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Eurobank EFG

GREECE MACRO MONITOR

November 28, 2011

Focus notes: Greece

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January-to-October State budget execution broadly in line with revised government projections; weak revenue growth, accumulating government arrears posing risks to the full-year deficit target

According to the final State budget execution data for October 2011, the central government deficit rose by 11.1%YoY over the first ten months of the year reaching €20.09bn. This implies an undershooting of the respective target of the MTFS (Medium-Term Fiscal Strategy) by €0.27bn. The State budget targets a 0.9%YoY increas000e in net ordinary revenue for the full–year. To achieve this, the government needs to generate additional revenue (mainly from taxation) of ca €11.6bn or €5.8bn per month in the remainder of 2011. This target seems ambitious and there are legitimate concerns over whether the revenue shortfall could be eliminated by the proper and timely implementation of the measures incorporated in the MTFS as well as those announced more recently.

Net revenues declined by 4.0%YoY in the 10 months to October 2011, underperforming the MTFS's respective revenue target of +2.5%. The main reasons behind the underperformance of budgetary revenues so far this year, include: **a)** the deeper than earlier expected domestic 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 amount of €0.39bn; **c)** reduced receipts from the withholding personal income tax in 2011 as a result of the economic recession and a more favorable tax treatment of personal incomes due to the new tax law; **d)** increased tax refunds due to the clearing of 2010 obligations; e) repeated strikes by tax office employees, causing delays in tax collections and f) delays in collecting licensing and royalty duties. Authorities now expect budget revenues in November-December 2011 to be boosted by increased collections of delayed tax payments and royalties as well as the new tax measures announced in September 2011. Persisting dysfunctionalities in the revenue collection mechanism and widespread tax evasion constitute additional factors that weighed on budget revenues in the first ten months of the year. In January-October 2011, VAT revenues decreased by 2.0% YoY. Specifically, VAT revenues from fuel and tobacco products increased by 0.3% YoY and 0.1% YoY, respectively, while, VAT revenues from other goods declined by -0.6% YoY.

In a its 1st quarterly report published recently, the Task Force for Greece, a European Commission sponsored technical assistance team on fiscal and structural issues, estimates that the total outstanding amount of unpaid taxes in Greece is ca €60bn (~28ppt-of-GDP). Out of this, ca €30bn are currently subject to court cases, some of which have been running for over a decade. Pending dysfunctionalities and long delays in the processing of tax related disputes in the Greek judicial system remain serious sources of concern. The Task Force further estimates that some €7bn could be collected in the immediate period, helping to improve Greece's fiscal accounts. The Task Force highlighted certain areas that appear to be critical for the improvement of tax revenue growth and tax administration. Among others, these include: **a)** debt collection, **b)** audit of large taxpayers, **c)** tax dispute resolution and **d)** tax audit.

Tax refunds increased by 14.2% YoY in the 10 months to October 2011, reaching €4.24bn. In an effort to reduce VAT evasion, the government introduced last year a scheme linking 2010 refunds with the volume of retail receipts submitted by tax payers. Reportedly, this was the main reason behind the sharp rise in tax returns during the first ten months of this year. The government already modified the tax refunds scheme in the calculation of the 2011 taxable income.

On the expenditure side, ordinary budget outlays rose by 5.7% YoY in January-October 2011, amounting to €57.44bn. This was mainly the result of a 2.4%YoY increase in primary expenditure over the first ten months of this year, mainly as a result of: **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)** higher payments (by €0.79bn) for the settlement of hospital expenditures incurred earlier this year and in 2010. Furthermore, Interest payments increased by 19.5%YoY year-to-October 2011. In the public investment budget (PIB), revenues increased by 38.1% YoY, while expenditures were down by 37.4%YoY over the same period.

