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FOCUS NOTES

Greece- Eurogroup May 24th expected to open the door for the release of the next ESM loan tranche

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Greek government submitted to Parliament key multi-bill incorporating implementation laws of remaining prior actions attached to 1st review

Aiming to fulfil all pending prior actions attached to the 1st programme review ahead of the May 24th Eurogroup, the Greek government submitted to the Hellenic Parliament under the emergency procedure[1] earlier this week (Wednesday, May 18) a multi-bill containing the relevant legislation required for their implementation. These reportedly include, inter alia:

(i) *The fiscal contingency mechanism*. The said mechanism will work as follows: If annual general government accounts released by Eurostat in mid- April show a deviation from the agreed primary surplus target[2] of the previous year, then a package of measures aimed at general government expenditure, including non-discretionary measures, will automatically be implemented following the issuance of a relevant Presidential Decree by Greece's Minister of Finance. The said decree will have to be issued by May 31st and the relevant measures, including pensions and public sector wages, should be implemented by June 1st. In case the required decree is not issued, the mechanism will be activated automatically and will be applied horizontally on all areas of general government expenditure. The said package will not incorporate certain socially-sensitive measures, including, among others: (i) public healthcare expenditure; (ii) public expenditure for unemployment benefits, family allowance and heating, the Public Investments Programme and public expenditure for the minimum guaranteed income. Should expenditure measures be automatically activated, the Greek government will be authorized to replace them in whole or in part with permanent structural measures, including revenue measures, in the draft budget that is submitted in Parliament each October. Exceptions to the activation of the mechanism will be limited to: (i) exceptional events outside government control with an economic negative impact above 0.5%-of-GDP; and (ii) a deviation from the agreed primary target up to 0.25%-of-GDP. For deviations between: (i) 0.26%-of-GDP and 0.75%-of-GDP, measures worth 0.5%-of-GDP will be activated; (ii) 0.76%-of-GDP and 1.25%-of-GDP, measures worth 1%-of-GDP; (iii) 1.26%-of-GDP and 1.75%-of-GDP, measures worth 1.5%-of-GDP; and (iv) 1.76%-of-GDP and 2.25%-of-GDP, measures worth 2%-of-GDP. The contingency mechanism will come in force in 2017 and will remain active at least until the end of May 2019.

(ii) *A package of additional parametric measures.* These are expected to secure €1.84bn in the period 2016-2018[3]; €363.6mn in 2016, €1.072bn in 2017 and the remaining €405mn in 2018 (see Table 1 below)

[1] Submission of a bill under an emergency procedure implies that the parliamentary debate will be limited to 48 hours.
[2] The respective targets according to the programme are as follows: 0.5%-of-GDP in 2016, 1.75%-of-GDP in 2017, 3.5% -of-GDP in 2018.
[3] The package of additional parametric measures along with the social security pension reform and the overhaul of the pension income tax are expected to secure savings/revenue of €5.4bn (€1.8bn each) in the period 2016-2018 to facilitate fulfilment of the primary surplus fiscal target of 3.5%-of-GDP in 2018. The legislation for the implementation of the social security pension reform and the overhaul of the pension income tax was approved by the Hellenic Parliament on May 8th.

Table 1- Parametric measures worth €1.8bn in 2016-2018

— An increase in the top VAT rate to 24% from 23% currently (as of June 2016)
— Increased luxury tax on cars and car registration fees (as of June 2016)
— Increased tax on mutual funds(as of June 2016)
— Abolishment of the special 50% reduction in alcoholic beverage that is currently applied in the island complex of Dodecanese (as of June 2016
— Imposition of a special levy on beer (as of June 2016)
— An increase in the special consumption tax on heating oil (as of June 2016)
— Imposition of a special consumption tax on electronic cigarettes (as of January 2017)
— An increase in the special consumption tax on cigarettes and tobacco (as of January 2017)
— An increase in the special tax on imported coffee (as of January 2017)
— Imposition of a 10% tax rate on cable TV & 5% tax rate on fixed e-bills (as of January 2017)
— An increase in the special consumption tax on gas (as of January 2017)
— An increase in the special consumption tax on unleaded petrol (as of January 2017)
— An increase in the special consumption tax on diesel (as of January 2017)
— Increased company car taxation (as of January 2017)
— A freeze in special payrolls (as of January 2018)
— Gradual reduction in the recruitment rule for the public sector, *i.e.*, 1-to-4 in 2017 & 1-to-3 in 2018 (as of January 2018)
— Imposition of an overnight fee on hotels ranked in categories above two starts (as of January 2018)
— Certain amendments to the implementation framework of the Unified Property Tax (ENFIA) via higher property rates and a broader property tax base through the imposition of the Supplementary Property Tax on owners whose properties are valued above €200k compared to €300k currently.

