IPOL | DIRECTORATE-GENERAL FOR INTERNAL POLICIES
EGOV | ECONOMIC GOVERNANCE SUPPORT UNIT

IN-DEPTH ANALYSIS

Greece's financial assistance programme (March 2017)

This briefing provides an overview of the economic situation in Greece and the main elements of the third financial assistance programme. This briefing is regularly updated (this version replaces the version published on 29 September 2016).

Summary

- Greece's economic output remained flat in 2016 (-0.04%), following a larger-than-expected drop in the last quarter of the year on the back of uncertainties linked to the completion of the second review under the third financial assistance programme. Looking ahead, the Commission (COM) expects in its Winter 2017 forecast that Greece's GDP rebounds by 2.7% in 2017 and 3.1% in 2018, conditional on programme implementation, mainly reflecting expansion in domestic demand on the back of improving financing conditions as capital controls are gradually eased.
- The second programme review is ongoing since October 2016. Greece has so far received €31.7 billion under the current programme (and paid back €2 billion following the sale of an asset by one bank that took part in the 2015 banking recapitalisation). Short-term debt relief measures were endorsed by the Eurogroup in December 2016 and adopted by the ESM on 23 January 2017. In February 2017, the Eurogroup welcomed a common understanding on outstanding issues (including the medium-term fiscal strategy and labour market reform) reached between the Greek authorities and the institutions, allowing the review mission (under the second review) to return to Athens and resume work in order to conclude a staff-level agreement on policy reforms; such an agreement is necessary for the successful conclusion of the review and therefore for receiving financial support. The Eurogroup President stated after the February Eurogroup that the institutions will work with the Greek authorities on the additional package of structural reforms, looking at the tax system, the pensions system, also labour market regulation.
- The IMF published recently a revised Debt Sustainability Analysis (DSA), and concluded that the Greek public debt is unsustainable. The latest DSA published by the COM is of June 2016. According to the European Stability Mechanism (ESM), and as a result of the short-term debt relief measures adopted in January 2017, the Greek debt is sustainable. The analyses differ substantially, mainly because of the assumptions at the basis of the projections; such differences affect the possible financial participation of the IMF in the programme.
- The reinstatement of the waiver in June 2016 regarding the eligibility of Greek government bonds as collateral in Eurosystem monetary policy operations enables Greek banks to swap costly Emergency Liquidity Assistance (ELA) refinancing for regular ECB funding. In February 2017, the ELA ceiling stands at approximately 50% of the level set in August 2015.

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1. Latest economic developments

Greece's economy unexpectedly contracted in the last quarter of 2016, as recovery struggles to gather momentum on the back of protracted uncertainty surrounding the completion of the second review. According to the latest Eurostat's estimate (7 March 2017), the Greek economy sharply contracted by 1.2% (q-o-q) in the last quarter of 2016 - that is three times more compared to the Flash Estimate released three weeks earlier. This larger-than-expected drop reflects declines in both private and government consumption as well as shrinking exports, the Hellenic Statistical Authority (ELSTAT) said. As a consequence, and contrary to the February 2017 Flash estimate which indicated a return to growth, **the Greek economic output remained almost unchanged in 2016 (-0.04%)**, somewhat below the latest estimations from both the COM and the IMF, as evidenced in Table 1. The COM notes in its Winter 2017 forecast that the Greek economy has been coping with a negative impact of capital controls[1] and delays in the completion of the first two reviews under the third financial assistance programme that added to uncertainty. On the other hand, the ECB's decision to reinstate the waiver for Greece's government bonds on 22 June 2016 has helped improving the liquidity situation of the Greek banks[2]. The fragility of earlier prospects of recovery is visible from a very volatile profile of quarterly GDP data: after contracting broadly in line with market expectations in Q1 2016, GDP data surprised on the upside during Q2 and Q3 2016 (with two quarters of positive growth) before contracting again and more than expected in Q4 2016. It is worth to mention that Greek GDP data is subject to frequent and large revisions (see Table 2).

Table 1: Comparison of the Commission and the IMF 2016 growth forecasts for Greece

	2016	2017
Eurostat March 2017 Estimate	**-0.1**	-
COM Spring 2016 Forecast (May 2016)	-0.3	2.7
COM Autumn 2016 Forecast (November 2016)	-0.3	2.7
COM Winter 2017 Forecast (February 2017)	0.3	2.7
IMF April 2016 WEO	-0.6	2.7
IMF October 2016 WEO	0.1	2.8
IMF February 2017 Article IV Report	0.4	2.7

Source: EGOV calculations based on Eurostat; the Commission and the IMF forecasts.

Table 2: Revisions in Greece's quarterly 2016 GDP data (% compared to the previous quarter)

2016	Flash estimate Q1 2016 May 2016	Estimate Q1 2016 June 2016	Flash estimate Q2 2016 August 2016	Estimate Q2 2016 September 2016	Flash estimate Q3 2016 November 2016	Estimate Q3 2016 December 2016	Flash estimate Q4 2016 February 2017	Estimate Q4 2016 March 2017
Q1	-0.4	-0.5	-0.1	-0.2	-0.6	-0.6	-0.6	-0.7
Q2	-	-	0.3	0.2	0.3	0.4	0.3	0.3
Q3	-	-	-		0.5	0.8	0.9	0.6
Q4	-	-	-	-	-	-	-0.4	-1.2

Source: EGOV based on Eurostat.

[1] On 29 June 2015, the Greek Government imposed capital controls to avert a collapse of its banking system. These controls have been progressively eased, in a series of steps, since 20 July 2015.

[2] On 22 June 2016, the ECB reinstated the waiver of minimum credit rating requirements for marketable instruments issued or guaranteed by the Hellenic Republic, subject to special haircuts. This means that these instruments may be used as collateral in Eurosystem monetary policy operations (i.e. allowing Greek financial institutions to access cheaper central bank money compared to the emergency funds under the ELA). The waiver has been applicable from the main refinancing operation settled on 29 June 2016. As of February 2017, ELA ceiling was reduced to EUR 46.3 billion, reflecting "*an improvement of the liquidity situation of Greek banks, amid a reduction of uncertainty and the stabilization of private sector deposits flows*". However, public sector securities are currently not eligible for the ECB's public sector purchase programme (PSPP), which is one of the components of the ECB's expanded asset purchase programme (APP).

Looking ahead, the COM expects in its latest vintage of projections (Winter 2017) that Greece's economy grows by robust 2.7% in 2017 and 3.1% in 2018, conditional on programme implementation, mainly reflecting further expansion in domestic demand on the back of improving financing conditions as capital controls are gradually eased. Uncertainties linked to the completion of the second review and a set of external factors (geopolitical as well as international and regional economic tensions, including the refugee crisis) are the main downside risks to this growth outlook.

Price declines reversed in the course of 2016 on the back of increases in indirect taxes and energy prices. Annual inflation, as measured by Harmonised Index of Consumer Prices (HICP) came in at 0.0% in 2016, after three years of negative readings in a row. Underlying price pressures gathered some momentum but still remain subdued overall[3]. According to the latest Eurostat data, headline inflation stood at 0.3% (y-o-y) in December 2016. For 2017 and 2018, the COM foresees a moderate increase in the inflation rate, to 1.3% and 1.0% respectively, as domestic demand further strengthens.

Greece's current account balance stood at 0.0% of GDP in 2015, extending a positive trend observed since 2008 when it reached a record high deficit of 15.8% of GDP[4]. This remarkable adjustment was initially driven by sharp decline in imports as the economy entered into unprecedented recession before structural reforms put into place have gradually improved external competitiveness. **For 2016, the COM expects Greece to run a slight current account deficit of 0.7% of GDP**, mainly driven by a projected reversal in trade balance following a decrease in net exports of services while net imports of goods remained broadly unchanged. Greece is projected to continue earning less from its international export transactions than spending abroad from import transactions with the rest of the world in 2017 and 2018, though current account deficit is set to remain little changed relative to the size of the economy at 0.7% of GDP and 0.6% of GDP respectively.

After peaking at 27.5% in 2013, the unemployment rate is projected to decline to 23.4% in 2016 reflecting the impact of past labour market reforms, including employment schemes promoting labour participation, as well as the Greek economy's gradual return to growth. However, Greece has still the highest unemployment rate within the EU countries. The latest available monthly data show that the unemployment rate stood at 23.0% in November 2016. Unemployment continued to mainly affect young people[5] and women[6]. According to the Winter 2017 COM forecast, Greece's unemployment rate is to further decrease to 22.0% in 2017 and 20.3% in 2018.

In its Winter 2017 forecast, the COM projects that **Greece's general government deficit narrows to 1.1% of GDP in 2016, as the primary surplus is set to exceed the target of 0.5% of GDP established under the ESM programme[7].** The COM also expects that Greece over-achieves this target by about 1.5 p.p. of GDP, reflecting stronger-than-expected tax revenues (mainly from indirect taxes and the corporate income tax following the adoption of a series of fiscal measures[8] in the context

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[3] Underlying inflation, as measured by headline HICP excluding unprocessed food and energy, rose to 0.7% in 2016, up from 0.1% in 2015, mainly reflecting price increases of processed food as well as of services related to transport, health and restaurants and hotels.

