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Enhanced Surveillance update - Greece, May 2022

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BACKGROUND

Economic developments and policies in Greece are monitored under the European Semester for economic policy co-ordination. Since 2018 and the end of the financial assistance programme, they have also been monitored under the enhanced surveillance framework according to Articles 2 and 3 of Regulation (EU) No 472/2013 ([1]). The implementation of enhanced surveillance for Greece ([2]) acknowledged the fact that Greece needed to continue implementing measures to address the sources or potential sources of economic and financial difficulties, while implementing structural reforms to support a robust and sustainable economic growth.

Enhanced surveillance provides a comprehensive framework for monitoring economic developments and the pursuit of policies needed following the completion of the financial assistance programme. It allows for a regular assessment of recent economic and financial developments in Greece, as well as for monitoring sovereign financing conditions and updates of the debt sustainability analysis.

Enhanced surveillance also provides the framework for assessing the general commitment given by Greece to the Eurogroup of 22 June 2018, i.e. to continue and complete reforms adopted under the financial assistance programmes and to ensure that the objectives of the important reforms adopted under the financial assistance programmes are safeguarded. In that context, enhanced surveillance has served to monitor the implementation of specific commitments to complete key structural reforms started under the programme, in six key areas by agreed deadlines up to mid-2022, namely: (i) fiscal and fiscal-structural policies, (ii) social welfare, (iii) financial stability, (iv) labour and product markets, (v) Hellenic Corporation of Assets and Participations and privatisation, and (vi) the modernisation of public administration ([3]).

This is the fourteenth enhanced surveillance report for Greece. The report is based on the findings of a mission held on 6 April 2022 and regular dialogue with the Greek authorities. The mission was conducted by the European Commission in liaison with the European Central Bank ([4]). The International Monetary Fund participated in the context of its Post Financing Assessment framework, while the European Stability Mechanism participated in the context of its Early Warning System and in line with the Memorandum of Understanding of 27 April 2018, on working relations between the European Commission and European

([1]) Regulation (EU) No 472/2013 of the European Parliament and the Council of 21 May 2013 on the strengthening of economic and budgetary surveillance of Member States in the euro area experiencing or threatened with serious difficulties with respect to their financial stability, OJ L140, 27.5.2013, p. 1.

([2]) Commission Implementing Decision (EU) 2022/216 of 15 February 2022 on the prolongation of enhanced surveillance for Greece.

([3]) https://www.consilium.europa.eu/media/35749/z-councils-council-configurations-ecofin-eurogroup-2018-180621-specific-commitments-to-ensure-the-continuity-and-completion-of-reforms-adopted-under-the-esm-programme_2.pdf.

([4]) ECB staff participated in the review mission in accordance with the ECB's competences and thus provided expertise on financial sector policies and macro-critical issues, such as headline fiscal targets and sustainability and financing needs. The review mission was preceded by a technical mission from 28 to 31 March 2022.

Stability Mechanism. The current report assesses the implementation of Greece's commitments to the Eurogroup regarding reform completion due up to mid-2022.

This report could serve as a basis for the Eurogroup to decide on the release of the next set of policy-contingent debt measures worth EUR 748 million. These measures were agreed with the Eurogroup on 22 June 2018 and include the transfer of income equivalent amounts stemming from central banks' holdings of Greek government bonds under the Securities Markets Programme and the Agreement on Net Financial Assets and a waiver for the step-up interest margin for certain loans provided by the European Financial Stability Facility. The sixth tranche of policy-contingent debt measures was released following the Eurogroup on 6 December 2021.

The commitments given by Greece to Eurogroup partners in June 2018, which are the basis for the release of additional debt relief measures, were established up to mid-2022. The decision on the release of the remaining debt relief measures will be taken by the Eurogroup. Taking account of the progress towards completion of commitments, the release of the final tranche of debt measures could take place end-2022. This report also sets out the specific commitments, which can provide a basis for the Eurogroup to decide on the release of this final tranche of debt relief measures. While the authorities have delivered on the majority of their commitments, some elements remain to be fully completed. Thus, the list of commitments to serve as a basis for the final disbursement consists of remaining steps. The list is agreed with the Greek authorities and can be found in annex to this report.

The successful delivery of the bulk of the policy commitments and the effective reform implementation have improved the resilience of the Greek economy and strengthened its financial stability. This has significantly reduced the risks of adverse spill-over effects on other Member States in the euro area, hence effectively addressing the condition underpinning the application of enhanced surveillance. The authorities remain committed to reform implementation and to completion of outstanding elements. On the basis of these considerations, the European Commission may not prolong enhanced surveillance after its expiration on 20 August 2022. If enhanced surveillance is not prolonged, the monitoring of Greece's economic, fiscal and financial situation would continue in the context of both the well-established post-programme surveillance ([5]) and the European Semester. Major reforms and investments would also continue to be followed in the context of the delivery of Greece's recovery and resilience plan ([6]). Monitoring of the specific commitments to serve as a basis for the final tranche of debt measures would be undertaken in a first post-programme surveillance report to be issued in November 2022.

([5]) Regulation (EU) No 472/2013 of the European Parliament and the Council of 21 May 2013 on the strengthening of economic and budgetary surveillance of Member States in the euro area experiencing or threatened with serious difficulties with respect to their financial stability, OJ L140, 27.5.2013, p. 1.

([6]) https://ec.europa.eu/info/business-economy-euro/recovery-coronavirus/recovery-and-resilience-facility/greeces-recovery-and-resilience-plan_en.

OVERALL ASSESSMENT

Following a strong rebound in 2021, the post-pandemic recovery is set to continue in 2022 at a somewhat weaker pace, as it is affected by higher energy prices and the economic impact of the Russian military aggression against Ukraine, amidst lingering uncertainty related to the pandemic. According to the Commission 2022 spring forecast, growth is expected to reach 3.5% in 2022 and 3.1% in 2023. Investment is forecast to be the main driver of growth, but private consumption and net exports will also contribute to the increase of economic activity. The general government primary deficit monitored under enhanced surveillance reached 5.5% of GDP in 2021, which is 2.1 percentage points lower than expected in autumn last year. The positive surprise stems mainly from to the quick economic recovery. Fiscal policy remains supportive in 2022 as some of the pandemic-related emergency and support measures are still in place for the year, whereas temporary fiscal measures were taken to address the impact of the energy price increases in 2022. In its 2022 Stability Programme, the government plans to reach a 1.1% of GDP primary surplus in 2023 and further decrease the high public debt ratio ([7]). Most support measures related to the energy price increases or the pandemic are set to be phased out by 2023. At the same time, the government plans to support growth by making permanent the reduction in the solidarity tax and social security contributions implemented during the pandemic. On the back of the economic recovery, the unemployment rate decreased to 14.7% in 2021, down from 17.6% in 2020 and its peak of 27.8% in 2013. While still one of the highest in the EU, it is expected to decrease further in 2023. Going forward, employment growth is expected to remain resilient in view of the still robust economic growth. The at-risk-of poverty rate remains high (17.7% in 2020).

Overall, this report concludes that Greece has taken the necessary actions to achieve its specific commitments, despite the challenging circumstances triggered by the economic implications of new waves of the pandemic as well as of Russia's military aggression against Ukraine. The authorities have completed a number of specific commitments in the areas of public financial management, property taxation, disability benefits, environmental inspections and justice, and agreed on the extension of the mandate of the Hellenic Financial Stability Fund. Greece also completed wider structural reforms including the public procurement reform and setting up a Justice Statistics department at the Ministry of Justice.

The Greek authorities remain committed to reform implementation and have committed to continue implementing actions to progress with outstanding commitments. The European institutions welcome the authorities' close and constructive engagement in all areas and encourage the authorities to keep up the momentum and, where necessary, reinforce the efforts to complete all agreed reform steps in time for the decision on the final disbursement at end-2022, in particular as concerns reforms in the area of financial sector policies, primary health care, cadastre, codification of the labour legislation, and reaching the agreed targets for the clearance of arrears.

The remainder of this section recalls the progress made in the framework of enhanced surveillance in the six key areas of Greece's commitments, assesses the latest

([7]) https://ec.europa.eu/info/sites/default/files/2022_el_stability_programme_en.pdf.

achievements over the last quarter (the “current reporting period”) and presents remaining reform steps under existing commitments.

Fiscal and fiscal structural policy

Greece achieved its **primary surplus target** of 3.5% of GDP in 2018 and 2019. Following the outbreak of the pandemic, the European Commission activated in 2020 the general escape clause, which allows for a temporary departure from the budgetary requirements, including Greece’s fiscal targets monitored under enhanced surveillance, provided that this does not endanger fiscal sustainability in the medium term. In its Communication of 3 March 2021 ([8]), the Commission set out its view that the decision on the deactivation or continued application of the general escape clause should be taken as an overall assessment of the state of the economy, with the level of economic activity in the EU or euro area compared to pre-crisis levels (end-2019) as a key quantitative criterion. Heightened uncertainty and strong downside risks to the economic outlook in the context of war in Europe, unprecedented energy price hikes and continued supply chain disturbances warrant the extension of the general escape clause of the Stability and Growth Pact through 2023.