Source: Local press, Eurobank Research

(iii) *Establishment of the Privatization and Investment Fund.* The new Fund will be dubbed Hellenic Company of Assets and Participations and will consist of four subsidiaries: (i) the Hellenic Republic Asset Development Fund (HRADF); (ii) the Hellenic Holdings Company [4]; (ii) the Public Properties Company (PPCo S.A); and (iv) the Hellenic Financial Stability Fund (HFSF). The fund's lifetime will be 99 years. The Supervisory Board will comprise five members while both the Greek government and official creditors will have veto rights on the appointment of the Board members. In more detail, three members will be appointed by Greece's Minister of Finance with the consensus of the EU Commission and the ESM and the remaining two, including the President, will be appointed by the EU Commission and the ESM subject to approval by the finance minister. All decisions will be reached by a qualified majority. The Board of Directors will comprise 5-7 members for a four-year term including the President and the CEO, who will be elected by the Supervisory Board. Under the May 9th Eurogroup agreement, the Supervisory Board must be appointed by June 2016 and the Fund should become fully operational no later than September 2016. 50% of privatization proceeds will be channeled towards investment and the remaining 50% will be used for decreasing Greece's debt to GDP ratio.

(iv) *Finalization of the NPL resolution framework.* Loans collateralized by the debtor's primary residence will be exempt from the scope of permitted sales to non-banking institutions until December 31st 2017, provided that the objective value of the primary residence does not exceed €140k. Reportedly, the remaining NPL categories that were excluded from the resolution framework that was initially agreed between the Greek government and official creditors late last year (i.e., consumer loans up to €20k, loans granted to SMEs up to €500k and loans granted to freelancers up to €250k that are not collateralized with the debtor's primary residence or the value of the collateralized residence is less than €140k) will be eligible for sale as units or in groups together with performing loans as of mid-June 2016, when the relevant protection scheme expires. NPLs will be eligible for sale only if the debtor and the guarantors have been invited by the seller to settle or reschedule the debt at least 12 months before the contemplated offer for sale. NPLs collateralized with Greek State guarantees will be reportedly excluded indefinitely from the scope of permitted sales.[5]

[4] The newly established Hellenic Holdings Company will reportedly incorporate five state enterprises: the Athens Transport Company (OASA) and its two subsidiaries STASY (operator of the metro and tram) and OSY (buses and trolleys), the Athens Olympic Sports Complex (OAKA) and the Hellenic Post (ELTA). As per the same sources, additional state enterprises will likely be transferred to the new company "at a later stage," namely Public Power Corporation (PPC), the Athens and Thessaloniki water companies (EYDAP and EYATH), the Hellenic Vehicles Industry (ELVO), Attiko Metro, State Infrastructures SA and the Hellenic Railways Organization (OSE).
[5] According to BoG Governor Yannis Stournaras, NPLs stood at 44.2% of total loans in December 2015 from 39.9% in December 2014.

(i) *Full independence of the General Secretariat of Public Revenues.* As of 2017, the General Secretariat of Public Revenues will be replaced by the Independent Authority for Public Revenue that will be fully autonomous, i.e. it will have operational independence, administrative and economic autonomy and will not be monitored by any government or state entity or other administrative authority. Its administration will be led by a Governor, an Administrative Council and a European Commission expert. The authority's interaction with the finance minister will be limited to the minister submitting proposals and supply strategic guidelines regarding the planning for the implementation of government policy. The sole person responsible for the authority's personnel will be the governor. In case of a disagreement between the governor and the finance minister regarding taxation policy, the solution will be given by the administrative council.