[4] Last time Greece's current account recorded a surplus was in 1994 (+1.3% of GDP).

[5] The youth unemployment rate declined from a record high of 60.5 % in February 2013 to 45.7% in November 2016. In this regard, a European Parliament study "Employment and social developments in Greece" showed that '*unemployment and poverty mostly hit younger people for whom a system focused on pensions offers no help*'. At the same time, this study concluded that actions agreed under the third economic adjustment programme aim at completing the unfinished reform agenda since 2010, while addressing criticism related to earlier programmes.

[6] In November 2016, the unemployment rate among women came in at 27.5% as compared to 19.4% for men.

[7] Under the ESM programme, primary surplus target is set in terms of primary balance, excluding one-off costs of bank recapitalisations, SMP and ANFA revenues as well as part of privatisation proceeds.

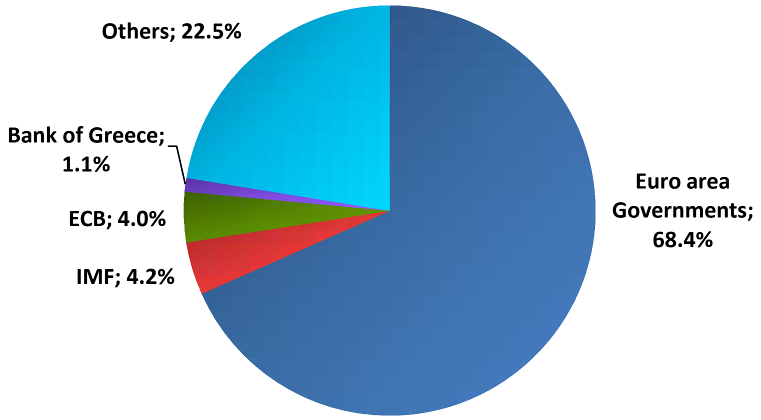
[8] According to the COM, these fiscal consolidation measures are worth about 3% of GDP through 2018.

of the first review under the third programme) as well as several one-off factors (including clearing of past tax liabilities). Note that Prime Minister Tsipras announced a one-off payment to low-income pensioners in December 2016 worth about EUR 600 million[9] financed from the higher-than-expected primary budget surplus. Looking ahead, assuming a successful completion of the second review of the ESM programme, the COM projects that Greece's general government deficit stabilises at 1.1% of GDP in 2017 before turning into surplus in 2018 as the Greek authorities are expected to ensure that the 2018 target for primary surplus (3.5% of GDP) is complied with.

Greece's general government gross debt stood at 176.9% of GDP in the third quarter of 2016, virtually unchanged from the level registered at the end of 2015. However, this data do not take into account the latest disbursement of ESM funds to Greece on 26 October 2016 (EUR 2.8 billion). According to the latest COM forecast, debt-to-GDP ratio is to peak at 179.7% in 2016, before declining to 177.2% of GDP in 2017 and 170.6% in 2018, reflecting "*improved fiscal position and stronger GDP growth*"[10].

The **distribution of the outstanding debt across different categories of bondholders** is depicted in Figure 1. Based on consolidated data published by Eurostat, Greece general government gross debt amounted to EUR 311.16 billion by the end of the third quarter of 2016. This figure shows that the Euro area governments (including EFSF and ESM) held more than two thirds of Greece's debt outstanding at the end of the third quarter of 2016 (68.4%, + 2.5 p.p. compared to the end of 2015). On the other hand, shares of the Greek debt held by the ECB, the IMF and the Bank of Greece have declined to 4.0%, 4.2% and 1.1% respectively (namely -0.7 p.p., -1.0 p.p. and -0.1 p.p. compared to the end of 2015).

Figure 1: Greece's general government gross debt by holder as of 30 September 2016



Source: EGOV calculations based on COM, IMF, ECB and PDMA (Greece's Public Debt Management Agency).
Note: The share held by euro area governments comprises EFSF, ESM and bilateral loans.

[9] This spending measure was announced by Prime Minister Tsipras without prior consultation with the lenders. He also pledged to freeze a planned VAT increase for selected Aegean Islands that were particularly impacted by the refugee crisis. In a letter to the Eurogroup President and the ESM Managing Director of 28 December 2016, Finance Minister Tsakalotos clarified that this VAT measure "*is limited to 2017 only and is fully funded in the 2017 budget*".

[10] According to a press report, Greece is to appoint Rothschild to advise it on "*all areas connected to its debt, including negotiations with creditors, potential inclusion in the ECB's* [APP] *programme and the resumption of Greek government bond sales*".

Box 1: Statistical governance in Greece

In **January/February 2017**, Eurostat visited ELSTAT in the framework of the regular meetings within the Excessive Deficit procedure; in order to promote transparency, ELSTAT also invited the COM, the ECB and the IMF as observers to these recent meetings.

On **22 November 2016**, at a meeting of the Financial Assistance Working Group (FAWG) of the EP, the Director General of Eurostat, *W. Radermarcher* and the former Head of ELSTAT, *A. Georgiou*, presented the situation of official statistics in Greece as well as the legal proceedings before the Greek courts against Mr. Georgiou on the ground of the accusation that he inflated 2009 Greek deficit figures (for more details on the case, see separate EGOV briefing):

- Mr. Radermacher highlighted the **important contribution** of Mr. Georgiou in ELSTAT since he modernised the latter and brought trust in every day's governance and full observance of EU statistical means. He stated that it is **misleading** to present the serious misreporting of EDP in 2009 as the cause of the economic crisis; it is rather a most blatant symptom of very serious fault and methodological obsolescence in parts of the Greek statistical administration at that time.
- Mr. Radermacher also stated that the situation in Greek statistics now is not comparable with the year of 2009. The weaknesses in the Greek statistical system are now of **technical nature** (e.g in implementation, capacity and skills) and not like the deliberate false deficit reporting until 2009.
- Mr **Georgiou referred** to the numerous prosecutions and investigations against him that have been going on for years. He stressed that if official statisticians cannot keep accurate official statistics without fear of being attacked and dragged through the courts for years, the integrity of the EU and its economic system is critically undermined.
- The state of play regarding the legal proceedings against Mr Georgiou is that on **18 November 2016**, Prosecutor Ioannis Koutras proposed that Mr. Georgiou should not stand trial for allegedly tampering with Greece's 2009 deficit figure, since no evidence was found to support that the 2009 deficit of Greece was artificially inflated by Georgiou with the intention to harm the Greek State. The final decision in the case will be made by the Appeals Justices' Council.

In **August 2016**, the COM expressed concerns regarding statements calling into question the quality of official statistics in Greece. It called upon the Greek authorities to actively and publicly challenge the false impression that data were manipulated during 2010-2015 and to protect ELSTAT and its staff from such unfounded claims. It also urges the Greek authorities to support and preserve the quality of Greek statistics, as well as the independence of the Hellenic Statistical System, along the lines defined in Greek statistical legislation and in the Commitment on Confidence in Statistics of 2012. A letter signed by Vice-President Dombrovskis, Commissioner Moscovici and Commissioner Thyssen was sent in this regard to Greek Minister of Finance, Euclid Tsakalotos.

EU National statistical institutes, supported by the European Statistical Governance Advisory Board (ESGAB) issued in **May 2015** the following statement *"(...) we confirm our concern with regard to the situation in Greece, where the statistical institute, ELSTAT, as well as some of its staff members, including the current President of ELSTAT, continue to be questioned in their professional capacity. We acknowledge the **clear improvements within the Greek statistical system** that have been achieved during the past five years, illustrated notably by Eurostat's consistent publication of Greek deficit and debt data without reservations nor amendments since November 2010. However, we are aware that **ELSTAT still has many challenges to face** to maintain the institution's independence given the above-mentioned political debates and judicial proceedings and the forthcoming recruitment of a new President of ELSTAT. We welcome, therefore, the reinforced provisions on professional independence in Regulation (EC) No 223/2009 whereby the recruitment of the new President must follow a transparent procedure and be based on professional criteria only."*

The above statement of May 2015 was made against the background of an ESGAB Opinion of **April 2015** on the implementation of the Hellenic Statistical Law (3832/2010) and Greece's commitment on confidence in statistics. ESGAB recognised in this opinion considerable progress since 2009, highlighting a number of concerns, inter alia that the principle of professional independence must be implemented in practice, that the Greek Government's commitment on confidence in statistics must be respected and put into practice, particularly in relation to ensuring institutional independence and providing adequate financial and other resources.

2. Main elements of the third programme

Following Greece's request for further financial assistance of 9 July 2015, the COM signed on 19 August 2015[11] (on behalf of the members of the euro area) **a Memorandum of Understanding (MoU) with Greece for a third economic adjustment programme of up to EUR 86 billion for the period 2015-18** [12] (Article 13 of the ESM Treaty). In particular, it outlines a reform agenda in the following areas: (1) fiscal sustainability; (2) safeguarding financial stability; (3) growth, competitiveness, investment; and (4) modern state and public administration structure. Greece is to cooperate with the COM's Structural Reform Support Service to demonstrate its commitment.