As regards fiscal structural reforms completed in the context of enhanced surveillance, Greece has improved its public financial management by completing a **cash monitoring and forecasting reform** for its treasury account system, and reformed the remuneration structure of the **Independent Authority for Public Revenues** by adopting a special wage grid, so as to allow it to retain and attract high calibre staff. This special wage grid complements the unified wage grid adopted under the financial assistance programme and could serve as a basis for other entities.

In the current reporting period, the authorities have completed further commitments in the area of public financial management and tax policy:

- In the area of public financial management, the authorities have completed the work on further refinements of the functional budgetary classification (part of the **chart of accounts reform**). This reform will allow for a deeper analysis of public expenditure and thus help improve the design of economic policy.

- The authorities have also completed the implementation of more than 200 **recommendations by the Hellenic Court of Auditors** to prevent the accumulation of arrears as well as a broader reform simplifying fiscal procedures and accelerating the payment chain in the public sector.

- The authorities have completed a reform of the **ENFIA property tax**. The reform applies new market-related property tax values, widens the tax base and improves the fairness and economic efficiency of the property tax. The authorities have issued the post-reform tax assessment bills for 2022 and the payment of the first instalment of the tax is due in May.

([8]) Communication from the Commission to the Council on one year since the outbreak of COVID-19: fiscal policy response, Brussels, 3.3.2021, COM(2021) 105 final.

By October 2022, the authorities have committed to deliver the following steps:

- Non-pension and pension **arrears** are expected now to be cleared by August 2022, which will complete the commitment. Following a slow-down in the pace of arrears clearance in the first months of 2022, this represents a delay of six months as regards non-pension arrears and two months as regards pension arrears, compared to plan. The delay has been largely caused by the continued pandemic, the hike in energy prices, slower-than-planned delivery of planned IT enhancements and lower than expected yield of previous measures. The authorities have proposed, and already partly implemented, a set of additional actions to speed up the clearance process. The actions include measures to improve, on a structural basis, liquidity of hospitals and public transport companies, and targeted changes in the process of awarding pensions.

- In the area of **tax administration**, the IT collection system is to be fully operational in all services of the Independent Authority for Public Revenues by September 2022, which will complete the commitment. The system is expected to strengthen the tax collection capacity of the Authority. Four out of seven modules are now operational in the central tax administration services and the remaining three are to be operational by September 2022, in line with the agreed timeline.

<u>Social welfare</u>

In the context of enhanced surveillance, Greece has modernised its social welfare system by completing the set-up of the **Single Pension Fund**, completing the roll-out of all three pillars of the **Social Solidarity Income**/Guaranteed Minimum Income scheme and adopting a new delivery model for active labour market policies. So far there have been approximately 400 000 recipients of the Guaranteed Minimum Income and it is estimated that in the next two years all of them will have received an individualised action plan. As a result of the reforms and the economic recovery, the share of people at risk of poverty decreased from 20.2% in 2017 to 17.7% in 2020, but remains among the highest in the EU. Greece also reviewed the system of **subsidies for local public transport**, set up the main body responsible for **centralised health procurement** (EKAPY) and achieved a 30% share of centralised procurement in total hospital expenditure.

In the current reporting period, the authorities have completed another commitment in the area of disability assessment and progressed according to schedule on the collection of health-care clawbacks:

- The authorities adopted legislation to introduce a new **disability assessment** approach based on both medical and functionality-related criteria. This new approach represents a significant improvement compared to the current system, where disability is assessed based on purely medical evaluations. Notably, the adopted legislation sets up multidisciplinary assessment committees made up of psychologists, occupational therapists and social workers who will apply a methodology suggested by the World Health Organisation for assessing functionality aspects of examined persons (named WHODAS 2.0). The Committees will consider every-day difficulties in domains such as cognition, mobility, socialisation, professional life, self-care etc. on top of prior medical assessments. The approach will first be used on a pilot basis for 24 months starting in autumn 2022 for granting personal assistance benefits to 1 000 persons with disabilities.

- The collection of health-care **clawbacks** (i.e. spending over and above the legislated ceiling for public spending on pharmaceuticals and other healthcare services that is due to be collected back from pharmaceutical suppliers and healthcare providers) is progressing according to schedule for both pharmaceuticals and other services, which is welcome.

By October 2022, the authorities have committed to deliver the following steps:

- Following the adoption of amendments to the primary legislation on the **primary health care system,** the authorities will adopt the secondary legislation by early-June 2022, which will specify the key elements of the system including incentives for patient registration and gatekeeping. The authorities have also committed to start patient registration, with the objective of reaching 25% of the total population registered in the system by the end of October and 50% by the end of 2022, and to complete the IT infrastructure for registration and appointments by end-June. By end-July, the registration of self-employed family doctors to the system will reach a level that allows to cover at least 85% of the population. By October, the authorities will activate the incentives/disincentives scheme for registration and gatekeeping. Reforming the primary health care system represented a key component of the financial assistance programme with the overarching objectives of enhancing citizens' access to health care services and strengthening governance and efficiency. Population registration and an effective system of gatekeeping are key defining elements conducive to delivering on these objectives. In the new framework, these key elements are pursued by means of financial incentives. Such a system, if fully implemented, has the potential to deliver on the objectives. At the same time, it creates challenges to ensure equal access and to deliver on the objective of full population coverage, which will need to be carefully monitored.

- The mid-2022 target of a 40% share of **centralised procurement** in total hospital expenditure is to be met, which will complete the commitment. The authorities are encouraged to proceed swiftly with the issuance of the planned tenders to reach the target.

<u>Financial stability and justice reforms</u>

Following an outstanding year in non-performing loans reduction in 2021, the focus gradually moves to the workout of non-performing debt for viable debtors, as well as to a sustainable improvement of banks' profitability and capital position. The non-performing loan ratio stood at 12.8% on a solo basis in December 2021, having declined strongly from 30.1% at end-2020 and 40.6% at end-2019. Making use of securitisations under the Hercules Asset Protection Scheme, two of the four systemic banks have recorded a single-digit non-performing loan ratio as of end-2021, while the other two are expected to meet the same target at the latest by the end of 2022. Nevertheless, the non-performing loan ratio in Greece remains the highest in the euro area. In addition, the limited net inflow of new non-performing loans ([9]) has continued in the fourth quarter of 2021 and will need to be closely monitored, as risks to banks' asset quality persist. Moreover, the successful resolution of non-performing debt increasingly depends on servicers, in charge of servicing securitised and sold loans. While the clean-up of banks' balance sheets continued to reduce banks' capital buffers and profitability, the outlook for 2022 benefits from reduced provisioning needs and internal capital generation through improved core profitability. Still, banks' capital position remains one of the lowest in the euro area and its quality continues to be a concern, as it contains a high and increasing share of deferred tax credits. Increased uncertainty around the economic outlook in the wake of Russia's aggression against Ukraine could weigh on credit growth going forward.

As regards financial sector reforms completed in the context of enhanced surveillance, Greece fully lifted **capital controls** imposed during the financial assistance programme, completed a major reform of the **insolvency framework**, including an **out-of-court workout** scheme and providing **financial training to judges** to implement those reforms, while just starting to put in place the sale-and-leaseback entity. The Hellenic Financial Stability Fund developed an **exit strategy** for the sale of the stakes owned in the systemic banks and Greece confirmed the **alignment of the mandate of its Selection Panel** with that of the Fund.

In the current reporting period, there has been further progress with the implementation of the agreed actions in the financial sector, but challenges remain, in particular with respect to clearing the backlogs of household insolvency cases and called state guarantees. The authorities have completed a commitment related to the Hellenic Financial Stability Fund and launched a tender for the integrated case management system for courts:

- The platforms under the **new insolvency framework** are gradually yielding results, particularly with respect to out-of-court settlements, and further improvements are continuously being developed.

- The upward trend in the assignment of new hearing dates for pending **household insolvency cases** has been maintained but the number of final court decisions is limited.

- Similarly, the **conduct of auctions** is gaining traction, and an increasing share of the assets transferred through successfully concluded auctions is being acquired by entities other than banks or servicers.

