GREECE

Highlights

- **Economic indicators continue to improve.** The economic recovery, which began in 2017, continued into 2018 and the first half of 2019, but at a relatively modest rate. Economic sentiment has risen sharply since May 2019, reaching a 12-year high, and unemployment has dropped below 17 per cent.
- **Important reforms have advanced.** The previous government made sufficient progress on achieving specific reform commitments by the end of 2018 to enable creditors to grant €970 million debt relief measures, while the new government has already brought forward important fiscal, labour market and governance reforms.
- **Capital controls have been fully lifted.** Effective since September 2019, this measure brings to an end more than four years of restrictions on the free flow of capital.

Key priorities for 2020

- **Further progress is needed in reducing non-performing exposures (NPEs).** New levers are now in place or in preparation, including an asset protection scheme, and should be used vigorously to help banks bring down the level of NPEs from current excessive levels.
- **Flagship privatisations should be carried out in a timely way.** The key short-term project is Hellenikon (the former Athens airport), which has the potential to be transformative for the economy, but other important assets should also be commercialised and prepared for sale in a timely way.
- **Reforms to governance are urgently needed.** Greece's ranking on global governance measures is poor, reflecting many years of weak public administration, problems in the judiciary and inadequate corporate governance standards. The new government should follow up promptly on its plans for reforms in these areas.

Main macroeconomic indicators %

	2015	2016	2017	2018	2019 proj.
GDP growth	-0.4	-0.2	1.5	1.9	2.0
Inflation (average)	-1.1	0.0	1.1	0.8	1.1
Government balance/GDP	-5.7	0.6	1.0	0.4	-0.2
Current account balance/GDP	-0.2	-1.7	-2.4	-3.4	-2.7
Net FDI/GDP [neg. sign = inflows]	0.2	-2.4	-1.5	-1.6	-1.8
External debt/GDP	245.5	236.1	224.0	217.7	n.a.
Gross reserves/GDP	n.a.	n.a.	n.a.	n.a.	n.a.
Credit to private sector/GDP	112.2	107.3	99.0	89.1	n.a.

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Macroeconomic performance

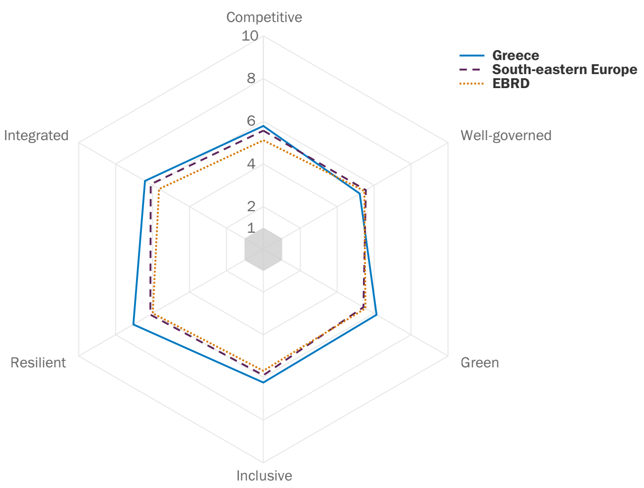
Modest economic growth has continued. GDP grew by 1.9 per cent in 2018. Private consumption continued to have a positive impact on growth and labour market developments have been encouraging, with unemployment falling to 16.9 per cent (seasonally adjusted) in July 2019 – still very high relative to peers but the lowest rate since 2011. The economic recovery is broad-based, with services being the main driver. In the first half of 2019, GDP increased by 1.5 per cent year-on-year, as exports of goods and services (including tourism) and public consumption all moved in a positive direction. Investment remains a weak spot, with gross fixed capital formation falling at double-digit levels in 2018, and net investment (gross investment minus depreciation) still strongly negative. However, all main components of investment apart from transport equipment and weapons investments are increasing and are expected to pick up further in the short term. Foreign direct investment (FDI) has been on an upward trend since 2015, reaching €3.7 billion in 2018, versus less than €1.2 billion in 2015, with further strong inflows (€2.5 billion) in the first seven months of 2019.

Fiscal and external balances remain encouraging. The primary fiscal surplus reached 4.3 per cent of GDP in 2018, outperforming significantly the target of 3.5 per cent of GDP. An expansionary fiscal package was adopted by the previous government in May 2019 but the recovering economy and boosted revenue collection should help ensure that the target is again achieved in 2019. Meanwhile the current account deficit rose from -0.8 per cent of GDP in 2017 to -3.4 per cent of GDP in 2018, despite the continued upward trend in exports of goods and services, but is countered by the positive developments in FDI noted above.