The Greek authorities have made a commitment to achieve a **primary surplus** (revenues less expenses without interests' payments) **over the medium-term of 3.5 % of GDP,** so as to progressively strengthen the sustainability of public finances (see Table 3 below).

Table 3: Primary surplus targets and GDP growth path underpinning the third financial assistance programme to Greece

Year	Primary surplus target	GDP growth
2015	-0.25%	-2.3%
2016	+0.50%	-1.3%
2017	+1.75%	+2.7%
2018	+3.50%	+3.1%

Sources: MoU and EU DSA of July 2015 (also included in the COM eligibility report of 10 July 2015) .

The primary surplus targets (for 2015-2018) and GDP assumptions (for 2017-2018) were not revised between July 2015 and the updated debt sustainability analysis (DSA) of June 2016 (part of the "compliance report", see also chapter 4 of this briefing). The updated DSA has only a higher growth assumption for 2016 (-0.3% compared to -1.3% in the original DSA); actual estimated growth in 2016 is higher (-0.04%, see first chapter above).

In accordance with the MoU, the primary surplus targets are to be achieved by:

- **Pension savings** (see pp. 13-14 of the MoU);
- **Health care sector:** various measures (see pp. 15-16 of the MoU);
- **Tax, revenue, and financial management reforms**, including various measures against tax fraud and evasion. A minimum VAT income of EUR 2.65 billion is to be ensured. Property tax rates will be aligned with market prices from 2017 and zonal property values are to be revised. The authorities are to improve the collection of tax debt, introduce independent agencies and make the Fiscal Council independent and operational. Many other tax related reform measures are included in the MoU (see pp. 6-11 of the MoU).

In addition, Greece was requested to enact, by October 2015, **structural measures expected to yield at least 0.75 % of GDP coming into effect in 2017 and 0.25 % of GDP in 2018**, so as to help

[11] On 19 August, the Greek Prime Minister also sent a letter to the European Parliament requesting its stronger involvement in the regular review process in implementing the programme. A day later, he resigned, triggering the sixth general elections in eight years on 20 September 2015. Following his re-election, PM Tsipras (Syriza) has renewed his party's coalition with the nationalist Independent Greeks (Anel), the junior partner in his previous government.

[12] According to Article 7.2 of Regulation (EU) No 472/2013, the Council shall, on a proposal by the Commission, approve the macroeconomic adjustment programme prepared by the Member State requesting financial assistance.

achieve medium-term budgetary targets. The measures would include, inter alia, defence expenditure savings, personal income tax reform and the freezing of public spending.

The Greek authorities have made a commitment to finalise a **strategy for the monitoring of the financial system**, aimed at (i) normalising liquidity and payment conditions, (ii) recapitalising the banks, (iii) enhancing governance and (iv) addressing non-performing loans (NPL). All banks are required to submit quarterly funding plans to the Bank of Greece (BoG), and a buffer of up to EUR 25 billion was set aside to address potential recapitalisation needs and resolution of banks.

The Government has also made a commitment to review all labour market institutions, adopt an integrated action plan to fight undeclared and under-declared work, expand vocational education and training, increase the capacity of the Ministry of Labour, open restricted professions, reduce the administrative burden of companies based on OECD recommendations, facilitate trade, improve EU funds absorption for agriculture and reform the electricity and the gas markets.

Proceeds from privatisation (e.g. of national and regional airports, harbours, energy providers, railway services, telecommunication providers) are to help reduce the Government's financing needs. The implementation of the Asset Development Plan (ADP) is expected to generate EUR 1.4 billion in 2015, EUR 3.7 billion in 2016 and EUR 1.3 billion in 2017. **A new independent guarantee fund is to be established and have in its possession valuable Greek assets.** An independent Task Force[13] will identify potential assets as well as the best options for their monetisation, so as to help in the repayment of ESM loans. The fund is foreseen to generate about EUR 50 billion, of which the first EUR 25 billion are to be attributed to the repayment of the recapitalisation of banks, while the remaining proceeds are to be used for debt reduction and investments in the same proportions (up to EUR 12.5 billion each).

A comprehensive three-year strategy was to be defined by December 2015 (in agreement with the COM) for **the reorganisation of administrative structures**, involving the rationalisation of administrative processes, the optimisation of human resources, the strengthening of transparency and accountability, the introduction of e-government and the formulation and implementation of a communication strategy.

3. Latest developments under the third adjustment programme

On 9 June 2016, the COM published a report on the compliance with the MoU upon **conclusion of the first review under the third programme**, including an update of the DSA. The report provided an overall positive assessment of Greece’s programme implementation, stating: “*On the basis of this analysis of compliance with the MoU, the ESM programme is broadly on track paving the way for the next disbursement to Greece of an amount necessary to cover the outstanding debt service until the expected completion of the next review, and an amount to help clear the sizeable stock of arrears in line with an agreed clearance plan*”.

The ESM authorised in **June 2016** the second tranche of EUR 10.3 billion. This tranche was paid in several disbursements:
(1) The first sub-tranche of €7.5 billion was disbursed on **21 June 2016**; within this sub-tranche €5.7 billion were to cover debt service needs and €1.8 billion to clear part of domestic arrears;

[13] The mandate and composition of this Task Force is to be defined by the Greek authorities, in agreement with the European institutions and in consultation with the Eurogroup.

(2) The remaining sub-tranches of altogether €2.8 billion were disbursed in **October 2016**; €1.1 billion (for debt servicing) were disbursed since Greece implemented a set of fifteen milestones (i.a. on pensions and bank governance) and €1.7 billion were disbursed after the clearance of net arrears by Greece. Altogether, Greece has so far **received €31.7 billion from the current programme**.

A Supplemental Memorandum of Understanding (sMoU) updating the policy conditionality set out in the MoU of August 2015 was published on 16 June 2016. **It inter alia presents fifteen key deliverables to be delivered between mid-September 2016 and September 2017** (measures nr. 41-56 in the chapter 6 of the compliance report of June 2016). The sMoU also states that the Greek authorities commit to ensuring sustainable public finances by pursuing the fiscal path agreed in August 2015 that was based on primary surplus targets of 0.5, 1.75 and 3.5 percent of GDP in 2016, 2017 and 2018 respectively. Furthermore, the programme definition of the primary balance will be adjusted to exclude migration-related expenditure net of EU transfers to the Greek budget subject to a proper monitoring mechanism and a cap being defined. To meet the fiscal targets, as a prior action the Government will adopt supporting legislation generating savings equivalent to ¾, 2¼ and 3 percent of GDP in 2016, 2017 and 2018 respectively through parametric measures, including a holistic pension reform.

On 9 September 2016, the Eurogroup concluded that representatives of the institutions should return to Athens to prepare the **start of the second programme review in October.**

On 5 December 2016, Mr Pedro Martins, Professor from the London School of Business and Management in London and a member of the "**Expert Group for the review of the Greek labour market institutions**" to present to the European Parliament the recommendations adopted by the expert group on 27 September 2016.

On 21 December 2016 the European Court of Justice (Judgment in Case C-201/15) ruled in respect of a case related to Greek labour legislation that **EU law does not, in principle, prevent a Member State from opposing collective redundancies in certain circumstances in the interests of the protection of workers and of employmen**t. However, under such national legislation, which must in that case seek to reconcile and strike a fair balance between, on the one hand, the protection of workers and of employment and, on the other, employers' freedom of establishment and their freedom to conduct a business, **the legal criteria which the competent authority is to apply in order to be able to oppose projected collective redundancies cannot be formulated in general and imprecise terms**.

Short-term debt relief measures were endorsed by the Eurogroup in December 2016 and adopted by the ESM on 23 January 2017. The December Eurogroup also welcomed the agreement on a 2017 budget which confirms the primary balance target of 1.75% of GDP and which allows for the national rollout of the Guaranteed Minimum Income; it noted that a staff-level agreement should include measures to reach the fiscal target for 2018 (primary balance of 3.5% of GDP), as well as reforms enhancing growth and competitiveness. In its "Explainer of the Short term relief measures for Greece", the ESM states that "*When implemented in full, these measures should lead to a cumulative reduction of Greece's debt-to-GDP ratio of 20 percentage points until 2016, according to ESM estimates in a baseline scenario. It is also expected that Greece's gross financing needs will fall by almost five percentage points over the same time horizon*". However, the ESM does not provide detailed information on its analysis, the assumptions of the model or the specific path of the debt indicators.

On 20 February 2017, Greece paid back €2 billion to the ESM following the sale of an asset by one of the banks that took part in the 2015 banking recapitalisation, financed with ESM loans.

On 20 February 2017, the Eurogroup welcomed a common understanding on outstanding issues (the main outstanding issues include the medium-term fiscal strategy and labour market reform) reached between the Greek authorities and the institutions, **allowing in the context of the ongoing second programme review the European institutions to return to Athens and resume work in order to conclude a staff-level agreement on policy reforms**. A staff-level agreement is a necessary condition for the successful conclusion of reviews and therefore for receiving financial support.