- Despite some improvements, the timeline for the clearance of the **backlog of called state guarantees** has been amended to reflect the accumulated shortfalls in the pay-out of called guarantees and unexpected legal challenges preventing the payment of certain claims. The authorities are assessing potential solutions to limit the resulting delays in the payment of such claims and remain committed to keep the deadline for the completion of all payments unchanged, i.e. by the second quarter of 2024. The

([9]) The term 'net inflows' refers to the difference between the volume of new non-performing loans and the volume of previously generated non-performing loans that have been cured or whose collateral has been liquidated in a given period of time. The overall stock of non-performing loans can decrease even if net inflows are positive, if for instance some non-performing loans are removed from the stock due to securitisation transactions or outright sales.

adoption of the new Code on the Organisation of Justice and the Status of Judges is expected to facilitate a speedier clearing of legacy backlogs, as well ensure the smooth functioning of the new insolvency framework.

- The concessionary process for the setup of the **sale-and-lease-back entity** is expected to be launched in May, and an interim support scheme for vulnerable debtors is being put in place to ensure a smooth transition during the period needed until the new entity commences operations, which is not expected to exceed 15 months.

- The authorities have agreed a reform of the **Hellenic Financial Stability Fund** with the European institutions. The law is expected to be adopted shortly. The duration of the Fund has been extended until the end of 2025 to allow the Fund to fulfil its dual objective of effectively divesting its assets while also contributing to the stability of the Greek banking system. The reform streamlines the Fund's governance structure and outlines a set of principles that will guide its divestment strategy. The Fund's special rights have also been streamlined.

- The authorities have launched the tender for the **integrated case management system** for civil and criminal cases (OSDDY-PP). The contract is expected to be awarded by end-2022 and implemented in the following 36 months.

By October 2022, the authorities have committed to deliver the following steps:

- **E-filing in administrative courts** is to be fully completed and the authorities are committed to achieve this by end-June 2022, which will complete the commitment. The implementation has seen progress and the platform enabling the filing of initial submissions, memoranda and procedural documents in the context of pending procedures is ready and will be fully operational in June 2022. The extension of functionalities has been launched in a pilot phase, two months later than previously envisaged, due to delays on the side of the contractor.

- Take a number of specific steps under the **agreed actions in the financial sector**, in particular as regards the clearance of the backlog of household insolvency cases and the backlog of state guarantees.

The authorities will also table in Parliament a broader reform in the area of justice, namely a new **Code on the Organisation of Justice and the Status of Judges**. The code will introduce numerous improvements regarding the performance of judicial duties, the professional assessment and advancement of judges, their disciplinary framework and measures to enhance the effectiveness and efficiency of judicial proceedings. The code was submitted to the General Secretariat for Legal and Parliamentary Affairs on 13 May 2022 and is to be tabled to Parliament by end-May. It will enter into force immediately thereafter, with the notable exception of the rules on evaluation of judges, which will enter into force at the beginning of the new judicial year. Moreover, the authorities will adopt by end-May the final piece of secondary legislation to operationalise the Justice Statistics (JustStat) department, tasked with the collection, aggregation, processing and publishing of judicial data from the courts and prosecutor's offices of Greece; the department is also expected to safeguard and improve, on a permanent basis, the quality of judicial statistics.

Labour and product markets

As regards labour and product market reforms completed in the context of enhanced surveillance, Greece completed the implementation of the action plan on **undeclared work**, updated the **minimum wage** in accordance with the procedure stipulated in Law 4172/13 in February 2019 and January 2022, revised the **nuisance classification**, simplified **investment licensing procedures** in agreed sectors, including transport, education, tourism, social welfare, and aquaculture and awarded a contract for the deployment of the relevant **information system**. In the energy sector, Greece launched the **Target Model** for the electricity market and agreed to an **anti-trust remedy** allowing the competitors of the Public Power Corporation, the Greek state-owned electricity incumbent, to purchase more electricity on a longer-term basis, thereby drawing to a close a long-standing anti-trust case.

In the current reporting period, the authorities have implemented an update of the minimum wage and completed another commitment in the area of inspections for the supervision of economic activities and product markets:

- In response to the high inflation, the authorities implemented an **increase in the minimum wage** on 1 May 2022, representing a second increase for 2022, following the established, yet advanced and shortened, consultation process. The minimum wage increased by 7.5% on 1 May 2022 ([10]). The increase follows a modest increase of 2% implemented on 1 January 2022, following a three-year freeze of the minimum wage. The authorities followed the steps outlined in amended law 4172/13 for determining the minimum wage. In the context of the consultation process, modest to more significant increases were suggested by the various social partners, research institutes and other contributors to mitigate losses in purchasing power due to the high inflation and to protect low-income workers, given that almost 28% of employees in the country receive a minimum wage. The authorities estimate that the real wage increase in 2022 would not outperform productivity growth – in fact, they expect real compensation of employees per head in the economy as a whole to decrease strongly in 2022 despite the increase in the minimum wage. These estimates are broadly in line with the Commission 2022 spring forecast, which nonetheless expects a stronger impact of the minimum wage on aggregate wage growth overall, while the real compensation of employees per head is also projected to decline. Competitiveness, as measured by unit labour cost ([11]), had improved before the pandemic largely on the back of a decrease in wages and increasingly supported by productivity gains. In 2021, labour productivity ([12]) grew by 7.8% and its growth rate is expected to reach 2.0% on average in 2022 and 2023. Taking this into account together with the expected impact of the minimum wage increase on overall wage growth, Greece's unit labour cost is expected to mildly deteriorate over the same period but less so than in the EU as a whole. Greece's export base nevertheless remains focused on products

([10]) In levels, the minimum wage increased from EUR 663 on 1 January 2022 to EUR 713 on 1 May 2022 calculated on a 14-month basis or EUR 831.8 calculated on a 12-month.

([11]) The unit labour cost (ULC) is defined as the ratio of the nominal compensation per employee to the real GDP per person employed.

([12]) Productivity is defined as the gross domestic product per occupied person.

with a low level of technological sophistication and the exports to-GDP ratio is low, despite recent improvements ([13]).

- The authorities completed the reform of the **inspections framework**, through adopting the last remaining secondary legislation in the area of environmental protection. The legislation allows for the activation of the enforcement management model, a system that helps inspectors to make enforcement decisions in line with predetermined criteria and facilitates a harmonised approach in the application of the enforcement system.

By October 2022, the authorities have committed to deliver the following steps:

- Complete the **legal codification of the labour legislation**. While the codification process has started, the deadline for the adoption of the consolidated texts, which will complete the commitment, has been postponed to October 2022 due to a recent significant reform of the Public Employment Service that needed to be included in the codification process. The draft codified legislation will be presented by June.

- Regarding the **cadastral reform**, cadastral mapping has continued to progress according to plan in the past quarter and 65% of total property rights will be in operation or publicly presented by end-September 2022. The ratification of the forest maps has been further delayed, which could further prolong the timeline for the completion of the cadastre. The delay is due to a recent legal amendment which has removed the status of 'forest', i.e. the presumption of public ownership, from about 5% of the country's area. While this amendment is solving some long-standing issues, it will require a revision of the existing contracts for cadastral mapping and expose the cadastre reform to a risk of new legal challenges. The timeline for the ratification of 95% of the forest maps has been delayed by two months to September 2022 to reflect the new situation. In order to avoid further delays to the completion of the ratification of forest maps and the completion of the cadastral mapping, the authorities have agreed to adopt a legal provision allowing for the withdrawal of public ownership in the above mentioned 5% of Greece's land area. The pace of establishing of the new offices of the Hellenic Cadastre has slowed down due to lack of managerial staff, but their recruitment is in progress. The authorities are urged to adhere to the revised timeline and to complete the full reform by December 2022.

Regarding broader reforms implemented in this reporting period, the authorities adopted the final piece of secondary legislation critical for the implementation of the **public procurement law**. The legislation concerns the set-up of a new legal entity, which will develop and maintain a new integrated system for technical specifications and costing of technical works. The authorities have also prepared and approved in the Council of Ministers a **higher education bill**. The law modernises and enhances the organisational and educational autonomy, flexibility and efficiency of higher education institutions, and decentralises and streamlines their governance. The bill is expected to be tabled to Parliament in June 2022.

([13]) For a detailed analysis on Greece's export performance, see also Commission's 2022 In-depth Review for Greece.

Hellenic Corporation of Assets and Participations and privatisation

In the context of enhanced surveillance, the Hellenic Corporation of Assets and Participations adopted its first two **Strategic Plans in 2018 and 2022**, implemented a range of **governance reforms** for the state-owned enterprises in its portfolio and completed extensive cycles of **board reviews and appointments at these enterprises,** initiated **turnaround interventions** in key state-owned enterprises (though real estate management remains a critical attention point), and began delivering **dividend revenue streams**. The Hellenic Republic Asset Development Fund closed a number of privatisation transactions, including for the **Hellinikon** transaction, the extension of **Athens International Airport concession agreement**, the sale of 66% of the natural gas transmission system operator **DESFA,** and the **Marina of Alimos concession**, for privatisation proceeds amounting to EUR 2.4 billion.