Capital market access has improved amid boosts to the country's sovereign credit rating. The government has issued several bonds in 2019, including a seven-year €2.5 billion bond in July 2019, with a yield of just 1.9 per cent (below US Treasuries' yields). The low yield reflects not only global financing conditions but also Greece's improved standing among creditors in recent years. In March 2019, Moody's raised Greece's sovereign rating by two levels to B1 and in October 2019, Standard & Poor's upgraded Greece's sovereign credit rating from B+ to BB-, given the reduced fiscal risks and lifting of capital controls. However, all major credit ratings agencies still have Greece several notches below investment grade.

Short-term GDP growth is likely to rise somewhat. Our current projection is that the economy will grow by 2.0 per cent in 2019 and 2.4 per cent in 2020. The main drivers of growth are likely to be exports and a stronger impact of private consumption as a result of the sharp increase in economic sentiment and falling unemployment rates. However, risks associated with a possible deterioration in the global economy remain significant. Internally, the new government has committed to an ambitious reform agenda, and investors will be looking to see if they can deliver on their promises and make major improvements to the business environment. If that happens, prospects for higher growth rates in the medium term will be significantly enhanced.

Assessment of transition qualities (1-10)



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Major structural reform developments

Important reforms have advanced. Following the completion of the Third Economic Adjustment Programme in August 2018, Greece is now in a post-programme enhanced surveillance framework. As of September 2019, there have been three enhanced surveillance reports, prepared by the European Commission in partnership with other institutions. The third report, published in June 2019, presented a mixed picture. It noted progress in areas such as public sector reform, corporate governance in state-owned enterprises (SOEs) and land reform, but it revealed that the pace of reform had slowed in 2019, with reversals in certain areas. Meanwhile, the new government, which took office in July 2019, has placed economic reform and governance improvements at the heart of its programme. An omnibus bill with a number of growth-enhancing reforms was submitted to parliament in September 2019.

Privatisation is advancing, albeit with some delays. The privatisation strategy and the governance reform of SOEs is being implemented by the Privatisation and Investment Fund (the Hellenic Corporation of Assets and Participations). Important deals in the past year include the sale of 66 per cent of the gas transmission systems operator, DESFA, which was closed at the end of 2018; and a 20-year extension of the concession agreement for Athens International Airport, completed in February 2019. Other major projects in preparation and at an advanced stage include the development of Hellenikon (site of the former Athens airport) and Egnatia motorway. With regard to the former project, final submissions under a tender for a casino licence were submitted on 4 October 2019, and construction should begin on site in early 2020. However, other privatisations have encountered delays, and the proposed sale of a majority stake in Hellenic Petroleum failed to attract any bids.

Capital controls have been fully removed. As of 1 September 2019, all remaining restrictions on the transfer of capital abroad were removed. Capital controls were introduced at the height of the crisis in June 2015 but had been relaxed gradually in stages since then.

The financial sector is still recovering and NPEs are being reduced. The banking sector as a whole is profitable, but banks continue to be burdened by exceptionally high levels of NPEs, which stood at €75.4 billion, or 43.6 per cent of total loans as of June 2019. The four systemic banks are addressing the problem using a variety of tools and according to targets agreed with the Bank of Greece. The new government has developed an asset protection scheme, which was approved by the European Commission (DG Comp) in October 2019. It is expected to be operational in the coming months. Under this scheme, special purpose vehicles would be set up to issue government-guaranteed bonds, allowing banks to take some of their NPEs off their balance sheets.

Further improvements have been made to the business environment. Important steps over the past year include efforts to streamline licensing and customs procedures, the introduction of one-stop shops, and progress on land and cadastral reform. Further business-friendly measures are in the pipeline of the new government's programme. At the same time, Greece's ranking on the World Bank's ease of doing business assessment remains low by EU and OECD standards, reaching 79th position (out of 190 countries) in the 2020 report (down seven places from the previous year), with persistent problems in getting credit, registering property, enforcing contracts and resolving insolvency.

Governance reforms are being introduced. A key pillar of the post-programme enhanced surveillance framework is public administration reform and building a modern state. Important steps have been taken in the past year to improve the management of human resources in public institutions and the development of a more modern staff appraisal system. The new government has also signalled that governance reform will be at the heart of its programme, and has already taken steps to unify all entities that audit and oversee the activities of the government.