The Eurogroup President stated after the February 2017 meeting that the institutions will work with the Greek authorities on the **additional package of structural reforms, looking at the tax system, the pensions system, also labour market regulation**: "*There will be a change in the policy mix, moving away from austerity and putting more emphasis on deep reforms, which has also been a key element for the IMF. So that is I think a good step and we have to realize that there is no agreement, there is no political agreement at this point, as that would be too early. It is a very positive and good step that the institutions have enough confidence and a common agreement to go back to Athens.*" He also added that there is no liquidity issue in the short run for Greece, while stressing "*But I think we all feel a sense of urgency because of the key issue of confidence. If you want economic growth in Greece to continue and to start picking up, confidence is a key factor. That confidence has been returning in the last year and needs to strengthen, and we don't want to jeopardize that*."

The **second review mission resumed on 28 February 2017**. The managing Director of the ESM stated in an interview on 6 March 2017: "*I'm not excluding the possibility that everything is ready by the next Eurogroup on 20 March, but we are not at all certain. We still have a lot of work to do. We need to see how much progress will be made in the next two weeks*"; "*We always find solutions in the end*" and "*Remaining steps on the fiscal consolidation side are very small*.

Box 2: Ex post evaluation on the role of the IMF in Greece

In February 2017, the IMF published its ex-post evaluation of the second Greek program (called "Exceptional access under the 2012 extended arrangement under the Extended Fund Facility - EFF"). The report derives a number of lessons:

- When the political base for reforms is fragile, or insufficient ownership is apparent or likely, program design should be more conservative from the start.
- Delays in addressing non-performing loans (NPLs), private sector insolvency frameworks, and governance issues in the banking sector weighed on the recovery, and steadfast implementation of reforms in these areas should be given high priority.
- Contrary to the initial program design, the quality of fiscal adjustment measures was weak. The initially agreed strong measures were replaced with ad hoc measures. Going forward, broadbased taxes, strong enforcement of tax compliance, pension reform, and development of targeted social safety nets are particularly important for making adjustment more durable and equitable.
- Greece needs to re-invigorate stalled structural reforms, including in the areas of product, service and labour markets to remain a viable euro area member. Securing strong ownership is key.
- Upfront commitments of debt relief which delivers debt sustainability based on a realistic target for the medium-term primary fiscal surplus are a prerequisite for program success in Greece.
- There is merit in formalizing the operational framework for Fund collaboration with monetary unions in the program context to clarify a number of issues, including information-sharing and assurances regarding union-wide policies affecting program member countries.
- Certain Fund policies would benefit from a fresh discussion, including risk acceptance guidelines and the requirements for meeting the exceptional access criterion on prospects for program success.

On 9 March 2017 (according to information in the public domain) the institutions said that "*Important progress has been made on a balanced fiscal package for the post-program period and a number of key reforms, notably in the financial sector. Follow up meetings have been scheduled for the next week in advance of the Eurogroup on March 20. The aim is to rapidly conclude a staff-level agreement.*" According to these sources, the main open issues are the size of the package of measures for 2019 onwards, labour reforms and some of the countermeasures proposed by the Greek government.

4. Debt Sustainability Analyses

Article 13.1 of the ESM Treaty, as well as Article 6 of EU Regulation (EU) No 472/2013 on surveillance of Member States with serious difficulties with respect to financial stability, requires the COM to assess whether the public debt of a Member State requesting financial assistance is sustainable. Similarly, Article V.3 of the IMF agreements, that sets the conditions governing the use of IMF resources, requires that the receiving country have the capacity to repay its debt to IMF.

The IMF and the COM publish their own DSA for Greece. The analyses differ substantially, not only for the assumptions of the projections, but also for the methodological framework. However, both analyses provide a path for the evolution of the two main indicators used to assess the debt sustainability, namely the **Debt-to-GDP** ratio and the **Gross Financing Needs-to-GDP** ratio (GFN), and extend the projections up to 2060.

The EU institutions have a significantly more optimistic baseline scenario than the IMF: this is due to the assumptions on nominal growth, on the primary balance and (to a lesser extent) on privatization receipts and bank recapitalisation needs. As a result, **debt relief needs are significantly smaller under the EU scenario.**

Box 4: Public Debt Sustainability Analysis

The Debt Sustainability Analysis (DSA) is an analytical framework that helps assessing a country's capacity to service its public debt over time, while financing its policy objectives without compromising its stability.

To this end, **two indicators** are typically used:

- The general government **Debt-to-GDP** ratio, which provides an overall measure of the country's debt compared to the size of its economy;
- The general government **Gross Financing Needs-to-GDP (GFN-to-GDP)**, which quantifies the country's debt payment obligations (principal plus interests), in relation to its economy. This indicator takes into account the debt structure (i.e. maturity, interest rates and interest deferrals).

The two indicators are interrelated, though the GFN-to-GDP ratio seems to better capture the country's short- and medium-term financial stability risks. In fact, low financing needs are generally associated with lower debt rollover and thereby reduced financial stability risks, and *vice versa*.

In practice, it is difficult to establish **numerical thresholds for debt sustainability**. As to the debt-to-GDP ratio, thresholds appear to vary across countries, depending on macroeconomic fundamentals and debt management capacities (e.g. Argentina defaulted when its debt was around 60% of GDP, while Japan continues to sustain debt of more than 200% of GDP). The IMF benchmark is set at 85%.

Regarding the GFN-to-GDP indicator, the IMF guidelines (p. 32) indicate that the ratio would need to remain below 15%-20% to ensure debt sustainability.

The **DSAs** are essentially constituted of projections and forecasts for the relevant economic indicators. As with all forecasts and projections, they are based on models and assumptions that vary across institutions and time. The IMF and the Commission have developed their own methodological frameworks, which include a "**baseline scenario**" as well as "**alternative scenarios**" that are built up under different assumptions regarding policy variables, macroeconomic developments, and financial conditions.

The COM published its latest DSA on 16 June 2016, as part of a "compliance report". The main assumptions of the COM' analysis were:

- real **GDP growth** is expected to be -0.3% in 2016, 2.7% in 2017 and 3.1% in 2018. The assumed annual growth amounts to 1.5% after 2021 and to 1.25% after 2030;
- the expected **primary surplus** is 0.5% in 2016, 1.75% in 2017 and 3.5% from 2018 until 2030, and decline to 1.5% by 2040;
- as regards **privatisations**, the COM expects EUR 18 billion over the programme period;
- long-term, risk free **interest rates** in the euro area are expected to be 3-3.3% from 2030 onwards;
- **market interest rates are on the Greek public debt** are expected to be around 5% until 2060.

The IMF published its latest DSA on 7 February 2017, in the wider context of an Art. IV consultation. The main assumptions of the IMF's model are the following:

- the real **GDP growth** is expected to be 0.4% in 2016, 2.7% in 2017, 2.6% in 2018 1.5% in 2021 and then stabilise around 1.0%. The long-term nominal GDP growth is expected to be 2.8%;
- the **primary surplus,** on the basis of current policies, will be 1.5**%** from 2018 onward;
- **privatisation** receipts amount to 3billion euro by 2018, rising to 5 billion thereafter. No proceeds are expected from bank privatisation ;
- the long-run, risk-free **market interest rates** in the euro-zone are expected to revert to the historical averages, i.e. 3.8 % ;
- **market interest rates on the Greek public debt** are expected to be around 6% in 2018 and to fluctuate between 4.5 and 6% afterwards ;
- a buffer of EUR 10 billion for **banks recapitalization** needs.

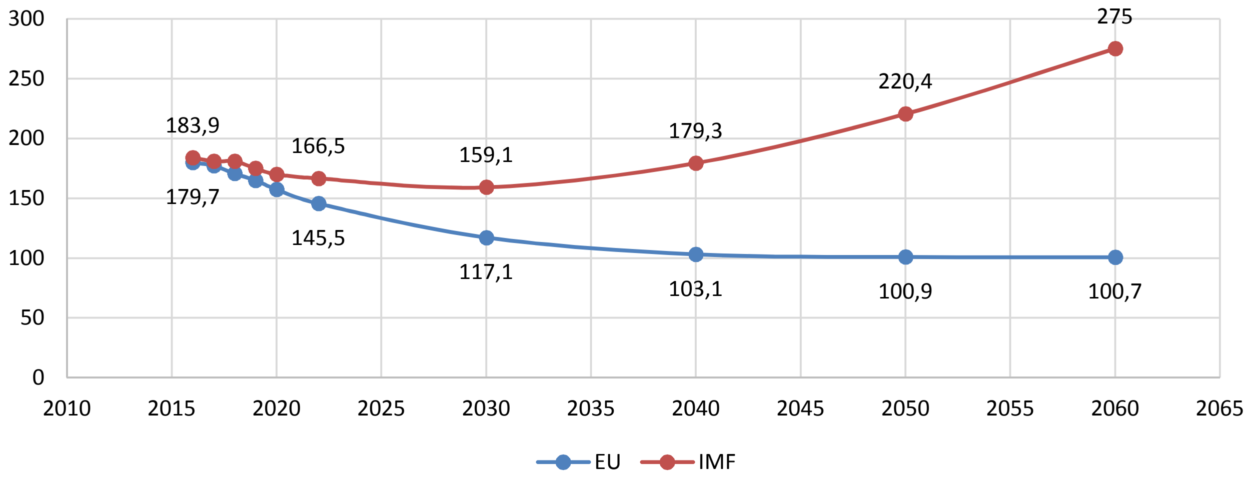
Table 4: Key assumptions of DSAs by COM and IMF