The multi-bill is expected to secure parliamentary approval ahead of the May 24th Eurogroup

The parliamentary debate on the aforementioned omnibus bill is scheduled to end with a roll call vote on Sunday afternoon (22 May), just a few hours before the Euroworking Group that convenes on May 23rd ahead of the following day's Eurogroup. As things stand at this point, the bill is expected to secure approval by all 153 SYRIZA/ANEL coalition MPs in the 300-seat Parliament. As a reminder, the government had secured earlier this month parliamentary approval of the social security and pension reform and the overhaul of the income tax code, two of the core prior actions for the finalization of the review, with the support of all 153 coalition deputies. Successful completion of the review is a key precondition for: (i) the release of additional funding under the 3-year ESM loan facility; (ii) initiation of official discussions on debt relief measures; (iii) reintroduction of a Greek collateral waiver (an issue which is reportedly expected to be discussed at the June 2nd ECB monetary policy meeting); and (iv) inclusion in the ECB's QE programme.[6]

Expectations that the May 24th Eurogroup will open the door for the release of the next ESM loan tranche

Conditional on the timely approval by the Hellenic Parliament of the aforementioned multi-bill, the Euro-Working Group which is scheduled to convene on Monday, May 23rd is anticipated to confirm at a technical level the completion of the 1st programme review. Provided that all goes as planned, the May 24th Eurogroup is expected to politically endorse the compliance report for Greece's 1st programme review, opening the door for the release of the next loan tranche. According to some press reports, it could amount to around €9 - €11bn, consisting of €5.4bn for the coverage of debt interest and amortization payments plus another €3 - €5bn for the clearance of state arrears.[7] The latter amount will be reportedly released in the form of monthly sub-tranches conditional on the government gradually paying off its arrears to third parties. After paying a total amount of c. €2.0bn to the IMF so far this year including c. €1.8bn in principal payments and c. €200mn in interest payments, Greece is next due to make a principal payment to the Fund on June 7 (€299mn) followed by another one on July 13 (€449mn). In addition to the scheduled payments to the IMF, Greece has also to make a maturity payment of €250mn on May 24 (State guaranteed bond issued by Hellenic Railways Organization in May 2004 under English law). Yet, the major hurdle comes on July 20 when two GGBs mature for a total notional amount of €2.3bn.

Divergence of views on debt relief prevails between the IMF and European creditors

With respect to debt relief, the issue is anticipated to feature high on the agenda of the May 24th Eurogroup but a final agreement on the issue may prove difficult to reach. According to European Commission Vice President Valdis Dombrovskis the aim at the upcoming Eurogroup is for European creditors and the IMF to agree on a specified debt "road map" of specific debt relief measures so as to ensure the Fund's participation in the program. However, a divergence of views on the issue reportedly continues to exist between European creditors and the IMF. The Fund urges for imminent and drastic debt relief measures to secure debt sustainability, a key prerequisite for its financial involvement in Greece's new adjustment programme. In more detail, international newswires suggested that the IMF made a rather bold proposal regarding Greece's public debt at the May 9th Eurogroup envisioning inter alia: (i) a grace period on all interest & amortization payments up to 2040: (ii) maturity extension to 2040-2080; and (iii) a fixed interest rate on all EU loans at 1.5% for the next 30-40 years. On their side, the majority of the European creditors including Germany, argue that Greek debt is not a pressing issue and any relief measures could be granted upon completion of the new programme contingent on full implementation of the attached conditionality. Nevertheless, in an interview to international newswires on the sidelines of the G7 Finance Ministers' meeting, Eurogroup President Jeroen Dijsselbloem stated that significant progress has been made on the issue of

[6] According to BoG Governor Yannis Stournaras, the reinstatement of sovereign debt waiver and the inclusion in the ECB's QE program could have a positive impact of €400- €500mn on Greek bank results in 2017.

[7] According to the Greek finance ministry, the total stock of state arrears (i.e., government debts outstanding for more than 3 months) stood at €6.674bn in March (including €1.099bn tax refunds arrears). Arrears clearance is estimated at c. €7bn over the programme period.

debt relief and an agreement is possible at the May 24th Eurogroup. In any case, should official creditors fail to reach a compromise now, deliberations on debt relief are expected to continue in the period ahead and a final agreement is reportedly anticipated to be sealed by September 2016, when official discussions on the 2nd review are scheduled to commence. In an interview to a local newspaper earlier this week, Greece's Prime Minister Alexis Tsipras stressed that a final agreement on public debt could facilitate Greece to return to markets within next year, ahead of the completion of the new programme.

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