Table1: January-to-October 2011 Budget execution

Ordinary Budget	Jan-Oct. 2010 (€bn)	Jan-Oct. 2011 (€bn)	Jan-Oct. 2011 (%YoY)	2011 MTFS target Jan-Oct. (€bn)	Annual target (% YoY)
1. Net Revenue (a-b-c)	40.91	39.27	-4.0	40.26	0.9
a. Gross revenue	44.61	43.48	-2.5	44.35	0.2
b. NATO revenue	0.01	0.03	127.3	0.03	
c. Tax refunds	3.71	4.24	14.2	4.12	-6.0
2. Expenditure (α+β+γ+δ+ε+στ)	54.32	57.47	5.8	58.55	3.8
α. Primary expenditure	40.57	41.57	2.5	42.33	-0.7
β. Transfer to hospitals for the settlement of part of past debt	0.30	0.43	44.7	0.45	22.6
γ. NATO expenditures	0.01	0.01	0.0	0.02	20.8
δ. Military procurement	0.55	0.20	-63.6	0.43	-41.0
ε. Forfeiture of Government Guarantees	0.11	0.03	-69.8	0.04	62.1
στ. Interest costs	12.74	15.23	19.5	15.28	23.9
Public Investment Budget (PIB)					
3. Revenue	1.37	1.89	38.1	1.96	9.5
4. Expenditure	6.05	3.79	-37.4	4.03	-18.5
5. Budget deficit (-) or budget surplus (+) (1-2+3-4)	-18.08	-20.09	11.12	-20.36	1.2

Source: Ministry of Finance

As an overall assessment, the most recent data for the State budget execution imply overshooting risks to the *upwardly revised* general government deficit target of 9%-of-GDP in 2011. The full-year data will not be known before February or March 2012, but accumulating government arrears to various suppliers - to the tune of €6.48bn or ca 3ppt-of-GDP as of Sept. 2011 – remain among the main concerns with respect to the attainability of this year's deficit target. As a reminder, the government has recently announced new measures to help bridge an identified gap in the 2011 budget. These included, among others, a special levy on property, a further reduction in tax exempt thresholds and the acceleration of a number of reforms agreed earlier with the Troika to help reduce public sector employment and close down or merge a range of unproductive public entities. These measures are likely to help improve budget execution in to the remaining months of this year, to the extent of course that they are rigorously implemented and they don't deal a much greater blow to a slowing domestic economy.

Current account deficit down 8.6%YoY in January-September; narrowing trend likely to continue in the remaining of 2011

According to the latest Bank of Greece data, the current account deficit in the nine months to September 2011 declined by €1.4bn or 8.6% relative to the same period a year earlier, reaching €15.02bn. This was mainly the result of a significant drop in the non-oil trade deficit (by €2.65bn) and a higher surplus in the services balance (by €0.8bn), which more than offset a large increase in the net oil import bill and a widening of the income account deficit. On the other hand, the current transfers balance remained virtually unchanged.

The overall trade deficit in the first nine months of the year declined by €1.28bn or 5.8% compared with the respective period in 2011. The deficit excluding oil and ships decreased by €2.50bn or 20.1% YoY. Receipts from exports of goods excluding oil and ships increased by €1.55bn or 18.8% YoY, while the corresponding import bill declined by €0.4bn or 0.94% YoY. These developments more than offset a €1.37bn increase in the net oil import bill. The services balance for the year-to-October 2011 period increased by €0.80bn or 7.1% YoY thanks to lower net payments for "other" services and slightly higher net travel receipts, which more than offset a contraction in net transport receipts. Net transport receipts fell by €0.59bn or 10.5% YoY. Net travel receipts increased by €0.73bn or 10.6% YoY as a result of **a)** higher travel spending by non-residents in Greece (+9.4% YoY), which more than offset a concomitant rise of travel spending by Greeks abroad (+5.0% YoY). Foreign tourist arrivals rose by 10.4% YoY in the year-to-September 2011 period. Elsewhere, the income account deficit for the year-to-September 2011 period rose by €0.67bn or 11.0% YoY, chiefly as a result of higher net interest, dividend and profit payments. On th other hand, the current transfers balance for the year-to-September 2011 period showed a surplus of €0.69bn and remained unchanged compared to the respective period a year earlier.

From the financing side, direct investment showed a net outflow of €1.6bn in January-October 2011 compared with a net outflow of €0.4bn in the corresponding period of 2010. A net outflow of €14.6bn was also observed under portfolio investment (compared with a net outflow of €18.3bn in the corresponding period a year earlier). In more detail, an outflow was recorded due to, mainly, a decrease of €19.9bn in non-residents' holdings of Greek government bonds and Treasury bills and, to a lesser extent, a €624mn rise in residents' investment in foreign derivatives and a €213mn decline in non-residents' holdings of shares of Greek firms. These developments were only partly offset by a €6.0bn decline in resident institutional investors' holdings of foreign bonds and Treasury bills and a €78mn decrease in residents' holdings of shares of foreign firms.

Greece and the euro area debt crisis - Event risks calendar through to year-end

Based on the information we gathered so far, we provide below an event risk calendar for Greece and the euro area debt crisis, covering the period until the end of this year.