	Year	**EU**	**IMF**
GDP real growth (year-on-year)	2016	-0.3%	0.4%
	2017	2.7%	2.7%
	2018	3.1%	2.6%
	Medium term	1.5%	1.5%
	Long term	1.25%	1.0%
Primary surplus (percentage GDP)	2016	0.5%	0.9%
	2017	1.75%	1.0%
	2018	3.5%	1.5%
	Long term	1.5%	1.5%
Privatisation revenues	2016-2018	18bn	3bn
	After 2018		5bn
Banks' buffer		-	10bn
Long-term market interest rate in the euroarea (ECB)	After 2018	-	3.8%
	2030 onwards	3-3.3%	-
Interest rates on Greek Govern-ment bonds	2018	5%	6%
	After 2018	5%	4.5-6%

Sources: COM (2016) and IMF (2017)

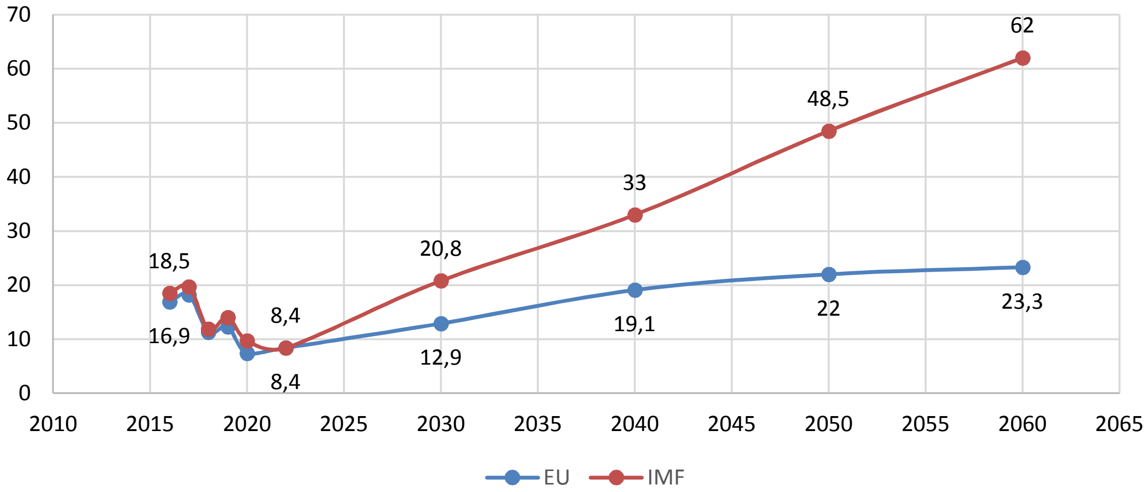
Figures 2 and 3 show that the differences between the latest EU and the IMF **baseline projections** increase over time for both the Debt-to-GDP and the GFN-to GDP indicators, with the IMF analysis being substantially more pessimistic in each case. Nevertheless, both analyses point to serious concerns regarding the sustainability of Greece's public debt over the projection horizon.

Figure 2: Debt-to-GDP (%)



Source: EGOV calculus based on COM forecast, COM 2016 DSA and IMF 2017 DSA

Figure 3: GFN-to-GDP (%)



Source: EGOV calculus based on COM forecast, COM 2016 DSA and IMF 2017 DSA

The IMF concludes that "*a substantial reprofiling of the terms of European loans to Greece is required to restore debt sustainability under the baseline scenario.*" Sustainability is in terms of GFN, which should not exceed 20% of GDP. It proposes therefore a mix of debt restructuring modalities for the European loans (GLF, EFSF and ESM), composed of:

- Grace extensions until 2040 (no repayment of capital);
- Maturity extension for all EU loans (GLF, EFSF and ESM) until 2070;
- Interest payment deferrals: principals and interests payment on all EU loans should be deferred until at least 2040;
- Fix interest rate on all EFSF and ESM loans at maximum 1.5%, for 30 years.

The IMF developed a "restructuring scenario" on the basis of these measures, which would lead to a sustainable debt, in terms of GNF-to-GDP ratio. However, such measures should be taken immediately and with no conditionality attached after the end of the programme, in July 2018. The IMF complemented its DSA with two alternative scenarios, aimed at assessing the robustness of the "restructuring scenario": an upside one (with nominal GDP growth of 3.2%, and no additional bank recapitalisation needs), and a negative one (with a primary balance of 1% of GDP). The optimistic scenario would lead to lowered GFN and faster reduction in debt; the pessimistic scenario would present a situation where both the public debt and the gross financing needs would become unstable and rising over time.

In June 2016, the COM had also developed the DSA for three alternative scenarios, two pessimistic (with growth lowered by 0.25 pp and decrease primary balance from 2023 and from 2018) and one more optimistic (with higher growth and higher privatisation revenues). Only the optimistic scenario would not require further debt restructuring.

Regarding the differences of the forecast between the EU and the IMF, the ESM chair, K. Regling, stated on 9 February 2017 that the IMF "*has so far not been able to integrate into its analysis of Greece fundamental factors that set a member of the eurozone apart from other countries in the world*".

In its press briefing of the same day, the IMF declared that "*in terms of possible participation by the IMF in a program, we have said repeatedly publicly that our strong preference is for a primary surplus target of 1.5 percent and that this should be accompanied by significant debt relief. We've referred to this as the two legs of the program that we think are required. We have also said that we think this target of 1.5 percent can be attained by the policies envisaged in the current ESM program. In short, the IMF is not asking for anymore austerity in Greece (...) We have also said before that if it is at the end of the day the firm desire of the Greek authorities and the European authorities to go with the 3.5 percent primary surplus, we believe that such higher level of primary surplus is sustainable, but for a limited number of years, and only if underpinned by high-quality structural reforms and by growth-friendly measures. But, again, our strongly desired preference is for the 1.5 percent.*"

5. Banking sector and financial stability

Greeks banks' recapitalisation was completed at the end of 2015

At the end of 2015, the four large Greek commercial banks (Piraeus Bank, NBG, Alpha Bank, and Eurobank) had completed their recapitalisation following the 2015 comprehensive assessment. All four large Greek banks managed to raise significant amounts of capital (see table 2), thereby escaping resolution:

- Both Alpha Bank and Eurobank managed to raise the full amount of capital required from private investors or through the conversion of creditors into equity;
- NBG and Piraeus Bank managed to raise from private investors or through conversion of creditors the amount of capital requested under the baseline scenario, that is to say those two injections of capital by the Greek authorities were considered *precautionary* in the meaning of article 32.4 of the BRRD and therefore did not trigger resolution. In line with State aid rules and with the Eurogroup statement of 14 August 2015, all subordinated and senior bondholders were bailed-in

in those two banks through the conversion of their notes into new equity, thereby reducing the amount of State aid needed. The preference shares issued by NBG, which were held by the Hellenic Republic, were also converted into equity.

The HFSF subscribed two categories of instruments: ordinary shares (25% of the total amount injected by the HFSF in NBG and Piraeus Bank) and contingent convertible instruments. Those State aid measures were approved by the COM on 29 November (Piraeus Bank) and 4 December 2015 (National Bank of Greece) on the basis of updated restructuring plans. On 22 December 2015, NBG announced the sale of its major Turkish subsidiary (Finansbank A.Ş). The transfer took place on 15 June 2016 and the bank could repay the contingent convertible bonds by 15 December 2016.

Table 5: Summary of the 2015 capital raising exercise

m€	NBG	Eurobank	Alpha Bank	Piraeus Bank	Total	%
Conversion of creditors into equity	759	418	1.011	582	**2.769**	*19%*
Capital raised from private investors	757	1.621	1.552	1.340	**5.271**	*37%*
Capital injected by the HFSF	2.706	-	-	2.720	**5.426**	*38%*
of which ordinary shares	*676*			*680*	*1.356*	*9%*
of which contingent convertible instruments	*2.029*			*2.040*	*4.069*	*28%*
Other capital actions	380	83	180	291	**935**	*6%*
Total capital shortfall	**4.602**	**2.122**	**2.743**	**4.933**	**14.400**	*100%*

sources: EGOV based on banks' websites

The shareholding structure of all four banks was significantly impacted by those recapitalisations, since former shareholders were heavily diluted, losing from 83% to 99% of the control over the Greek banks. The HFSF now owns (as of 30 September 2016) between 2% and 40% of those banks when it held 35% to 67% as of 30 September 2015. However, the shares subscribed by the HFSF in 2013 had restricted voting rights, while the new shares subscribed in 2015 do not. Therefore the HFSF is able to exercise an influence in those banks where it holds significant shareholdings (NBG and Piraeus).