In the current reporting period, the **Hellenic Corporation of Assets and Participations** has started to implement its Strategic Plan approved in January 2022, including board renewals in companies in its portfolio, but some of the actions have been scaled down due to uncertainty as to the Corporation's dividend revenue path. The implementation of the Coordination Mechanism has progressed with the issuance of the secondary legislation necessary for the implementation of the performance contract with the Athens Urban Transport Organisation (OASA) and further steps to update the Statements of Commitments, setting out key performance indicators for state-owned enterprises in the Corporation's portfolio. In the area of privatisation, the **implementation of the Asset Development Plan** has progressed and the updated Plan has been adopted, laying down the next steps for the transactions included in it.

By October 2022, the authorities have committed to deliver the following steps in relation to public asset management and the Corporation:

- Adopt legislation for the **modernisation of the institutional framework for state-owned enterprises,** including the independent commercial operation of companies in the Corporation's portfolio. Following the submission of the draft legislation to Parliament, the reform is expected to be adopted by June. This is expected to be a significant reform strengthening the governance of state-owned enterprises.

- Outline a comprehensive strategy for the **Public Real Estate Company** to achieve an ambitious yield for the entire real estate portfolio. The Corporation expects this to be ready by end-May 2022.

- Launch the detailed feasibility study for the **Olympic Athletic Centre (OAKA)**, as part of its future transfer to the Hellenic Corporation of Assets and Participations. The authorities expect this to be done by June 2022.

- Complete **the transfer of the eligible real estate assets** included in the 2018 package of the Public Real Estate Company.

Specifically regarding privatisation transactions under the Asset Development Plan, the authorities will actively seek to make progress in the follow areas:

- The Hellenic Republic Asset Development Fund (TAIPED) is close to completing the privatisation of the **Public Gas Corporation (DEPA)** Infrastructure which is expected to be successfully privatised for a considerable financial offer of EUR 733 million (for the 65% stake of the Fund this corresponds to EUR 476 million). The privatisation transaction is of significant importance as the purchaser, an Italian company, is expected to contribute to improving and expanding the gas distribution network of the country.

- Despite some progress, the works to finalise the construction works and licensing of tunnels on the **Egnatia** highway are accumulating delays and there is a risk that the highway will not be ready for the handover to the selected concessionaire by end-2022, as originally planned. This could result to compensations having to be paid by the state to the concessionaire, with the concessionaire assuming the works for construction and licensing and the related costs. The concession is worth an upfront payment of almost EUR 1.5 billion, on top of regular annual payments by the concessionaire.

- The ongoing tender process for the concession of the **underground natural gas storage in South Kavala**, which is particularly important in view of improving security of energy supply, can move ahead only once the Regulatory Authority for Energy issues a decision regarding its tariff setting framework. This decision has suffered delays and is now expected to be issued by end-May 2022.

- Other ongoing transactions, in particular those for the **regional ports** and the '**Gournes Heraklion**' (development of part of the former American military base on Crete) are progressing well. The authorities will continue with the implementation of the Asset Development Plan.

<u>Public administration</u>

In the context of enhanced surveillance, the authorities completed the appointment of **Permanent Secretaries** and all **Directors General** as part of the efforts to depoliticise the public administration, the envisaged cycles of **mobility and performance appraisals**, and key elements of the **integrated Human Resources Management System**, namely digital organisational charts and job descriptions, for the public administration. In view of enhancing legal certainty and access to law through legal codification, the authorities has awarded a contract that is expected to put in place a **National Gateway for Codification** by 2024. It also completed the implementation of its national **anti-corruption plan** for 2018-2021.

In the current reporting period, the authorities completed another commitment in the area of the fight against corruption:

- The authorities have put in place significant measures to implement the remaining three recommendations from the fourth evaluation round of the **Group of States against Corruption** (GRECO). Many of the measures will be introduced through the Code on the Organisation of Justice and the Status of Judges, which was submitted to the General Secretariat for Legal and Parliamentary Affairs on 13 May and is to be tabled to Parliament by end-May 2022. GRECO will formally reassess the recommendations in its 2023 report.

Regarding broader reforms implemented in this reporting period, the authorities have made progress to strengthen control over hiring and salaries of public officials. First, a needs assessment for permanent and temporary teachers has been prepared and is expected to be completed by end-May 2022, following the review by the Ministry of Education and Religious Affairs. This is expected to improve predictability of such positions, which in the past had led to large increases in temporary positions, which were often converted to permanent posts. Second, the authorities prepared legal amendments to address a number of observed deviations from the unified wage grid, which are expected to be adopted by end-May 2022. These include provisions to ensure consistent application of the remuneration for management posts and travel expenses. A new methodology for granting allowances for hazardous and arduous jobs has been finalised and is planned to be in place by August 2022. Finally, the appointment process for the Permanent Secretary post at the Ministry of Education and Religious Affairs has been launched and is expected to be completed by July 2022.

MACROECONOMIC DEVELOPMENTS

Despite the prolonged uncertainty due to the successive waves of the pandemic, the Greek economy recovered quickly in 2021, offsetting almost entirely the sharp economic decline from 2020. Greece's real GDP grew by 8.3% in 2021, reflecting the better-than-expected tourism season, while private consumption recorded almost a full recovery to its pre-pandemic levels, on the back of the effective emergency income support implemented by the government and the use of accumulated savings. Growth was also driven by a notable boost in private investment, supported by the government support measures to businesses, and the gradual rollout of actions under Greece's recovery and resilience plan as well as the European Social Fund and the Cohesion Fund. Goods exports continued growing, as the country benefits from the recovery in the EU and other trading partners. At the same time, increasing energy prices continue to affect real incomes and the current account deficit. Driven especially by the international energy price hikes, headline inflation increased considerably to 9.4% in April 2022, following an average rate of 0.6% in 2021.

The economic developments in the first months of 2022, before Russia's military aggression against Ukraine, signalled that the recovery in Greece was gaining traction. High frequency indicators for the first two months of 2022 pointed to increased private spending, while economic sentiment remained strong until end-February, as reflected both in consumers' and business confidence. Early indications for tourism showed that Greece was heading for a strong season, while the government was implementing support measures to partially cushion the negative effects from high energy prices on disposable income.

Russia's invasion of Ukraine is forcing a reassessment of the economic outlook for all Member States, including Greece. The war is expected to affect the Greek economy through three main channels. First and foremost, the war has further increased global energy prices, which are expected to aggravate domestic inflationary pressures and erode the real disposable income of households. However, the government support measures, the increase in the minimum wage from May 2022, and the still large accumulated savings are expected to partially cushion the negative effects on private consumption. Secondly, while the direct exposure of the financial sector to Russia is very limited, the heightened uncertainty and risk aversion, along with increased supply bottlenecks may delay the kick-off of some new investment projects. Finally, export growth is likely to decrease in view of the slowdown projected for the EU and the global economy as a whole. Tourism is nevertheless expected to remain resilient, as the tourists coming from Russia, Ukraine and Belarus represent only a small share in the total number of tourists. Against this background, the Commission 2022 spring forecast projects that real GDP would grow by 3.5% in 2022 and 3.1% in 2023.

Inflation is expected to peak in the second quarter of 2022 and remain high thereafter, before easing in 2023. The main drivers of the rise in inflation are the increasing international oil and gas prices, while food prices are affected by a surge in key input costs, such as fertilizers and transport. Headline inflation is projected to reach 6.3% in 2022, and 1.9% in 2023.

The situation in Greece's labour market has further improved, but unemployment remains one of the highest in the EU. The targeted employment support measures in sensitive sectors have allowed employers to retain employees following the outbreak of the coronavirus crisis and facilitate the recovery of the economy. Job creation showed a strong growth in the second half of 2021, which is expected to continue also in 2022, despite the overall slowdown in economic activity due to the inflationary pressures in that year. According to the Commission 2022 spring forecast, the unemployment rate is forecast to, reach 13.7% and 13.1% in 2022 and 2023, respectively. Long-term unemployment – in a downward trend since 2015 – further decreased from 10.5% in 2020 to 9.2% in 2021. The increase in the minimum wage as of May 2022 is set to support nominal wage growth in the second half of the year, given that almost 28% of employees in the country receive a minimum wage ([14]). The tax cuts announced for 2023 are expected to have a positive effect in disposable income, investment, and employment (see section on fiscal developments below).