November 28, 2011: **President of the European Council Herman Van Rompuy and President of the European Commission Jose Manuel Barroso** will represent the European Union at an **EU-US summit** in Washington DC. The official agenda includes, among others, global economic issues, bilateral relations and opportunities to promote growth and jobs. The sovereign debt crisis is also expected to be a topic of discussion.

November 29-30, 2011: Eurogroup/Ecofin meeting, the last scheduled for this year. Reportedly, the agenda will include, **i)** further discussions on the parameters of the two main options agreed at the October Summit to boost the EFSF's firepower; **ii)** relevant indicators and respective thresholds for the macroeconomic "scoreboard" to detect macroeconomic imbalances as per the recent EU proposals for tighter economic and fiscal governance in the euro area; **iii)** discussions on the European Commission's recent proposal for a financial transaction tax. According to that proposal, the tax would be levied on transactions between financial institutions when at least one of the counterparties is located in the EU. The exchange of shares and bonds would be taxed at a rate of 0.1%, while a rate of 0.01% would apply for transactions involving derivative contracts. The Commission has proposed that the tax should come into effect from 1st January 2014. The Nov 29th Eurogroup is also widely expected to give the green light for the **disbursement of the next loan tranche to Greece**, which is deemed crucial for avoiding unforeseen State funding problems.

November 30, 2011: Italy has €8.8bn in 6-month T-bills redemption

Early December, 2011: French President Nickolas Sarkozy and German Chancellor Angela Merkel to present joint proposals to enforce EU budget rules. In a closely-watched meeting in Strasburg earlier this week, President Nicolas Sarkozy, German Chancellor Angela Merkel and newly appointed Italian Prime Minister Mario Monti discussed, among others, possible changes to EU Treaty aiming to enhance fiscal discipline among member states. At a joint press conference following the conclusion of the meeting, the French President and the German Chancellor pledged to present proposals for EU Treaty modifications before the December 9 EU Summit. The Merkel-Sarkozy-Monti meeting in Strasburg earlier this month came on the heels of a number of new proposals made by the European Commission to further strengthen budgetary surveillance in the euro area. Among others, these included: a) the submission of new national draft budgets to the European Commission by mid-October each year; b) the use of independent macroeconomic forecasts for the drafting of new budgets; c) closer monitoring of countries which break EU budget rules or risk being cut off from international markets; and d) the inclusion of fiscal rules into national legislation (preferably the constitution).The German Chancellor has repeatedly stressed in recent weeks that certain changes are required in the European Treaty so as to pave the way for closer European integration, address the lingering debt crisis and restore market confidence. According to a number of reports, under the German proposals the EU would have the right to interfere in national budgets in cases they violate EU budget rules. Furthermore, delinquent governments could face sanctions by the European Court of Justice, with their budgets risking to be declared void. Germany reportedly wants potential EU Treaty amendments to be ratified by all 27 EU national parliaments by end-2012 at the latest.

December 1, 2011: France has €7.11bn in T-bills redemption

December 1, 2011: Strikes in Greece. GSEE (the General Confederation of Greek Workers) and ADEDY (the Civil Servants' Confederation) trade unions are due to hold a one-day strike to protest against the 2012 Budget.

December 7, 2011: Greek parliament votes on the 2012 Budget. Approval of the new budget in Parliament is a key prerequisite for the implementation of the new bailout package for Greece agreed at the October 26-27th EU Summit (a more thorough analysis regarding the 2012 Budget can be found in Eurobank EFG Research, Greece Macro Monitor: 2012 Budget: Main Targets & Assessment, November 22, 2011,

http://www.eurobank.gr/Uploads/Reports/FOCUSGreece%20November%2022%202011ii.pdf)

December 8, 2011: France has €9.43bn in T-bills redemption

December 8, 2011: ECB policy meeting. In view of Eurozone's deteriorating economic growth outlook and mounting tensions in financial markets, a further 25bps cut in the key 1wk repo rate can not be ruled out. Recent readings in a range of high-frequency real activity and sentiment indicators from a number of euro area member states (including Germany and France) signal a sharp slowdown in the pace of economic activity in recent months. These also seem to be in line with comments made by ECB President Mario Draghi at the press conference accompanying the last policy meeting in early November. Mr. Draghi noted back then that the Eurozone economy may be heading towards a "mild recession" by the end of the year. In an effort to help stabilise interbank money market, the ECB is also likely to take new initiatives to ease liquidity strains. Reportedly, options under consideration include, among others, plans to relax collateral rules for liquidity operations and/or funding to banks with loan tenors extended to two or three years, from a maximum of 13-months, presently.

