Agreement reached on 3-year reform programme supported by Euro area Member States and the IMF

HELLENIC REPUBLIC
MINISTRY OF FINANCE

Hellenic Stability and Growth Programme Newsletter

17 May 2010

- ***The new Economic Policy Programme will be supported with a Euro 110 billion financing package*** *provided by Euro area Member States (Euro 80 billion) and the IMF (Euro 30 billion). The programme will be monitored through twelve quarterly reviews.*

- ***The programme includes both structural and fiscal reforms*** *that will help Greece overcome deep-rooted structural deficiencies that persist in public fiscal management, the real economy and the financial sector.*

- ***The Greek government has proceeded decisively with the implementation*** *of the existing Stability and Growth Programme as well as with the actions foreseen in the new programme. All fiscal measures necessary to achieve the 2010 fiscal targets have been adopted.*

- ***Consolidation of the budget remains on track*** *with the state budget deficit over the period January – April 2010 registering a year-over-year reduction on an accrual basis close to 42%.*

The new economic policy programme

The Greek government's programme, agreed on May 3rd in coordination with Euro area Member States and the IMF, combines:

- **Fiscal consolidation**
- **Structural reform**
- **Financial sector support.**

Combined bilateral assistance from Euro area Member States (totalling Euro 80 billion) and the IMF (totalling Euro 30 billion) will support the government's programme financially.

The 3-year programme will be monitored through twelve quarterly reviews. Its progress will be measured against a set of quantitative performance criteria and structural benchmarks. The first review will take place in the third quarter of 2010.

Fiscal consolidation measures

The programme includes cumulative fiscal consolidation measures (additional to those already adopted by the Government in March) of the order of 11% of GDP through 2013. From 2013 onward the debt-to-GDP ratio is projected to follow a downward trend.

The programme revises the Government's deficit target for 2010 to 8.1% of GDP, down from its 2009 level of 13.6%. Additional fiscal measures for 2010 of euro 5.8 billion – 2.55% of GDP - were adopted by the Parliament on May 6th and include:

An additional Euro 1.25 billion increase in tax revenues, equivalent to 0.6% of GDP, with a significant carry over for 2011, through:
- An increase in VAT rates (from 21% to 23%, and from 10% to 11%);
- An increase in excise tax on fuel, cigarettes and alcohol.

An additional Euro 4.55 billion in expenditure cuts, equivalent to 1.9% of GDP, by means of:
- Nominal wage cuts of about 7% through a reduction of Easter, summer and Christmas bonuses and allowances (total nominal wage cut from all 2010 measures: about 14%);
- Nominal pension cuts of 9% through a reduction of Easter, summer and Christmas bonuses and a reduction in the highest pensions;
- An intermediate consumption cut;
- An elimination of the one-off solidarity allowance (second installment);
- A reduction in public investment.

Table of Contents

2010 milestones

May 2010
Greek government *adopts fiscal measures in parliament (increases in VAT and excise taxes, reductions in public sector wages and pensions).*
First disbursement of Euro 20 billion *(Euro 14.5 billion by Euro area member states, Euro 5.5 billion by the IMF).*

June 2010
Greek government *meets structural benchmarks.*

September 2010
Greek government *meets structural benchmarks*
Second disbursement of Euro 9 billion *(Euro 6.5 billion by Euro area Member States, Euro 2.5 billion by the IMF).*

December 2010
Greek government *meets structural benchmarks*
Third disbursement of Euro 9 billion *(Euro 6.5 billion by Euro area Member States, Euro 2.5 billion by the IMF).*

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Structural reforms

The fiscal adjustment programme is underpinned by a comprehensive structural reform programme aiming at:

