

# GREECE MACRO MONITOR

November 18, 2011

Focus notes: Greece

## Latest macro & market developments

### Written By:

**Dr. Theodoros Stamatiou**  
Research Economist  
[tstamatiou@eurobank.gr](mailto:tstamatiou@eurobank.gr)

- 2012 budget plan: updated deficit target for 2011 at -9.0% of GDP; 2012 deficit target at -5.4% of GDP after PSI
- Greek GDP Q3:2011 flash estimate: Non-seasonally adjusted real GDP contracted by -5.2%YoY in Q3:2011, higher than the Q2:2011 figure of -7.4%YoY
- Preliminary budget execution data for year-to-October 2011 undershoot the 10-month MTFS target for 2011
- General Government arrears for year-to-September 2011 at €6.49bn or 2.7% of GDP; upwards risk for the 2011 budget deficit target of 8.5% of GDP
- Unemployment rate in August 2011 at 18.4%, higher than July's reading of 16.5%
- CPI rate in October 2011 at 3.0%, slightly lower than September's reading of 3.1%

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### 2012 budget plan: updated deficit target for 2011 at -9.0% of GDP; 2012 deficit target at -5.4% of GDP after PSI

The Greek government unveiled earlier today the 2012 Budget plan as well as the updated 2011 budget. The 2011 budget deficit is expected at -9.0% of GDP higher than the -8.5% announced in early October. The 2011 deficit target was revised upwards because of the larger than expected economic recession as well as the inability of the government to deliver proper results in a series of revenue increasing and cost cutting measures included in the Medium Term Fiscal Plan for 2011-2015 (MTFS) and the additional measures announced in mid September 2011. The 2012 budget deficit is expected at -5.4%-of-GDP, if the new PSI for Greece currently under discussion will be implemented and -6.7%-of-GDP if it is not.

The government expects that the Greek economy will revert to positive GDP growth from 2013 onwards. However, details on the 2013-14 budgets are not available yet.

The 2012 budget has been approved already by the cabinet and submitted to the Parliament. The Parliament is expected to vote for the 2012 budget in the following days (until November 21 2011), earlier than the previous years. Passing the final bill in Parliament requires absolute majority. The new coalition government has a majority of 255 out of 300 seats in the Parliament.

**Table 1: Greek Economy: Basic Indicators**  
(%annual changes, constant prices)

	2010	2011	2012
<b>GDP growth</b>	-3.5	-5.5	-2.8
<b>Private consumption</b>	-3.6	-6.2	-4.1
<b>Public Consumption</b>	-7.1	-8.0	-7.5
<b>Investment</b>	-13.3	-12.9	-4.0
<b>Exports of G&amp;S</b>	4.2	4.5	6.4
<b>Imports of G&amp;S</b>	-7.2	-5.9	-2.8
<b>Harmonised CPI</b>	4.7	2.8	0.6
<b>GDP deflator</b>	1.7	1.4	0.4
<b>Employment</b>	-2.1	-5.7	-2.0
<b>Unemployment</b>	11.9	15.4	17.1

Source: Ministry of Finance

The new budget is framed on an adverse domestic macro environment with a larger than

previously expected recession in 2011, and a continuation of the economic recession in 2012. Specifically, real GDP growth is now expected to contract by -5.5% and -2.8% -of-GDP in 2011 and 2012 respectively. The unemployment rate is expected to climb further, reaching 15.4% of the labor force in 2011 and 17.1% in 2012, from 11.9% in 2010. On the other hand, domestic inflation is expected at 2.8% in 2011 and 0.6% in 2012. Note that 2010 inflation was 4.7%.

In addition, general government gross debt is expected to reach 161.8%-of-GDP or €352bn in 2011 and 145.5%-of-GDP or €309.3bn, if the new PSI will be implemented. The respective 2010 figure was 142.8% of GDP.