Russia's military aggression against Ukraine has magnified the downside risks surrounding the economic outlook. The forecast relies on technical assumptions concerning the duration and severity of the global energy price hikes and the disruptions in the global value chains. Estimates for the spending outlook of domestic households and the investment dynamic are highly sensitive to these assumptions. A disruption of the supply of energy resources to Greece represents another downside risk. Uncertainty also concerns the tourist season, as real household disposable incomes in countries, from where tourists originate, may be reduced by inflation, although early bookings remain strong. On the upside, the strong performance in exports of goods over the previous period of heightened supply-side disruptions indicate that Greece's exports have become resilient, which could result in a stronger outlook for the external performance of the country.

([14]) Bank of Greece, Evaluation of the current legislated minimum wage increase, April 2021.

Table 1: **Summary of main macroeconomic variables (%)**

	2021	2022	2023
Real GDP growth	8.3	3.5	3.1
Employment growth	0.5	1.2	1.2
Unemployment rate	14.7	13.7	13.1
Harmonized index of consumer prices growth	0.6	6.3	1.9

Source: European Commission

FISCAL DEVELOPMENTS

Greece's primary deficit monitored under enhanced surveillance reached 5.5% of GDP in 2021. This is 2.1 percentage points lower than projected in the Commission's 2021 autumn forecast. The improvement is attributable mainly to faster growth of nominal GDP as well as a more favourable evolution of tax bases, especially of corporate and personal income. This explains around 1.8 percentage points of the improvement. Also related to the recovery, spending on social benefits was less than anticipated.

Most fiscal measures adopted to mitigate the social and economic costs of the pandemic will be phased out in 2022. Most of the measures have already been lifted by May 2022 and the remaining ones will be gradually phased out until the end of the year, e.g. an extended recruitment subsidy programme to create 50 000 new jobs by subsidising social security contributions for six months for each new employment contact and increased healthcare expenditure partly linked to the vaccination campaign. The fiscal impact of the pandemic-related measures is expected to reach 1.8% of GDP in 2022, down from 7.2% of GDP in 2021.

In light of the surging energy prices, the government has adopted significant temporary measures to mitigate their negative impact on households and businesses. The total volume of these measures are estimated at 2.3% of GDP in 2022 but their direct budgetary impact is limited to 1.1% of GDP as part of these expenditures is covered by the windfall revenues from the renewable sources prompted by the increase in electricity prices (1.2% of GDP). These measures include:

i) Measures to alleviate the increased cost of *electricity consumption and of gas used for heating:*

   They consist of subsidies to households and enterprises linked to the excess of current electricity prices over a given threshold. For households, the subsidy covers on average 80% of the price increase above the threshold (i.e. 90% of the increase for the first 150 KWh consumed monthly and 70% of the increase for the next 150 KWh), while the coverage is 95% for vulnerable households. No subsidy is given for the part of consumption above 300 KWh. Enterprises benefit from a subsidy, which covers 40% and 30% of the price increase in the first and second semester of 2022, respectively. Very small enterprises were granted an additional subsidy for the first four months of 2022, covering in total 80% of the price increase for the consumption of this period. The authorities also granted an additional heating allowance to alleviate the impact of the sharp increase in natural gas prices for the period January-April 2022. The total size of these subsidies are expected to reach 1.9% of GDP until the end of the year with an expected budgetary cost of 0.7% of GDP. The level of the above-mentioned subsidies is determined by a formula which ensures that the measure is temporary and will expire once the energy prices would fall below a given threshold. The authorities plan to use the increased revenues from the emissions trading system to cover the expected budgetary cost of the measure.

ii) Measures addressing the *impact of high inflation on vulnerable households:*

A voucher of EUR 200 was granted to vulnerable households including low-income pensioners, beneficiaries of disability benefits and non-insured older people. An additional instalment of the guaranteed minimum income and child benefit were paid in April 2022 in order to mitigate the impact of increased inflation. In addition, a subsidy was granted to breeders of animals to compensate the increased cost of animal feed. The fiscal cost of these one-off payments is estimated at 0.2% of GDP in 2022.

iii) Measures addressing the impact of the *high fuel prices:*

The authorities decided to subsidise, for three months, the cost of fuel to individuals with a declared annual family income of up to EUR 30 000 in the form of a pre-paid card worth of EUR 40. In addition, the diesel price is subsidised with EUR 0.12 per litre while taxi drivers received a one-off benefit of EUR 200 for the increased fuel costs. The fiscal cost of these measures is expected to reach 0.1% of GDP in 2022.

iv) Targeted *tax cuts*:

The authorities decided to extend the reduced value added tax rate for transport until December 2022, which would otherwise expire in June 2022, to decrease the value added tax rate for agricultural fertilizers from 13% to 6% from April 2022 onwards, and to refund the special levy on diesel for farmers collected for 2022. The loss in revenues is estimated at 0.1% of GDP.

Given that the expenditures are expected to exceed the original budget ceilings, the authorities adopted a supplementary budget of EUR 2 billion (1.0% of GDP) in early-April. This allows for increased spending on measures and costs for general government entities related to the high energy prices. To cater for uncertainty the Commission assumes additional appropriations of 0.4% of GDP for 2022, which are also included in Greece's Stability Programme projections. These appropriations are expected to be voted through a second supplementary budget by September 2022.

The Commission 2022 spring forecast expects that the primary balance will be in deficit of 1.9% of GDP in 2022 and reach a surplus of 1.3% of GDP in 2023, which is aligned with the projection of the authorities. The improvement in the budgetary position compared to 2021 is mainly due to the ongoing economic recovery and the phasing out of the fiscal support measures. Greece's 2022 Stability Programme has very similar projections, with a projected primary deficit of 2.0% of GDP in 2022 ([15]) and a primary surplus of 1.1% of GDP in 2023.

The forecast factors in the authorities' plan to make permanent two growth-friendly tax cuts in 2023, the implementation of which is presented in the Stability Programme as contingent on compliance with the applicable EU fiscal rules. The authorities indicated in their Stability Programme that they intend keep in place as of 2023 the current reduced rate of social security contributions and of the solidarity surcharge. These measures aim to reduce the high tax burden on households (before the pandemic, the tax wedge on labour in Greece was two percentage points higher than the euro area average [16]), support labour demand and boost households' disposable income, which is expected to have a positive effect on consumption and the economic recovery in general. They build on measures originally introduced for 2021 and 2022 to alleviate the impact of the pandemic, which would expire at the end of this year. In particular, the measures make permanent the temporary three percentage point reduction in the social security contribution (1.8 percentage points of which is a cut in employers' contributions and 1.2 percentage points in employees' contributions) and the waiver of the solidarity surcharge granted during the pandemic. The solidarity surcharge applies to a different tax base compared with the personal income tax, which offers scope for further simplification of the tax system. The fiscal cost of these measures is estimated at 0.8% of GDP per year. According to the Stability Programme, the implementation of this policy action is contingent on its compliance with the European fiscal rules applicable from 2023 onwards.

Following the submission of Greece's Stability Programme and the cut-off date of the Commission 2022 spring forecast, the government announced a new package of measures which aim to address the consequences of increased energy prices. First, Greece announced a new mechanism to reduce the wholesale electricity price, which will be introduced as of 1 July 2022. Second, the existing subsidy scheme (see point i) above) will continue to apply until the end of 2022 and will be expanded from May 2022 to cover a larger share of the price increase for monthly consumption up to 300 KWh, monthly consumption above 300 KWh, and all residencies, i.e. not only the main residency. Finally, a retroactive subsidy will be issued to cover 60% of the electricity bills from December 2021 to May 2022 for the main residency. The size of these measures is projected to reach 0.4% of GDP in 2022. The authorities intend to cover the cost of these measures as well as the loss of revenues from the renewable sources due to the reduction of the wholesale price by a newly imposed extraordinary 90% levy on windfall revenues of the energy producers for the period from October 2021 to June 2022 (0.3% of GDP) and by the use part of the reserve (0.4% of GDP), which was already included in the Commission 2022 spring forecast. Commission's services are currently assessing the compliance of the new measures with the guidance

([15]) The fiscal deficit monitored under the enhanced surveillance is projected at 1.9% of GDP in 2022. The adjustments agreed under the enhanced surveillance framework are applied only until 2022.

([16]) Tax wedge for a two-earner couple with two children, with the principal earner earning the average wage while spouse earning 67% of the average wage. European Commission, DG TAXUD, Tax and benefits indicators database, 2022.

provided in the Commission Communication on REPowerEU ([17]) and relevant EU legislation.

Notwithstanding the better-then-expected outturn of 2021, fiscal risks remain substantial. The uncertainty surrounding the energy markets constitutes the biggest risks to the forecast because it might increase the cost of the energy subsidies and create pressures for additional support measures, even if increased revenues due to increase in energy prices would somewhat mitigate the cost. As regards the pandemic, while the short-term risk of extending further the existing emergency measures is fading out, the risk of the guarantees issued as part of the support measures to be called in the coming years still remains. The recent or planned financial policy arrangements, including the sale and lease-back scheme for properties owned by vulnerable debtors, may entail a deficit- and debt-increasing impact depending on their final statistical classification. Additional risks stem from the pending legal cases, most notably the case on the retroactive compensation for cuts in the supplementary pensions and seasonal bonuses and litigation cases against the Public Real Estate Company (ETAD). On the upside, corporate profitability may continue to outperform expectations as it did for the 2021 fiscal outcome.