Table 6: Value of the HFSF shareholding in the four large Greek banks

		NBG	Eurobank	Alpha Bank	Piraeus Bank	Total
shareholding	HFSF	40%	2%	11%	26%	21%
	Other shareholders	60%	98%	89%	74%	79%
	Total former shareholders	100%	100%	100%	100%	100%
book value and market value	**Equity - 30/09/2016 (excl. CoCos and preference shares)**	**7.778**	**6.286**	**8.946**	**7.924**	**30.934**
	of which equity held by the HFSF	*3.141*	*150*	*985*	*2.094*	*6.370*
	Market value - 13/02/2017	**2.131**	**1.283**	**2.597**	**1.598**	**7.610**
	of which shares held by the HFSF	*861*	*31*	*286*	*422*	*1.600*

sources: EGOV based on banks financial statements as of 30/09/2016 and www.helex.gr

As of 30 September 2016, the HFSH had already lost EUR 36.6 billion out of the invested capital amounting to EUR 44.2 billion[14]. As of 13 February 2017, the market value of the HFSF shareholding in those banks was about EUR 1.6 billion for a current book value estimated at about EUR 6.4 billion

[14] This includes losses related to the liquidation of small banks, amounting to about EUR 11 billion as of 30 September 2016.

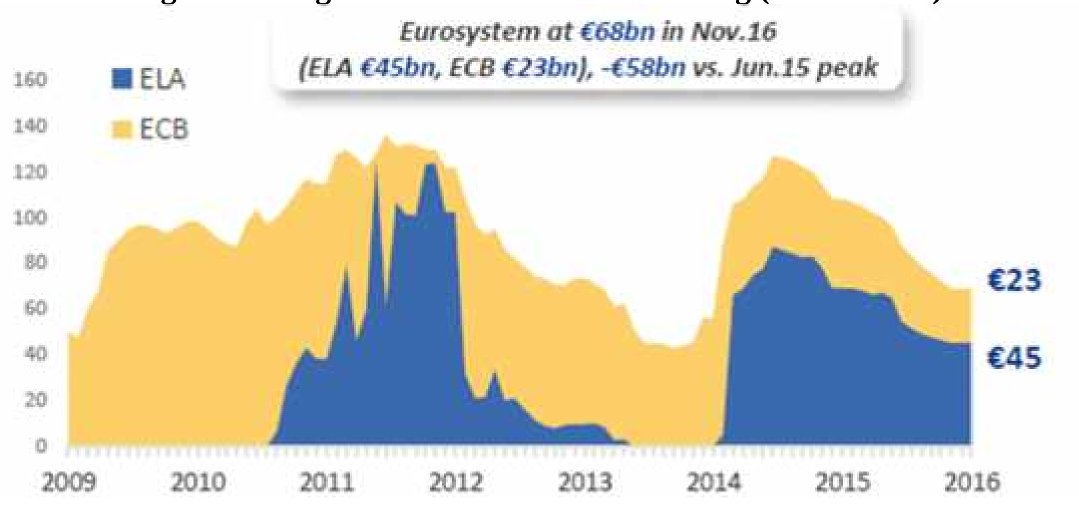
(see table 6). Therefore only a marginal part of the incurred loss could potentially be recovered over time through an appreciation of the market value.

Greeks banks' liquidity is now progressively normalizing, albeit it remains vulnerable

The liquidity position of Greek banks is progressively normalizing, with a slow but continuous decrease in ELA funding since June 2015 (see figure 4). Central bank refinancing amounted to EUR 68 billion for the four largest banks at the end of November 2016, that is to say EUR 58 billion lower than the peak observed in June 2015. Regarding the provision of ELA by the Bank of Greece, the ceiling set by the ECB decreased from EUR 91 billion at the peak in August 2015 to EUR 46.3 billion in February 2017, following in particular:

- the recapitalisation of the four large banks at the end of 2015, with the injection of fresh cash into the banking system;
- the amendments to the subscription agreements between Greek banks, the EFSF and the HFSF, whereby, since April 2016, the Greek banks have been allowed to sell their EFSF notes[15] to the Eurosystem under the Public Sector asset Purchase Programme ("PSPP");
- the reinstatement, as of 29 June 2016, of the waiver affecting the eligibility of Greek government bonds used as collateral in Eurosystem monetary policy operations. The reinstatement of the waiver will in particular enable Greek banks to swap costly ELA refinancing for regular ECB funding;
- the increased access to short-term funding through interbank repos (EUR 18.8 billion at 30 November 2016 vs EUR 1 billion at 31 August 2015); and
- net inflows of deposits and cash since July 2015. It is to be noted that the stock of domestic deposits from Greek residents decreased rapidly again in December 2016 (EUR 132 billion vs EUR 136 billion at the end of November 2016).

Figure 4: Progressive decline in ELA funding (EUR billion)



Source:Piraeus Bank

The gradual decrease in ELA funding also allows for the gradual relaxation of capital controls, with further flexibility introduced in July 2016. Amounts which are deposited in cash in Greek bank accounts can now be fully withdrawn (see box 5). Authorities expected that such measure would

[15] EFSF notes were used by the HFSF to participate in banks' capital increases or to fund the liquidation of small banks when those failed banks were resolved and deposits transferred to a bigger bank.

facilitate the inflows of deposits from excess liquidity held in cash by Greek residents. However the stock of domestic deposits from residents at 31 December 2016 is no higher than at 30 June 2016.

Box 5: Capital controls

Greek banks remained closed for three weeks from 29 June to 20 July 2015, while customers were not allowed to withdraw more than 60 euros per bank card and per day. All transactions to foreign banks had to get prior approval from a government body. There was no limit on domestic transactions by debit/credit cards, nor on withdrawal with cards issued outside Greece.

From 20 July 2015 onwards the cumulative withdrawal of deposits was allowed, up to EUR 420 per week (i.e. if part of the EUR 60 daily allowance was not withdrawn on any day, it could be withdrawn at a later stage within one weeks). In addition, a number of exceptions were introduced, as for instance transfers on foreign bank accounts for the payment of medical fees or tuition fees, and the re-transfer of amounts transferred from abroad.

On 24 July 2015 a ministerial decision further relaxed a bit the capital controls in place, notably regarding amounts which were transferred from abroad. In addition transfers of currency abroad were allowed up to EUR 2000 euros per individual and per trip abroad.

On 20 August 2015 a new ministerial decision allowed for the transfer abroad of EUR 500 per individual and per month, as well as for a number of transactions necessary for the management of banks' liquidity.

On 25 September 2015 the rules governing the restriction on the opening of new bank accounts and the use of fixed-term deposits were relaxed. In addition cash withdrawals on amounts transferred from abroad were allowed up to 10% of the amount transferred, and a number of further exceptions were introduced.

On 22 July 2016 a further relaxation of capital controls increased the amount of cumulative withdrawal allowed, up to EUR 840 every two weeks. In addition, amounts deposited in cash after 22 July 2015 could be fully withdrawn, and early repayment of bank loans was allowed. Other restrictions were relaxed, in particular rules regarding the opening of bank accounts, with exceptions benefiting Erasmus students and pensioners abroad.

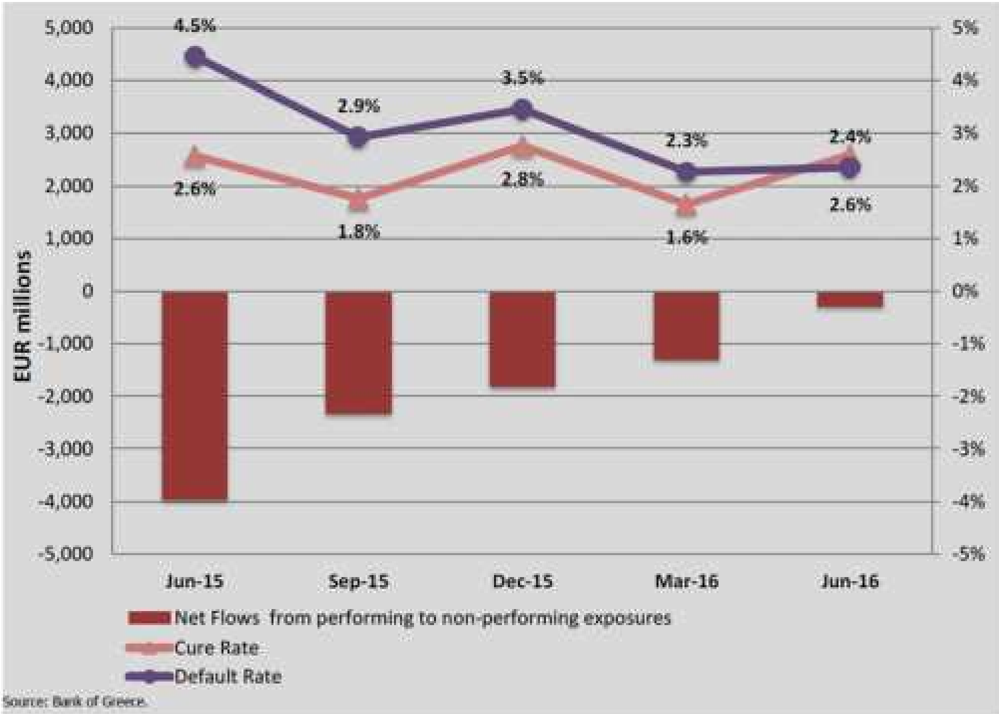
The challenge of non-performing loans is being addressed, but results have yet to materialize

Non-performing loans (NPL) continue to burden the recovery of Greek banks. The NPL ratio (loans 90 days past due) continues to increase and now amounts to 47.1% of total loans at the end of September 2016[16]. However, the outstanding amount of non-performing exposures (NPE) has started decreasing in the third quarter of 2016, from EUR 106.9 billion to EUR 106 billion[17]. In the second quarter of 2016, the cure rate (ratio of NPE moved to performing status to total NPE) was for the first time higher than the default rate (ratio of performing exposures moved to NPE to total NPEs).