- **Restoring fiscal and debt sustainability** by introducing specific and quantified revenue and expenditure measures, while simultaneously protecting vulnerable lower-income groups;
- **Enhancing the efficiency and credibility of fiscal management** by improving the quality, reliability and accessibility of fiscal data, moving to a multi-year budget process, introducing programme budgeting and improved monthly reporting, and by monitoring accountability, including to parliament (through the creation of an independent fiscal agency);
- **Introducing a comprehensive public administration reform programme**, and a fundamental reorganisation of local administration, so as to increase the efficiency and transparency of the operations of the state, as well as its interaction with the private sector;
- **Introducing improved monitoring and accountability** in key areas of the administration with significant expenditure implications, such as the introduction of a single payment authority for civil service remuneration and the strict monitoring of health expenditures;
- **Addressing chronic imbalances in the social security system** and ensuring its viability by taking into account Greece's demographic trends and its ageing population;
- **Accelerating the absorption of EU Structural funds**, which are key for investment and growth;
- **Removing existing distortions in Greek goods and labour markets** so as to ultimately attract domestic and foreign investment, strengthen competition, entrepreneurship, innovation and job growth, while fully safeguarding the rights of workers in line with EU directives; and
- **Restoring international competitiveness and facilitating** the economy's export orientation and sustained supply-side response, leading to environmentally sustainable growth and welfare.

Financial sector policies

Finally, financial sector policies aim at maintaining the stability of the financial system given the current tight liquidity conditions.

A key role is to be played by **the fully independent Financial Stability Fund (FSF)**, which is due to be established by the end of June 2010. The FSF will be supported with Euro 10 billion of initial equity provided by the financial support mechanism.

The FSF's role will be to preserve the financial sector's soundness by providing the necessary equity support to commercial banks, thus ensuring that the banking system continues financing the real economy. For banks that are not able to raise capital on their own to repay the FSF, a restructuring process led by the FSF in accordance with EU competition and state aid requirements is also foreseen. In addition, the programme will strengthen the role of the Bank of Greece in the area of banking supervision (including cross-border bank supervision) and insurance supervision.

The Memorandum of Understanding on Specific Economic Policy Conditionality and the Memorandum of Economic and Financial Policies may be downloaded at: **http://www.minfin.gr/portal/en**

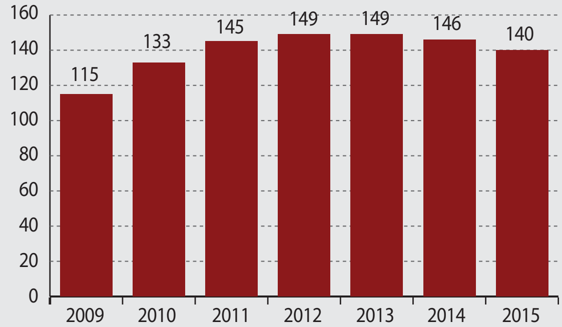
Macro and fiscal aggregates

The new economic policy programme is based on a significantly revised macroeconomic scenario and foresees a different fiscal adjustment path compared to the initial Stability and Growth Programme. Projected GDP growth rate starts with a deeper recession of -4% in 2010 and returns to positive growth in 2012. The general government deficit is projected to fall bellow the threshold of 3% of GDP in 2014, starting with 13.6% of GDP in 2009 and following a front-loaded fiscal adjustment programme that reduces the deficit by more than 5.5 percentage points in 2010.

General Government Deficit (% of GDP) and Real GDP Growth Rate (%)

General government Consolidated Gross Debt (under the Maastricht definition) is expected to increase, yet with diminishing rates, up to 2012 and continue declining onwards.

General Government Consolidated Gross Debt (% of GDP)



2010 Budget on track

*According to preliminary data, over the first four months of 2010 (January - April), **the state budget deficit on an accrual basis** amounted to 6,283 million euro, versus 10,791 million euro during the same period of 2009 and thus **declined by 41.8% against an annual targeted reduction of 35.1%.***

The deficit reduction over the first four months of 2010 is due to both expenditure reductions and revenues increases. Net revenues of the ordinary budget increased by 10.0% against an annual target of 11.7% as set in the SGP and ordinary budget expenditures during the same time period declined by 8.1% against a target set in the SGP for a reduction of 4.8%.

It should be noted that the additional measures taken on March 3rd and May 6th (tax increases and further expenditures cuts) are not yet fully reflected in the fiscal indicators; these are expected to further improve the deficit-reduction effort. Targets will be revised to reflect the measures adopted on May 6th.

*Source: **http://www.minfin.gr/portal/en***