**Greek GDP Q3:2011 flash estimate: Non-seasonally adjusted real GDP contracted by -5.2%YoY in Q3:2011, higher than the Q2:2011 figure of -7.4%YoY**

According to ELSTAT, the Greek Statistical Authority, the Greek economy contracted by -5.2%YoY in Q3:2011, compared to the respective 2010 period. The figure is based on available non-seasonally adjusted data. The agency did not provide a seasonally-adjusted figure. The Q2 2011 seasonally unadjusted GDP figure was -7.4% of GDP.

It needs to be noted that ELSTAT has recently changed the methodology it uses to compile quarterly data for general government transactions. Specifically, quarterly estimates for the years 2009-2011 are now based on data mainly from direct sources, while for the period 2000-2008 estimates were made by allocating the annual results to the quarters. This affects the comparability of the 2008 and 2009 data, and ELSTAT warns that its quarterly GDP growth figures between these two years should be treated with caution. Furthermore, due to the relatively short time span of the available quarterly general government data in the period Q1:2009-Q1:2011, the previously implemented method for the seasonal adjustment did not provide satisfactory results.

Note that according to the recently announced 2012 Budget plan, Greek GDP is expected to contract by -5.5% in 2011 and remain at negative levels in 2012 at -2.8%. Return to positive levels is postponed for 2013.

**Preliminary budget execution data for year-to-October 2011 undershoot the 10-month MTF5 target for 2011**

Preliminary data for the execution of Greece's State budget for year-to-October 2011 showed that the central government

deficit rose by 11.2%YoY, compared to October 2010, reaching ca €20.10bn. This resulted into an undershooting of the respective Medium Term Fiscal Strategy (MTFS) 10-month target by €1.35bn or -6.3%.

Net revenues for year-to-October 2011 were at €43.44bn, a decline of -2.6%YoY compared with the respective 2010 period. Net revenues for the year-to-October are lower by €1.03bn or -2.6% from the respective MTF5 10-month revenue target.

The main reasons driving revenues were: **a)** the larger than previously projected recession, **b)** the non repetition of an extension granted for the payment of prior year road duties, which inflated State receipts in January 2010 by an estimated €0.39bn, **c)** the reduced receipts from withholding personal income tax in 2011 due to a more favorable tax treatment of personal incomes as a result of the new tax law and the income reduction, and **d)** the increased tax refunds due to the clearing of 2010 obligations. Moreover, strikes of tax office employees caused delays in tax collection and at the same time there were delays in collecting licensing and royalties' revenue by the State. The authorities expect that the November-to-December 2011 revenues will include the delayed tax receipts and royalties revenue.

Tax refunds amounted to €4.24bn for year-to-October 2011, a 14.2%YoY increase relative to the respective period a year earlier. Note here that the government, in an effort to reduce VAT evasion, introduced in 2010 a scheme linking 2010 tax refunds with the volume of retail receipts submitted by tax payers. Reportedly, this was the main reason behind the sharp rise in tax returns in the year-to-October 2011. The government already modified the tax refunds scheme in the calculation of the 2011 taxable income.

In addition to the aforementioned, it appears that persisting disfunctionalities in the revenue collection mechanism and widespread tax evasion continued to weigh on budget revenues over the first ten months of the year.

With regards to the tax collection system and revenues, the recently published 1<sup>st</sup> quarterly report of the Task Force for Greece, a European Commission sponsored technical assistance team on fiscal and structural issues, is of critical importance. The Task Force estimates that there are ca €60bn outstanding in unpaid taxes. Out of these, €30bn are the subject of court cases – some of which have been running for over a decade. The processing of the tax related disputes from the Greek courts remains one of the major concerns of the EC/ECB/IMF officials. The Task Force further estimates that on average €7.0bn could be collected in the immediate period, improving in this way the Greek fiscal situation. The Task Force for Greece highlighted the following areas as critical for the improvement of the tax administration and tax

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revenues:

- debt collection
- audit of large taxpayers
- dispute resolution
- tax audit

For the current year as a whole, the State budget targets a 1.4%YoY increase in net ordinary revenue. To achieve the latter target, the government needs to generate additional revenue (mainly from taxation) of ca €11.63bn (or €5.81bn per month) for the remaining months of 2011. This target seems overambitious and there are serious concerns whether the revenue shortfall could be eliminated by the proper and timely implementation of the tax measures incorporated in the MTFs and the new measures announced on September 11 2011.