[16] Source: EBA Risk dashboard as of Q3 2016.

[17] The NPL ratio has nevertheless increased since the decrease in performing loans is faster than the decrease in non-performing loans.

Figure 5: Net flows of NPE, cure rate and default rate



Source: Bank of Greece

The Eurogroup statement of 14 August 2015 urged "*the authorities to take all necessary steps (...) including opening the market for NPL servicing (...) and exploring the possibility of a bad bank*". A number of measures were therefore committed to that end in the MoU of 19 August 2015, albeit it did not mention any concrete step toward the creation of a bad bank.

In the second half of 2015[18], Greece implemented a number of those measures: amendments to the corporate and household insolvency laws, creation of the regulated profession of insolvency administrators, reactivation of the Governing Council of Private Debt, strengthening of the Code of Conduct, new NPL law aimed at facilitating the transfer of NPL to non-bank service providers, enhanced supervision by the Bank of Greece. The implementation of this comprehensive strategy seems critical for the resolution of the NPL issue in Greece. The Eurogroup statement of 24 May 2016 indicates that the Greek parliament has adopted "*most of the agreed prior actions for the first review, notably the adoption of legislation [...] to open up the market for the sale of loans*" albeit some corrections are requested by creditors before the completion of the review. The legislative framework was further amended on 27 May and 6 June 2016, broadening the application and scope of the previous law passed in December 2015 to facilitate to disposal of NPL and their management by specialised companies.

The supervisory framework governing the management of NPL has been further enhanced. The Bank of Greece published on 7 December 2016 a report on the operational targets agreed with commercial banks in cooperation with the ECB. Those targets, declined by bank and by portfolio over a three-year horizon, cover a wide range of indicators (gross volumes, cash recoveries, loans with long term modifications, ratio of viability analysis carried out over the past 12 months for active

[18] See Commission compliance reports of 14 August, 20 November and 21 December 2015.

SMEs,...). The aggregate targets forecast a decrease in NPE by 38% from June 2016 to December 2019 (see table 7). According to the report by the bank of Greece, the first milestone has been met since NPE and NPL respectively amount to EUR 106.0 billion and EUR 77.7 billion at 30 September 2016.

Table 7: Operational targets on NPE and NPL gross volumes in Greece

A.-Result oriented operational targets	Q2 2016	Q3 2016	Q4 2016	Q1 2017	Q2 2017	Q3 2017	Q4 2017	2018	2019
Target 1: NPE Volume (Gross)	106.9	106.9	105.8	105.2	103.4	102.0	98.2	83.3	66.7
Monitoring: NPE Ratio	51%	51%	51%	51%	50%	50%	48%	42%	34%
Target 2: NPL Volume (Gross)	78.3	78.1	76.3	74.7	72.4	70.5	65.9	53.0	40.2
Monitoring: NPL Ratio	37%	37%	36%	36%	35%	34%	32%	27%	20%

Source: Bank of Greece

The solvency of the Greek banking sector remains subject to the solvency of the Greek government

The Greek banks remain heavily exposed to the Greek sovereign risk. At the end of September 2016, Greek banks held about EUR 20 billion of deferred tax assets, on top of Greek government bonds and Greek treasury bills. That means the total exposure to the Greek sovereign risk is significant when compared to the total amount of equity as of 30 September 2016, which stands at about EUR 36 billion (including CoCos and preference shares). In addition, as observed in 2015, any worsening of the political situation could be detrimental to the Greek economy and thereby to the financial position of Greek banks.

Table 8: Selected banking indicators for Greece

End of period	Dec-13	Dec-14	Dec-15	Jun-16	Sep-16	Dec-16
Domestic residents deposits (in EUR million)	177.018	173.220	133.788	132.170	133.883	132.112
Market Capitalisation 4 largest banks (in EUR million)	26.905	19.473	11.666	n.a.	n.a.	8.905
NPL ratio in Greece (%)	37,1%	39,7%	46,2%	46,9%	47,1%	n.a

Sources: Bank of Greece, Bankscope, Helex and EBA Risk Dashboards

The appointment of a new CEO of the HFSF is pending the appointment of new Members of the General Council, following the resignation of M. Xenofos in July 2016. In the meantime M. Stratos has been appointed CEO. This happened during a year when the HFSF had to review the governance of Greek banks, with the assessment of the Boards of Directors of the four systemic banks. This assessment triggered some resignations in the Boards of Directors of the four main banks.

Box 6: EBA Risk Dashboard: benchmarking Greek banks to EU peers

The European Banking Authority (EBA) publishes a quarterly report on the main risks and vulnerabilities in the European banking sector, showing the situation for a wide sample of European banks, among those four Greek banks (Alpha Bank; Eurobank; National Bank of Greece; Piraeus Bank).

Overall, the risk indicators used by EBA suggest that European banks are currently not in a very comfortable position, with all of the 11 risk areas identified by the EBA at levels deemed medium to high at the end of September 2016.

Following the recapitalisation of the four Greek banks and further divestments in 2016, they report very high CET 1 ratio, at 17.0% on average compared to 13.6% for their EU peers ("fully loaded", i.e. being calculated without applying the transitional provisions set out in Part Ten of the CRD IV Regulation).

However, the level of NPL in Greece continues to represent an enormous challenge, as the average ratio of non-performing loans amounted to 47.1% in September 2016, slowly increasing since December 2015. At EU level the NPL ratio stands at 5.4% (5.7% in December 2015).

The profitability of European banks is in general still low. The average Return-on-Equity bounced back in 2016 to 5.4% in the third quarter (from 4.5% in the last quarter of 2015); Greek banks performed worse in this respect, with a negative Return-on-Equity. On the other hand, the net interest income on interest bearing liabilities is nearly twice as high as the EU average (2.9% vs 1.5%) while the cost-to-income ratio of Greek banks remains lower than the EU averages (51% and 63% respectively).

As regards the balance sheet structure, Greek banks still strongly rely on central bank funding which requires pledging their assets in order to secure or collateralise the transactions. Greek banks therefore have an asset encumbrance ratio of 44%, which is markedly higher than the EU average (26.5%). As to their loan-to-deposit ratio, it is close to the EU average.

Related documents:

- Supplemental MoU: June 2016 detailing the economic reform measures and commitments associated with the financial assistance package going ahead
  - Annex 1 – Asset Development Plan
  - Annex 2 – Government Pending Actions
  - Technical Memorandum of Understanding (TMU) supporting the MoU. It sets out the definitions of the indicators subject to quantitative targets, including performance criteria and indicative targets. It also describes the methods to be used in assessing programme performance.
- Compliance report – First review of the ESM programme.