December 9, 2011: European Council (last scheduled summit for 2011). European Council President Herman Van Rompuy is expected to deliver proposals on limited EU Treaty changes, aiming to enhance economic policy coordination. High level EU officials have recently expressed certain reservation over idea of implementing Treaty amendments on the basis that potential changes would need to be approved by national parliaments in EU-27, a process that could turned out to be lengthy and unpredictable.

December 12, 2011: Team of senior troika inspectors arrives in Athens to commence talks with the new government on the new bailout package for Greece agreed at the October 26-27 EU Summit. According to Greek Finance Minister Evaggelos Venizelos, both the new rescue deal and the corresponding implementation measures supporting the package are planned to be approved by the Greek Parliament by the end of January 2012. Reportedly, the debt exchange with private investors is also expected to have been completed by that time. In the meantime, the government should try to complete negotiations with private sector investors on the terms of the new PSI by the end of this year. According to a finance ministry statement earlier this month, the Greek authorities already initiated consultations with private-sector bond holders through the IIF, other industry bodies and directly. A more thorough analysis regarding the impact of the new PSI on improved terms on official loans on Greece's borrowing needs and debt sustainability can be found in Eurobank EFG Research, Greece: Debt sustainability outlook post the Oct. 26th EU Summit, October 31, 2011,

http://www.eurobank.gr/Uploads/Reports/31%2010%2011%20Greece%20Debt%20Sustainability%20Outlook.pdf)

December 13, 2011. Spanish parliament reconvenes. Spanish centre-right opposition People's Party defeated the Socialist government and secured a crushing election victory last Sunday, as widely anticipated. Specifically, the People's Party, which has vowed to push through drastic austerity measures, won 186 seats in the 350-seat lower house or 44.6% of the votes, up from 154 in previous elections. The Socialist party dropped to 110 seats or 28.7% of the votes from 169 in the outgoing parliament. According to an updated round of forecasts published earlier this month, the European Commission revised lower its 2011 and 2012 real GDP projections for the Spanish economy to 0.7%, from 0.8% and 1.5% previously. The EC also reviserd its 2011 and 2012 budget deficit forecasts for Spain to 6.6%-of-GDP and 5.9%-of-GDP respectively, from 6.3% and 5.3% reported in Spring 2011.

December 15, 2011: Italy has €7.0bn in 6-month and €4.16bn in 12-month T-bills redemptions

December 15, 2011: France has €7.01bn in T-bills redemption

December 16, 2011. Greece has €2.0bn in 26-wk T-bills redemption. According to recent press reports quoting finance ministry sources, Greece has enough cash reserves to meet its funding needs until mid-December 2011.

December 19, 2011. €1.17bn in 3-year Greek government bonds mature

December 20, 2011: ECB longer-term refinancing operations announcement date. This is the second of the two longer-term refinancing operations LTROs the ECB announced at the October 6 policy meeting aiming to ease stresses in bank-funding markets. This liquidity tender will have a maturity of approximately 13 months and the allotment date is 21 December. The operations will be conducted as fixed rate tender procedures with full allotment.

December 22, 2011. €979.6mn in 1-year zero coupon Greek government bonds mature

December 22, 2011: France has €8.81bn in T-bills redemption

December 23, 2011: Greece has €2.0bn in 13-wk T-bills redemption

December 27, 2011: Italy has €2.5bn in 3-month T-bills redemption

December 29, 2011: France has €4.61bn in T-bills redemption

December 30, 2011: Italy has €8.8bn in 6-month T-bills redemption

<u>December 30, 2011:</u> €714.7mn in 1-year Greek zero-coupon bonds mature

Table 2: Greece-Key Indicators	Last	ytd	2010	2009
Macroeconomic indicators				
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
Consumer-vigor indicators				
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
Industrial-activity indicators				
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
Construction sector & other investment-activity indicators				
Gross 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
Balance-of-Payments statistics *(€-terms)*				
Tourism revenues (% YoY-cumulative ytd)	7.1 (Sept. 11)	9.5	-7.6	-10.6
Transportation revenues (% YoY-cumulative ytd)	-5.3 (Sept 11)	-10.8	13.8	-29.4
Customs-based statistics *(€ - terms)*				
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
Domestic MFI credit to domestic enterprises & households *(outstanding balances and net flows)*				
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
Private-sector credit outstanding (% GDP)**				
Total domestic enterprices & 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 (€ 230bn) and 2011 (€ 226bn) were used.*

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