On the expenditure side, ordinary budget outlays for the year-to-October 2011 totaled ca €57.44bn, a 5.7% YoY increase, compared with the respective 2010 period. This was mainly the result of a €0.97bn or 2.4%YoY increase in primary expenditure over the first ten months of this year, mainly due to **a**) higher transfers to social security funds by €1.84bn due to lower social security contributions, **b**) higher grants by €0.31bn to the Employment Agency for unemployment benefits and **c**) hospitals procurement expenses rising by €0.79bn covering this year's and past year's hospitals expenditure. Interest payments for year-to-October 2011, increased by 19.5%YoY, compared to the respective 2010 period. In the public investment budget (PIB), year-to-October 2011 revenue amounted to €1.89bn, an increase of 38.1% YoY compared with the respective 2010 period. On the other hand, PIB expenditure was down by €3.79bn or -37.4%YoY compared to the respective 2010 period.

As an overall assessment, the developments in the State budget deficit for year-to-October 2011 signal a deviation from the updated 2011 annual deficit target of -8.5% of GDP. According to the 2012 Budget proposal, the 2011 budget deficit will be around -9% of GDP. The recent measures announced by the Government in September 11<sup>th</sup> 2011 – if rightly and timely implemented – provide a temporary fix. In the medium term however, the fight against tax avoidance and the reduction of the costs in the broader public sector are the necessary prerequisites for a sustainable improvement in public economics.

Table 2: January-to-October 2011 Budget execution

Ordinary Budget	Jan-Oct.	Jan-Oct.	Jan-Oct.	2011 MTFs	Annual target (%YoY)
	2010 (€bn)	2011 (€bn)	2011 (%YoY)	target Jan-Oct. (€bn)	
<b>1. Net Revenue (a-b-c)</b>	<b>40.91</b>	<b>39.23</b>	<b>-4.1</b>	<b>40.26</b>	<b>1.4</b>
<b>a. Gross revenue</b>	<b>44.61</b>	<b>43.44</b>	<b>-2.6</b>	<b>44.35</b>	<b>0.2</b>
<b>b. NATO revenue</b>	<b>0.01</b>	<b>0.03</b>	<b>127.3</b>	<b>0.03</b>	
<b>c. Tax refunds</b>	<b>3.71</b>	<b>4.24</b>	<b>14.2</b>	<b>4.12</b>	<b>-11.7</b>
<b>2. Expenditure (α+β+γ+δ+ε+στ)</b>	<b>54.32</b>	<b>57.44</b>	<b>5.7</b>	<b>58.55</b>	<b>4.5</b>
<b>α. Primary expenditure</b>	<b>40.57</b>	<b>41.54</b>	<b>2.4</b>	<b>42.33</b>	<b>-0.7</b>
<b>β. Transfer to hospitals for the settlement of part of past debt</b>	<b>0.30</b>	<b>0.43</b>	<b>27.7</b>	<b>0.45</b>	<b>22.6</b>
<b>γ. NATO expenditures</b>	<b>0.01</b>	<b>0.01</b>	<b>-20.4</b>	<b>0.02</b>	<b>73.9</b>
<b>δ. Military procurement</b>	<b>0.55</b>	<b>0.20</b>	<b>-63.6</b>	<b>0.43</b>	<b>8.2</b>
<b>ε. Forfeiture of Government Guarantees</b>	<b>0.11</b>	<b>0.03</b>	<b>-70.1</b>	<b>0.04</b>	<b>54.3</b>
<b>στ. Interest costs</b>	<b>12.74</b>	<b>15.23</b>	<b>19.5</b>	<b>15.28</b>	<b>23.3</b>
<b>Public Investment Budget (PIB)</b>					
<b>3. Revenue</b>	<b>1.37</b>	<b>1.89</b>	<b>38.1</b>	<b>3.07</b>	<b>8.1</b>
<b>4. Expenditure</b>	<b>6.05</b>	<b>3.79</b>	<b>-37.4</b>	<b>8.45</b>	<b>-10.7</b>
<b>5. Budget deficit (-) or budget surplus (+) (1-2+3-4)</b>	<b>-18.08</b>	<b>-20.10</b>	<b>11.2</b>	<b>-21.46</b>	<b>5.1</b>