SOVEREIGN FINANCING

Greece repaid its outstanding International Monetary Fund loans ahead of time. Greece executed the early repayment of its remaining loans towards the Fund at the beginning of April 2022. The amount of the repayment reached EUR 1.9 billion. These loans would have matured mainly in 2023-2024 under the original schedule. The early repayment was made possible by Greece's improving financial position, favourable financing conditions and its high cash buffer. Greece is expected to make a partial early repayment of its loans under the Greek Loan Facility towards the end of 2022.

The cash buffer remains high, supported by a new bond issuance and by the first instalment of the Recovery and Resilience Facility. At the end of April 2022, Greece has successfully raised EUR 1.5 billion on the market by re-opening the books of the 7-year bond maturing in 2027. The achieved yield was 2.4%, which reflects that yields and spreads over the German Bund have remained relatively high compared to their level during the pandemic. The cash buffer reached about EUR 38 billion in the middle of April 2022 ([18]). This amount includes the first instalment of the Recovery and Resilience Facility worth EUR 3.6 billion which Greece received on 8 April 2022. Greece credit rating was upgraded to BB+ with stable outlook by Standard & Poor's at the end of April 2022 on account of the continuous improvement in Greece's policy effectiveness. With this, the country's rating by Standard and Poor's is only one notch away from investment grade.

([17]) Commission Communication on REPowerEU: Joint European Action for more affordable, secure and sustainable energy, COM(2022) 108

([18]) The cash buffer account balance remained at EUR 15.7 billion. The cash buffer account was built also through disbursements under the third financial assistance programme and is dedicated to debt service. Greece may use this amount for other purposes as well, following an approval of the European Stability Mechanism's governing bodies.

DEBT SUSTAINABILITY ANALYSIS

Following the publication of the Commission Fiscal Sustainability Report ([19]), **the methodology used for the debt sustainability analysis for Greece has now been fully aligned with the Commission's horizontal approach used for all other Member States.** The current methodological update follows the alignment of the macroeconomic and interest rate assumptions already presented in the 12th enhanced surveillance report to the Commission's horizontal approach and concerns the assumptions for the fiscal policy. The fiscal assumption used so far in enhanced surveillance reports assumed a primary balance of 2.2% of GDP beyond the short-term forecast horizon, to be reached on average over the 2023-2060 horizon. This assumption was projected to be compliant with the Stability and Growth Pact based on an assessment performed in June 2018 on the basis of data available at that time. The revised methodology implements the no-policy-change fiscal assumption applied to all Member States in the Commission Fiscal Sustainability Reports and Debt Sustainability Monitors. In particular, it assumes that the structural primary balance remains constant as of the last forecast year (in this case 2023) ([20]).

The no-policy-change fiscal assumption implies on average a higher nominal primary balance than the previous assumption over the full projection horizon. Table 2 compares the primary balance assumptions applied in the previous report and the one applied in this one. In the short term, both follow the Commission 2022 spring fiscal forecast. The assumption of a constant structural primary balance implies, for the period between 2024 and 2026, a considerably higher primary balance than the one assumed earlier, on account of the positive and widening output gap forecast and the savings on public pension expenditure stemming from previous pension reforms (i.e. a lower cost of ageing). From the late 2020s, once the output gap closes, the primary balance decreases, but remains slightly above the previous assumption until the late 2050s, as implied by the current forecast of the structural primary balance and ageing cost assumptions. Towards the end of the horizon, a further decline in cost of ageing – other things equal – drives a significant improvement in the primary balance, reaching 3.6% in 2060 ([21]). The Commission horizontal approach assumes that reforms related to the pension system result in the fiscal savings presented in the 2021 Ageing Report ([22]) and all related savings are used for debt repayments.

([19]) This alignment was first implemented in the Fiscal Sustainability Report 2021, Institutional Paper 171.

([20]) The fiscal path for 2022-2023 is aligned with the Commission 2022 spring forecast. Beyond 2023, the primary balance applied in the present analysis is derived from the structural primary balance forecast for 2023 by adjusting it with the cyclical component, the cost of ageing, pension related taxes and property income.

([21]) On the back of the previous pension reforms, Greece's pension expenditure is assumed to decrease from 15.7% of GDP to 12% of GDP between 2019 and 2060.

([22]) The 2021 Ageing Report: Economic and Budgetary Projections for the EU Member States (2019-2070), Institutional Paper 148.

Table 2: Changes in the fiscal assumption

		2022	2023	2024	2025	2030	2040	2050	2060	average 2023-2060
Primary balance (% of GDP)	Previous methdology	-1.9	1.3	2.2	2.2	2.2	2.2	2.2	2.2	2.2
	Current methdology (baseline)	-1.9	1.3	2.7	3.4	2.5	2.3	2.3	3.6	2.6

Source: *Commission services*
Note*: The primary balances presented in this table is in terms of the European System of Accounts 2010 and are based on the Commission 2022 spring forecast for 2022-2023.*

Table 3: Main assumptions of the baseline scenario – draft

		2022	2023	2024	2025	2026	2030	2040	2050	2060	average 2023-2060
Assumptions	Primary balance (% of GDP)	-1.9	1.3	2.7	3.4	3.7	2.5	2.3	2.3	3.6	2.6
	Real GDP growth	3.5	3.1	2.7	1.9	1.1	0.9	1.7	1.6	1.5	1.5
	Nominal GDP growth	8.4	5.2	4.9	4.1	3.4	3.3	4.0	3.6	3.6	3.7
	Re-financing rate (10 year maturity)	2.2	2.2	2.2	2.2	2.2	2.2	3.0	3.9	4.0	3.1
Results	Gross financing needs (% of GDP)	19.2	14.4	8.2	7.6	12.8	11.2	11.6	10.0	5.1	
	Gross goverment debt (% of GDP)	185.7	180.4	172.0	164.9	159.8	141.1	97.8	62.4	31.6	

Source: *Commission services*
Note*: The primary balance presented in this table is in terms of the European System of Accounts 2010 and is based on the Commission 2022 spring forecast for 2022-2023.*

Table 4: Main assumptions of the scenarios - draft

		2022	2023	2024	2025	2030	2040	2050	2060	average 2023-2060
Nominal GDP growth (%)	Baseline scenario	8.4	5.2	4.9	4.1	3.3	4.0	3.6	3.6	3.7
	Higher risk premium scenario	8.4	5.2	4.9	4.1	3.3	4.0	3.6	3.6	3.7
	Low growth scenario	8.4	5.2	4.9	4.1	3.3	3.3	3.0	3.0	3.2
	Lower structural primary balance scenario	8.4	5.2	4.9	4.1	3.3	4.0	3.6	3.6	3.7
Re-financing rate (%)	Baseline scenario	2.2	2.2	2.2	2.2	2.2	3.0	3.9	4.0	3.1
	Higher risk premium scenario	2.2	2.2	2.2	2.2	3.3	3.4	3.9	4.0	3.5
	Low growth scenario	2.2	2.2	2.2	2.2	3.3	3.6	4.3	4.2	3.7
	Lower structural primary balance scenario	2.2	2.2	2.2	2.2	2.2	3.0	3.9	4.0	3.1
Primary balance (% of GDP)	Baseline scenario	-1.9	1.3	2.7	3.4	2.5	2.3	2.3	3.6	2.6
	Higher risk premium scenario	-1.9	1.3	2.7	3.4	2.5	2.3	2.3	3.6	2.6
	Low growth scenario	-1.9	1.3	2.7	3.4	2.5	2.3	2.3	3.6	2.6
	Lower structural primary balance scenario	-3.2	-0.9	0.5	1.2	0.3	0.1	0.1	1.4	0.4

Source: *Commission services*
Note*: The primary balances presented in this table is in terms of the European System of Accounts 2010 and are based on the Commission 2022 spring forecast for 2022-2023.*

The update of the debt sustainability analysis results in a significant downward shift of the debt and gross financing needs trajectories in all scenarios reflecting the lower starting point, higher inflation expectations ([23]) and the new fiscal path based on the no-

([23]) To recall, the GDP deflator in the analysis is aligned with the Commission 2022 spring forecast for the years 2022-2023 and assumed to converge thereafter to the euro area inflation currently expected by the markets for 2031. Beyond that, inflation is assumed to converge to 2% by 2051 and remain constant afterwards.

