76.3
Consumer-vigor indicators				
Private consumption in constant prices (% YoY)	-8.6 (Q4 10)	-8.6	-8.6	-2.2
Retail sales excl. fuels & lubricants volume (% YoY)	-25.1 (March 11)	-28.2	-23.7	-0.7
New private passenger car registrations (% YoY)	-18.1 (April 11)	176.1	-61.9	22.0
Consumer confidence (index level - period average)	-68.5 (May 11)	-68.8	-63.4	-45.7
Retail trade expectations (index level - period average)	-43.1 (May 11)	-31.2	-33.7	-15.4
Industrial-activity indicators				
Industrial production (% YoY)	-8.1 (March 11)	-0.9	-5.2	-6.8
Capacity utilization in industry (index level - period average rate)	68.0 (Feb 11)	68.4	68.6	70.5
Industrial confidence (index level - period average)	-20.4 (May 11)	-2.4	-22.5	-28.4
Manufacturing PMI (index level - period average)	46.7 (April 11)	44.4	43.8	45.4
Construction sector & other investment-activity indicators				
Cross fixed capital formation in constant prices (% YoY)	-7.6 (Q4 10)	-7.6	-7.6	-15.1
Housing investment in constant prices (% YoY)	-18.5 (Q4 10)	-18.5	-18.5	-23.0
Other construction in constant prices (% YoY)	35.3 (Q4 10)	35.3	35.3	-16.7
Private building permits volume (% YoY)	-31.4 (Nov 10)	-39.9	-	-22.6
Construction confidence (index level - period average)	-64.6 (May 11)	-66.1	-55.4	-39.5
Balance-of-Payments statistics (€-terms)				
Tourism revenues (% YoY)	2.3 (March 11)	4.7	21.0	-10.2
Transportation revenues (% YoY)	-18.7 (March 11)	-9.1	-7.7	-7.9
Customs-based statistics (€ - terms)				
Goods exports (% YoY)	22.8 (March 11)	-4.0	43.8	-3.2
Goods exports to EU (% YoY)	11.2 (March 11)	5.7	17.1	4.2
Goods exports to non-EU countries (% YoY)	43.2 (March 11)	-13.7	89.8	-14.4
Goods imports (% YoY)	-32.9 (March 11)	-12.1	-6.7	1.0
Goods imports from EU (% YoY)	-17.3 (March 11)	4.4	-15.7	-7.8
Goods imports from non-EU countries (% YoY)	-48.4 (March 11)	-21.5	8.0	1.1
Domestic MFI credit to domestic enterprises & households (outstanding balances)				
Private sector (% YoY)	-0.5 (April 11)	-1.6	0.0	1.5
Enterprises (% YoY)	1.2 (April 11)	-1.7	1.1	1.0
Households (% YoY)	-2.2 (April 11)	-1.5	-1.3	1.9
Housing loans (% YoY)	-1.6 (April 11)	-1.0	-0.4	3.7
Consumer credit (% YoY)	-4.9 (April 11)	-2.9	-4.2	-1.6
Private-sector credit outstanding (% GDP) *				
Total domestic enterprises & households	113.9 (April 11)	-	112.0	106.6
Domestic households	52.2 (April 11)	-	51.3	50.2

Source: Hellenic Statistical Authority, Bank of Greece, ECOWIN, AMECO

* AMECO's nominal GDP Spring forecasts for 2010 (€ 230.2 bn) and 2011 (€ 222.8 bn) were used.

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