Source: Ministry of Finance

### General Government arrears for year-to-September 2011 at €6.49bn or 2.7% of GDP; upwards risk for the 2011 budget deficit target of 8.5% of GDP

According to the most recent data published by the Ministry of Finance, total general government arrears for the year-to-September 2011 period amounted to €6.49bn or 2.7 % of GDP. The figure is lower from the respective August figure by €0.04 bn but its level causes concerns for the achievement of the 2011 budget target of 8.5% of GDP.

According to the draft of the 5th Review of the EC/ECB/IMF adjustment programme for Greece, the criterion of the non-accumulation of arrears was missed. This was due primarily in the delays in the disbursement of the EC/ECB/IMF loan. However, the chronic problems with the deficiencies in a) expenditure control in the several government entities, b) administrative delays in payments by social security to hospitals which in turn lead to delays in hospitals' payments to suppliers, contributed significantly in the accumulation of arrears.

**Unemployment rate in August 2011 at 18.4%, higher than July's reading of 16.5%**

According to ELSTAT, the Greek Statistical Authority, unemployment in August 2011 reached 18.4%; higher than July's reading of 16.5% because of seasonal factors (the end of the peak of the tourism sector employment) as well as due to the continuing recession. Note that the rate of unemployment was at 12.2% in August 2010. According to the 2012 Budget plan, the 2011 unemployment is at 15.4%.

**CPI inflation in October 2011 at 3.0%, slightly lower than September's reading of 3.1%**

According to ELSTAT, CPI inflation in October 2011 was at 3.0%, compared to October 2010. The respective October 2010 reading was 5.2%. The CPI in October 2011 compared to September 2011 increased by 0.1%. In October 2010, the monthly rate of change of the CPI was 0.2%.

Note however that the increases in VAT rates and special consumption taxes introduced by the MTFs in early July and implemented after September 1st 2011 as well as the new measures announced in September 2011 and implemented from October 1st onwards contributed to this increase. The CPI target for 2011 is at 3.0% lower than 2010 CPI of 4.7%, according with the 2012 Budget plan.

**Concluding Remarks**

The Greek economy is expected to continue in a recessionary path in 2011 as the GDP data for Q3 2011 indicate. The 2012 Budget plan forecasts -5.5% of GDP contraction for 2011 and further continuation of the recession by -2.8% in 2012. Budget execution data, at the central and general government level, indicate a slight derailment from the recently upwards revised budget deficit target of -8.5% of GDP. The recent report of the Task Force for Greece highlights the lingering deficiencies of the Greek tax collection system and urges the government to work on their improvement.

We consider the austerity and structural measures that the Greek Government announced in the previous period together with the actions mentioned in the Task Force's report as prerequisites not only for the achievement of the 2011 deficit target but also for the continuation of the fiscal consolidation effort of the Greek economy.