policy-change assumption ([24])**.** In 2021, the debt-to-GDP ratio reached 193%, which is 10 percentage points lower than expected in the previous report. This improvement was primarily due to the higher-than-expected nominal GDP, but also to the lower-than-expected primary deficit. Overall, given the high level of debt, the debt sustainability analysis indicates high risks over the medium term ([25]). In the baseline scenario, the debt-to-GDP ratio decreases to around 32% in 2060, while gross financing needs decline below 10% in the long run ([26]). One of the main driving factors of the change compared to the previous report is the faster increase of nominal GDP, especially over the short and medium-term, which is principally driven by the surge in inflation also reflected in market-based inflation expectations. This improvement is not fully offset by the increase in interest rates, because of the very long weighted average maturity of the Greek debt, which cushions the impact of market interest rate movements in the short and medium term. The other major contributor to the updated results is the fiscal trajectory based on the no-policy-change assumption. Given the forecast structural primary balance of 1.4% of GDP for 2023 and the assumptions on cost of ageing developments, the fiscal trajectory from 2023 to 2060 is on average 0.4 percentage points higher than the previous assumption of 2.2% of GDP. In the higher-risk-premium scenario, debt decreases to 42% of GDP in 2060 and gross financing remain below 10% of GDP in the long run. Even in the low-growth scenario ([27]) debt ratio remains on a downward trajectory in the long run, and gross financing needs remain below 20% of GDP. To cater for fiscal policy risks, a fourth scenario assumes a lower primary balance trajectory ([28]). This scenario implies a significantly lower primary balance averaging at 0.4% of GDP for the period 2023-2060. In this scenario, debt still remains on a downward trajectory, but declines at a much slower pace than in the other scenarios, remaining above 100% of GDP by the end of the projection horizon. Gross financing needs are also more elevated, hovering around 15% of GDP in the medium-term, and slightly above 20% of GDP in the long term.

([24]) Note, however, that following the technical update of the DSA for the latest macroeconomic data, the debt trajectory would be on a firmly downward path also under the previous fiscal assumption (i.e. a primary balance of 2.2% of GDP), and gross financing needs would remain below 20% of GDP in all three scenarios.

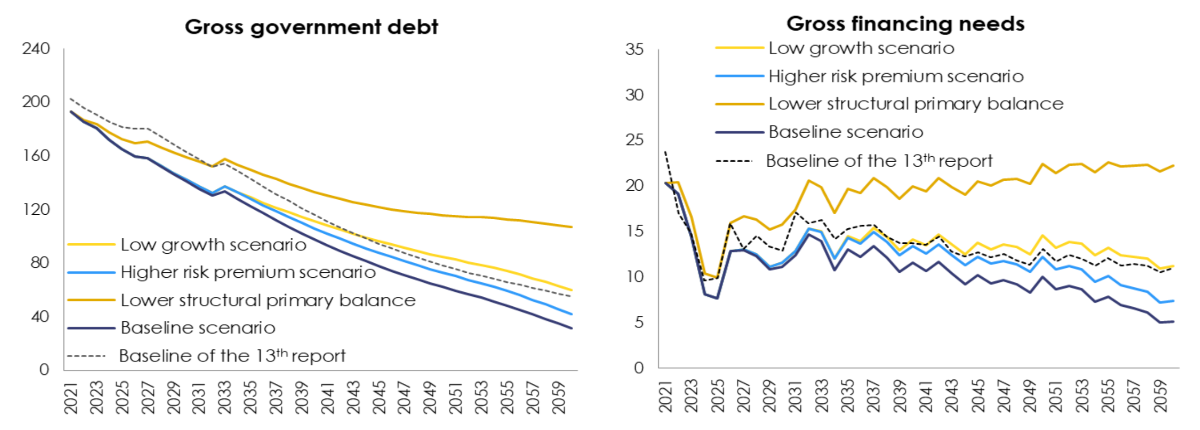
([25]) Country Report Greece 2022, SWD(2022) 609 final, Annex on *Debt Sustainability Analysis*.

([26]) The baseline scenario follows the methodology applied to all other Member States and is an update to the analysis which was published in the 2021 Fiscal Sustainability Report. The alternative scenarios presented here complement the analysis.

([27]) As in previous reports, the low-growth scenario builds on the higher risk premium scenario, but assumes a lower real GDP growth in the long run.

([28]) The "lower structural primary balance" scenario is part of the set of standard alternative scenarios used in the European Commission's horizontal framework, and was published in the 2021 Fiscal Sustainability Report for the previous vintage. This scenario builds on the baseline scenario and assumes that throughout the whole projection period the structural primary balance level is reduced by half of the cumulative forecast change over 2021-2023 in the Commission 2022 spring forecast.

Graph 1: **Results of the debt sustainability analysis**



Source: Commission services

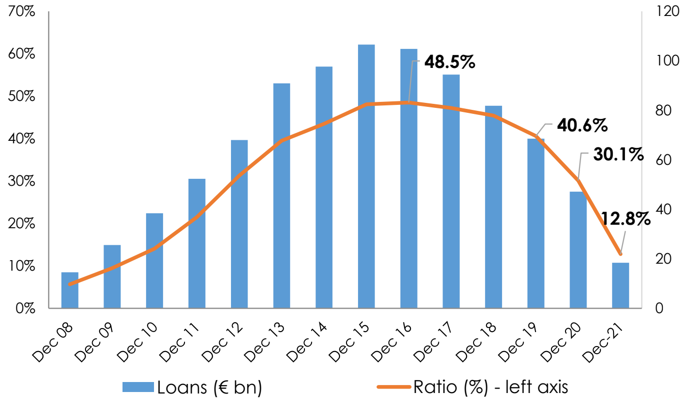
The assessment of debt sustainability hinges on the underlying assumptions and is subject to considerable uncertainty linked in particular to the current inflationary shock. The new fiscal path implies on average a significantly higher primary surplus than under the previous fiscal assumption. Achieving and maintaining an average primary balance of 2.6% over close to 40 years is highly ambitious and would require fiscal discipline that is unprecedented in almost all EU Member States. The no-policy-change fiscal assumption represents the current fiscal policy setting and will be revised following each Commission forecast. As highlighted by the lower structural primary balance scenario, where sustainability risks are more pronounced, fiscal prudence is key for ensuring debt sustainability. As regards inflation, should its current surge be less persistent than assumed based on the current methodology and market expectations, it would lead to a higher debt trajectory on account of lower nominal growth. Regarding real growth, Greece's potential growth has recently been below the long-run growth assumed in both the baseline and the lower growth scenarios, which include the expected growth impact of the investments under the Recovery and Resilience Facility based on the Commission's standard T+10 simulations adjusted on the basis of the QUEST model up to the 10th forecast year, and are anchored to the macroeconomic assumptions of the 2021 Ageing Report thereafter ([29]). Achieving the higher projected potential output growth rates will require the implementation of structural reforms and strong growth-enhancing investments, including those presented in Greece's resilience and recovery plan. They are also key to sustaining favourable interest rates in the long run.

([29]) See Commission (2020), The 2021 Ageing Report, "Underlying assumptions & projections methodologies", November 2020. These assumptions reflect the reforms affecting the sustainability of public finances in the long run (such as pension reforms, and health and long-term care measures), demographic projections with an impact on participation rates and labour market variables, and the assumption of convergence in labour productivity across Member States.

FINANCIAL SECTOR DEVELOPMENTS

Greek banks have completed an outstanding year in non-performing loan reduction, as the focus gradually moves to the workout of non-performing debt for viable debtors, where feasible. The non-performing loans ratio stood at 12.8% on a solo basis in December 2021, having declined strongly from 30.1% at end-2020 and 40.6% at end-2019. Two of the four systemic banks have recorded a single-digit non-performing loan ratio as of end-2021, while the other two are expected to meet the same target at the latest by the end of 2022. The main driver behind this rapid fall in the stock of non-performing loans, which has dropped to EUR 18.4 billion from its peak level of EUR 107.2 billion (end-March 2016) ([30]), have been the securitisation transactions under the Hercules Asset Protection Scheme. Three more securitisation transactions by systemic banks remain still in the pipeline ([31]) and are expected to be completed on time. The cost for the originating banks for future transactions will increase, because of rising guarantee fees due to the impact of the war in Ukraine on credit default swap spreads. Future efforts to move the non-performing loan ratio closer to the EU average will increasingly rely on the banks' offering of new loans (denominator effect), as well as the management of loans in or at risk of default and their ability to offer viable long-term solutions. At the same time, effective collateral recovery will be crucial when successful restructuring is not feasible.