Annex 1: Key Macro-Economic Indicators Greece

	2012	2013	2014	2015	2016[f]	2017[f]	2018[f]
Real GDP growth – *% change on previous year*							
Greece	-7.3	-3.2	0.4	-0.2	0.3	2.7	3.1
EA	-0.9	-0.3	1.2	2.0	1.7	1.6	1.8
GDP per capita – *Purchasing power parities, Euro*							
Greece	19,100	19,200	19,400	19,600	n.a.	n.a.	n.a.
EA	28.700	28.800	29,400	30,700	n.a.	n.a.	n.a.
General government budget balance – *% of GDP*							
Greece	-8.8	-13.2	-3.6	-7.5	-1.1	-1.1	0.7
EA	-3.6	-3.0	-2.6	-2.1	-1.7	-1.4	-1.4
General government structural budget balance* – *% of potential GDP*							
Greece	0.3	2.3	2.3	1.8	3.7	2.3	2.6
EA	-2.1	-1.4	-1.1	-1.0	-1.1	-1.2	-1.4
General government gross debt* – *% of GDP*							
Greece	159.6	177.4	179.7	177.4	179.7	177.2	170.6
EA	91.4	93.7	94.4	92.6	91.5	90.4	89.2
Interests paid on general government debt – *% of GDP*							
Greece	5.1	4.0	4.0	3.6	3.4	3.3	3.0
EA	3.0	2.8	2.7	2.4	2.2	2.1	2.0
Inflation (HICP) – *% change on previous year*							
Greece	1.0	-0.9	-1.4	-1.1	0.0	1.3	1.0
EA	2.5	1.4	0.4	0.0	0.2	1.7	1.4
Unemployment – *% of labour force*							
Greece	24.5	27.5	26.5	24.9	23.4	22.0	20.3
EA	11.3	12.0	11.6	10.9	10.0	9.6	9.1
Youth unemployment – *% of labour force (15 - 24 years)*							
Greece	55.3	58.3	52.4	49.8	n.a.	n.a.	n.a.
EA	23.6	24.4	23.8	22.4	n.a.	n.a.	n.a.
Current account balance* – *% of GDP*							
Greece	-4.2	-2.2	-2.6	0.0	-0.7	-0.7	-0.6
EA	1.9	2.4	2.5	3.3	3.6	3.2	3.1
Exports – *% change on previous year*							
Greece	1.2	1.5	7.8	3.4	0.7	3.9	4.7
EA	2.6	2.1	4.5	6.5	2.7	3.3	3.7
Imports – *% change on previous year*							
Greece	-9.1	-2.4	7.6	0.3	1.5	3.2	4.2
EA	-0.8	1.4	4.9	6.4	3.3	3.8	4.3
Total investments – *% change on previous year*							
Greece	-23.5	-8.4	-4.6	-0.2	4.0	12.0	14.2
EA	-3.5	-2.5	1.4	3.2	2.8	2.9	3.4
Total investments – *% of GDP*							
Greece	12.6	12.2	11.6	11.5	n.a.	n.a.	n.a.
EA	20.2	19.6	19.6	19.7	n.a.	n.a.	n.a.
General government investments – *% of GDP*							
Greece	2.5	3.4	3.7	3.9	4.0	3.8	3.5
EA	2.9	2.8	2.7	2.7	2.6	2.6	2.7
Total final consumption							
Greece	-7.5	-3.5	0.0	-0.2	n.a.	n.a.	n.a.
EA	-0.9	-0.4	0.8	1.7	n.a.	n.a.	n.a.
Households final consumption expenditure – *% change on previous year*							
Greece	-8.3	-2.8	0.5	-0.2	n.a.	n.a.	n.a.
EA	-1.2	-0.8	0.8	1.8	n.a.	n.a.	n.a.
Income Inequality (Gini Coefficient) – *Scale 0-100: 0 = total income equality; 100 = total income inequality*							
Greece	34.3	34.4	34.5	34.2	n.a.	n.a.	n.a.
EA	30.5	30.7	31.0	30.8	n.a.	n.a.	n.a.
Unit labour cost – nominal – *% change on previous year*							
Greece	-2.0	-6.9	-2.4	-2.2	2.1	0.4	1.1
EA	2.0	1.1	0.7	0.3	0.8	1.1	1.3

Sources: all indicators (if not indicated differently) are from Eurostat, with data extracted on 16/02/2017; (*) the source for these indicators is the 2017 Winter forecast); (f): forecasts are from the 2017 Winter forecast.

Annex 2: Greece's Macroeconomic Imbalance Scoreboard

Indicators			Threshold	2007	2008	2009	2010	2011	2012	2013	2014	2015
External imbalances and competitiveness	**Current account balance as % of GDP**	**3 year average**	-4/+6%	-11.8	-13.9	-14.2	-12.9	-11.2	-8.4	-5.3	-2.5	-1.2
		Year value	-	-15.2	-15.1	-12.3	-11.4	-10.0	-3.8	-2.0	-1.6	0.1
	Net international investment position as % of GDP		-35%	-93.7	-75.8	-87.5	-99.0	-88.8	-115.9	-130.4	-132.5	-134.6
	Real effective exchange rate - 42 trading partners	**% change (3 years)**	± 5% €A	- 0.4	2.3	4.8	2.9	1.8	-5.0	-4.4	-5.6	-5.5
		% change y-o-y	-	0.7	1.6	2.4	-1.2	0.6	-4.4	-0.6	-0.7	-4.3
	Share of world exports	**% change (5 years)**	-6%	9.3	4.8	-10.2	-14.0	-15.5	-24.7	-25.2	-18.0	-20.6
		% change y-o-y		6.9	1.2	-5.6	-11.5	-6.6	-4.8	0.6	3.4	-14.2
	Nominal unit labour cost	**% change (3 years)**	9% €A	11.0	7.4	15.8	14.0	6.8^{p}	-2.3^{p}	-10.0^{p}	-10.9^{p}	-11.1^{p}
		% change y-o-y	-	2.6	5.3	7.1	1.0	-1.4^{p}	-2.0^{p}	-6.9^{p}	-2.4^{p}	-2.2^{p}
Internal imbalances	**House prices** % change y-o-y deflated		6%	2.2^{e}	-2.5^{e}	-4.6^{e}	-8.0^{e}	-7.6^{e}	-12.0^{e}	-9.1^{e}	-5.1^{e}	-3.5^{e}
	Private sector credit flow as % of GDP		14%	16.2	15.5	2.2	5.5	-6.5^{p}	-5.9^{p}	-6.4^{p}	-2.8^{p}	-3.1^{p}
	Private sector debt as % of GDP		133%	101.5	113.0	116.5	128.1	130.2^{p}	131.5^{p}	129.1^{p}	128.5^{p}	126.4^{p}
	General government gross debt (EDP) as % of GDP		60%	103.1	109.4	126.7	146.2	172.1	159.6	177.4	179.7	177.4
	Unemployment rate	**3 year average**	10%	9.1	8.4	8.6	10.0	13.4	18.4	23.3	26.2	26.3
		Year value	-	8.4	7.8	9.6	12.7	17.9	24.5	27.5	26.5	24.9
	% change y-o-y in **Total Financial Sector Liabilities,** non-consolidated		16.5%	22.2	4.4	10.1	8.3	-3.7	-2.6	-17.2	-6.7	15.7
Employment indicators	**Activity rate % 15-64 total pop.** (3 year change)		-0.2%	0.3b	0.3	0.7b	1.3	0.6	0.1b	-0.3	0.1	0.3
	Long term unemployment active pop. 15-74 (3 year change).		0.5%	-1.4	-1.5	-1.0	1.5	5.1	10.6	12.8	10.7	3.7
	Youth unemployment % active pop. 15-24 (3 year change)		0.2%	-3.8	-3.9	0.7	10.3	22.8	29.6	25.3	7.7	-5.5

Source: Eurostat MIP Scoreboard indicators, data updated on 14/2/2017.
Notes: ^{p} (Provisional); ^{e} (Estimated); b (Break in time series). See also MIP procedure.

Indicators above/ below the thresholds

Annex 3: Greece's progress towards EU2020 targets

Indicator	Greece			EU28	
Employment rate (% of population aged 20-64)	**70**		**Target 2020**	**75**	
	54.9		2015	70.1	
	53.3		2014	69.2	
	52.9		2013	68.4	
	55.0		2012	68.4	
Expenditure on R&D (% of GDP)	**1.21**		**Target 2020**	**3**	
	0.96		2015	2.03	
	0.84		2014	2.04	
	0.81		2013	2.03	
	0.70		2012	2.01	
Greenhouse gas emission[1]	**Total** **n.c.s.t.**[1] (Index 1990 = 100)	**Non-ETS** **96**[1] (Index 2005 = 100)	**Target 2020**	**Total** **80** (Index 1990 = 100)	
	n.a.	69.78	2015	n.a.	
	97.18	69.61	2014	77.06	
	99.88	69.26	2013	80.26	
	106.94	75.64	2012	81.83	
Share of renewable energy (%)	**18**[2]		**Target 2020**	**20**	
	n.a.		2015	n.a.	
	15.3		2014	16.0	
	15.0		2013	15.0	
	13.4		2012	14.3	
Primary energy consumption (million tonnes of oil equivalent-TOE)	**27.1**		**Target 2020**	**1,483**	
	23.7		2015	1,529.6	
	23.7		2014	1,508.3	
	23.6		2013	1,569.9	
	26.8		2012	1,585.4	
Early school leaving (% of population aged 18-24)	**9.7**		**Target 2020**	**10**	
	7.9		2015	11.0	
	9.0		2014	11.2	
	10.1		2013	11.9	
	11.3		2012	12.7	
Tertiary educational attainment (% of population aged 30-34)	**32**		**Target 2020**	**40**	
	40.4		2015	38.7	
	37.2		2014	37.9	
	34.9		2013	37.1	
	31.2		2012	36.0	
Population at risk of poverty or social exclusion (thousand - % of total population)	**Reduction by 450 thousand**	**n.c.s.t.**	**Target 2020**	**Reduction by 20 million**	**n.c.s.t.**
	3,829	35.7	2015	118,820	23.7
	3,885	36.0	2014	121,897	24.4
	3,904	35.7	2013	122,703	24.6
	3,795	34.6	2012	123,614	24.7

Source: Eurostat (data extracted on 27/02/2017).
Note: (1) The Effort Sharing Decision (2009/406/EC) sets country-specific targets for non-ETS emissions only and an EU target for ETS-emissions. For Greece, non-ETS emissions will be reduced by 4% compared to 2005 levels. For the EU, ETS-emissions will be reduced by 21% compared to 2005 level and overall emissions by 20% compared to 1990 levels. (2) Greece committed to a target of 18% by 2020, increased to 20%, by national legislation (Law 3851/2010).
n.c.s.t. = "no country specific target"; n.a = "not available".