Table 3: Greece-Key Indicators				
	Last	ytd	2010	2009
<b>Macroeconomic indicators</b>				
GDP growth (%YoY)*	-7.3 (Q2 11)	-2.8	-3.5	-3.2
CPI	3.0 (Oct. 11)	2.4	4.7	1.2
Unemployment rate	18.4 (Aug. 11)	35.9	14.8	10.2
Labor Cost (%YoY)	-5.2 (Q2 11)	-11.7	-4.2	3.6
Economic Sentiment (index level-period average)	67.5 (Oct. 11)	73.5	75.1	76.3
<b>Consumer-vigor indicators</b>				
Private consumption in constant prices (% YoY)	-6.1 (Q2 11)	-5.5	-3.6	-1.3
Retail sales excl. fuels & lubricants volume (% YoY)	-0.5 (Aug. 11)	-21.7	-23.7	-0.7
New private passenger car registrations (% YoY-cumulative ytd)	-35.7 (Oct. 11)	-35.7	-35.6	-17.8
Consumer confidence (index level - period average)	-83.8 (Oct. 11)	-72.5	-63.4	-45.7
Retail trade expectations (index level - period average)	-37.3 (Oct. 11)	-35.4	-33.7	-15.4
<b>Industrial-activity indicators</b>				
Industrial production (% YoY)	-1.8 (Sept 11)	4.0	-5.2	-6.8
Capacity utilization in industry (index level -period average rate)	66.0 (Oct. 11)	67.7	68.6	70.5
Industrial confidence (index level - period average)	-25.4 (Oct 11)	-20.1	-22.5	-28.4
Manufacturing PMI (index level - period average)	40.5 (Oct 11)	44.0	43.8	45.4
<b>Construction sector &amp; other investment-activity indicators</b>				
Cross fixed capital formation in constant prices (% YoY)	-21.8 (Q2 11)	-2.6	-7.6	-15.1
Housing investment in constant prices (% YoY)	-21.9 (Q2 11)	-14.1	-18.5	-24.8
Other construction in constant prices (% YoY)	-16.6 (Q2 11)	-39.6	-11.7	-4.7
Private building permits volume (% YoY-cumulative ytd)	-37.4 (Feb 11)	-58.8	-24.1	-26.1
Construction confidence (index level - period average)	-70.6 (Oct. 11)	-68.8	-55.4	-39.5
<b>Balance-of-Payments statistics (€ terms)</b>				
Tourism revenues (% YoY-cumulative ytd)	6.5 (August 11)	10.0	-7.6	-10.6
Transportation revenues (% YoY-cumulative ytd)	-4.3 (August 11)	-10.9	13.8	-29.4
<b>Customs-based statistics (€ - terms)</b>				
Goods exports (% YoY-cumulative ytd)	65.0 (Sept. 11)	41.2	10.9	-18.1
Goods exports to EU (% YoY-cumulative ytd)	18.4 (Sept. 11)	13.3	8.5	20.5
Goods exports to non-EU countries (% YoY-cumulative ytd)	160.6 (Sept. 11)	61.1	12.9	-16.3
Goods imports (% YoY-cumulative ytd)	-23.0 (Sept. 11)	-11.0	-3.5	-19.2
Goods imports from EU (% YoY-cumulative ytd)	-1.7 (Sept. 11)	-7.4	-12.9	-17.7
Goods imports from non-EU countries (% YoY-cumulative ytd)	-44.9 (Sept. 11)	-20.2	-2.4	-31.7
<b>Domestic MFI credit to domestic enterprises &amp; households (outstanding balances and net flows)</b>				
Private sector (% YoY)	-2.2 (Sept. 11)	-1.9	0.0	1.5
Enterprises (% YoY)	-0.9 (Sept. 11)	-0.5	1.1	1.0
Households (% YoY)	-3.1 (Sept. 11)	-3.0	-1.2	1.9
Housing loans (% YoY)	-2.1 (Sept. 11)	-1.7	-0.3	3.7
Consumer credit (% YoY)	-6.5 (Sept. 11)	-4.0	-4.2	-1.6
<b>Private-sector credit outstanding (% GDP) **</b>				
Total domestic enterprises & households	111.9 (Sept. 11)	-	112.1	106.6
Domestic households	50.7 (Sept. 11)	-	51.4	50.2

Source: Hellenic Statistical Authority, Bank of Greece, ECOWIN, AMECO, Eurobank EFG Research

\* Non-seasonally adjusted GDP data were used for columns Last and ytd. Seasonally adjusted data not available yet (October 6, 2011).

Growth rates for 2009-10 include the recent ELSTAT's revision.

\*\* 4th Review of the EC/ECB/IMF adjustment programme forecasts for 2010 (€ 230 bn) and 2011 (€ 226 bn) were used.

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Eurobank EFG, 20 Amalias Av & 5 Souris Str, 10557 Athens, tel: +30.210.333.7365, fax: +30.210.333.7687, contact email: [Research@eurobank.gr](mailto:Research@eurobank.gr)

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