Graph 2: **Evolution of the stock of gross non-performing loans and the non-performing loan ratio of Greek banks**



Source: *Bank of Greece*
Note*: Gross non-performing loans as a share of total customer loans, for on-balance-sheet loans in accordance with European Banking Authority's definitions.*

Net creation of new non-performing loans continues at a limited rate, as risks to banks' asset quality persist. Net inflows ([32]) of non-performing loans continued in the fourth quarter of 2021, for the fifth quarter in a row, albeit at a more limited rate. Banks' 'step up'

([30]) Source: Bank of Greece.
([31]) The loan portfolio under one of these three securitisations was classified as held for sale by the respective bank as of end-2021 and hence is already reflected in the improvement of the non-performing loan ratio at the end of 2021. Moreover, beyond these three planned transactions by systemic banks, two less-significant institutions are reportedly interested in making use of the Hercules Asset Protection Scheme within 2022.
([32]) See footnote 9.

products offered to viable customers facing temporary difficulties and the remaining payment moratoria granted to the hospitality sector have almost completely expired at the end of 2021, while the material number of loans benefitting from state-support measures through the "Gefyra" and "Gefyra II" schemes ([33]) are gradually exiting the schemes in the first half of the year. Banks continue to report a stable and limited default and re-default rate for loans after exiting moratoria and the initial signs point to similar default rate for loans exiting the "Gefyra" schemes and somewhat higher rates for those exiting banks' 'step up' products. However, the first solid results after the end of these support measures will not be available before the end of June 2022. In addition, although the direct or indirect exposure of the Greek banking sector to Russian or Ukrainian residents is limited, there are downside risks for banks' asset quality stemming from potential second round effects on the economic outlook and the real disposable income of households related to Russia's unprovoked invasion of Ukraine.

The successful resolution of legacy private non-performing debt increasingly depends on servicers in charge of servicing securitised and sold loans. The non-performing debt that has exited the banks' balance sheets remains in the hands of specialised non-bank financial institutions (i.e. servicers), which managed EUR 79.7 billion of predominantly non-performing loans as of end-December 2021, large part of which in the form of securitised non-performing loan portfolios under the Hercules scheme. These institutions aim to maximize recoveries through restructurings, and if not feasible, liquidations. The pandemic has complicated the smooth execution of the servicers' business plans for some of the securitised non-performing loan portfolios. The new out-of-court workout tool and the normalisation of the debt enforcement process, which has started in the fourth quarter of 2021, is also expected to facilitate servicers' efforts to meet business plan targets. Moreover, in order to improve cash flow generation for some of these vehicles, servicers are considering targeted sales of loan portfolios. The gradual development of a secondary market for these loans is expected to facilitate bank refinancing of debtors that will undergo restructuring and become re-performing, possibly allowing them under certain conditions to enter again the banks' loan books in the future.

The banks' core profitability has improved with one-off items weighing on results. All four banks booked profits in 2021 when excluding one-off events. The results of two systemic banks were affected by the one-off losses deriving from the clean-up of non-performing loans. Nevertheless, according to banks' own calculations, all recurring operations have been profitable, which indicates a gradual return to profitability. Robust growth in fees and commissions has helped to largely offset pressures on interest revenues due to the low interest rate environment and the completion of non-performing loans securitisations ([34]), while improving the quality of the revenue mix. Given their significant

([33]) The two "Gefyra" schemes are temporary instalment subsidy schemes set up by the authorities for performing or restructured coronavirus-affected debtors.

([34]) Securitisations of non-performing loans lead to a recurrent loss of net interest income, as they result in the loss of the accrued interest income from the transferred non-performing loan portfolios. However, as accrued interest income is interest income earned but yet to be received, the average quality of the bank's recurrent holdings of domestic sovereign bonds, systemic banks have taken measures to mitigate the impact of potential increases in sovereign yields on their profitability. On the cost side, banks continue their efforts to contain staff costs. The current market uncertainty has had an adverse effect on the long-term unsecured funding costs of the banks and may affect their strategy for further debt issuances in order to meet the minimum requirement for own funds and eligible liabilities (MREL) ([35]), both in terms of timing and type of instruments issued. The banks envisage to counterbalance potential pressures on their cost of funding due to these factors by the implementation of business plans, which take into account the prospects for credit growth, the reduced impairments following recent efforts to reduce non-performing loans, and the development of alternative sources of revenue by accelerating the banks' digital transformation. Banks have maintained their ambitious business plan targets for sizeable new lending, despite the downside risks stemming from any second-round effects of the current geopolitical uncertainty and high energy costs on credit demand. At the same time, the nature of the demand for credit by corporates may shift towards working capital rather than the financing of investment needs.

The clean-up of the banks' balance sheets continued to impact on bank capital positions but the outlook for 2022 benefits from reduced provisioning needs ([36]) and stronger internal capital generation through increased profits. Banks' average Common Equity Tier 1 and Total Capital ratios stood at the end of 2021 at 12.6% and 15.2% of risk-weighted assets on a consolidated basis, respectively ([37]). Banks' capital position was still lower than end-2020 (15.0% and 16.6%), reflecting the cost of non-performing loan deleveraging and the phasing out of transitional prudential adjustments ([38]). The capital position of the banks in 2021 has been supported by two banks' successful share capital increases and some synthetic securitizations ([39]). Further upcoming capital enhancing actions are expected to materialize in 2022, while the banks' capital position is expected to benefit also from organic profit generation, through increased profits. As the bulk of non-performing loan reduction actions are completed, the impact of non-performing loan clean-up on capital positions is expected to diminish. However, the capital position remains one of the lowest in the EU and its quality continues to be a concern, as it contains a high and increasing share of deferred tax credits (circa 64% of supervisory capital at end 2021 at consolidated level).

The outlook for credit growth has become more uncertain, although banks' credit

net interest income will improve once the offloaded non-performing loans are replaced with profitable new lending.

([35]) Binding MREL targets are established by the resolution authorities on a bank-by-bank basis on the basis of the provisions of the Bank Recovery and Resolution Directive (2014/59/EU) and the Single Resolution Mechanism Regulation (806/2014/EU) and their subsequent amendments.

([36]) The need for provisions set aside for potential losses on new loans granted is reduced as the average quality of the banks' loans improves.

([37]) Source: Bank of Greece (provisional data).

([38]) These transitional arrangements refer to the phasing in of the new accounting standards on impairments of financial assets and the implementation of new rules leading banks to more quickly write down non-performing exposures, according to Regulation (EU) 2019/630 amending Regulation (EU) No 575/2013 and relevant supervisory guidance.

([39]) Share capital increases were concluded by two systemic banks in early May and early July. Third quarter figures do not reflect yet a share capital increase undertaken by a less-significant bank in December 2021.

expansion plans remain ambitious. The average annual rate of growth in credit to non-financial corporations remained almost unchanged in 2021 (5.7%) in comparison to 2020 (5.6%). However, net credit towards firms has registered a gradual slowdown in the second half of 2021, which continued at the beginning of 2022, with an annual growth of 3.4% in March 2022, down from 8.7% in March 2021. Credit growth to large corporates has taken the lead in the last quarter of the year, as SME credit growth seems to be lagging behind. Net credit growth to households, particularly mortgages, remains steadily negative, despite an increase in gross credit flows in 2021. The average cost of bank lending to businesses continued to fluctuate at historical lows and has decreased to 2.76% in February 2022 from 2.92% a year earlier, substantially lower than the cost of credit for unincorporated business (5.16%) and households (4.88%). The Hellenic Development Bank has extended the deadline for applications of the third call of guarantees under the Covid-19 Enterprise Guarantee fund, with a still unutilised guarantee budget of EUR 150 million, to provide working capital loans to SMEs and will launch new financial instruments in 2022 with a strong focus on SMEs. In addition, loan disbursements linked to the RRF Loan Facility are expected to start after April and increase more substantially in the second half of the year. The Russian military aggression against Ukraine increases uncertainty for the credit demand for this year but banks believe that it should not change fundamentally their credit expansion plans.

The authorities have agreed a reform of the Hellenic Financial Stability Fund with the European institutions. The law is expected to be adopted shortly. The duration of the Fund will be extended until the end of 2025 to allow the Fund to fulfil its dual objective of contributing to the stability of the Greek banking system, while effectively disposing its assets. The reform streamlines the Fund’s governance structure, outlines a set of principles that will guide the Fund’s divestment strategy and establishes a communication channel for the Fund to the Ministry of Finance for reporting on the state of its implementation. The Fund’s special rights will also be streamlined.

The Hellenic Financial Stability Fund intends to participate, within its mandate, together with private shareholders in the second share capital increase of a less significant institution. The Fund had obtained a majority stake, in the context of the conversion of part of the bank’s deferred tax credits, and it also participated in the bank’s share capital increase, in 2021. The Fund and the major private shareholders entered into an agreement in April 2022, which envisages a second investment in the bank comprising a further share capital increase and, if required, an additional contribution in capital or alternative actions as part of the implementation of the bank’s business plan.