

## 8. GREECE

### Signs of recovery linked to programme implementation

*The Greek economy has been gradually growing since the conclusion of the first review of the ESM programme. Brighter economic sentiment is supporting recovery in domestic demand, reflected also in labour market developments. Public finances are performing better than expected and the overall macro outlook remains positive, though subject to downside risks.*

#### Growth in third quarter points to the prospect of a sustained recovery

Greece's economy grew by 0.8% q-o-q (1.8% y-o-y) in 2016-Q3 in seasonally adjusted terms following 0.4% (q-o-q) in 2016-Q2. Growth was mainly driven by private consumption, investment and exports. While part of these increases is explained by base effects, short-term indicators overall point towards positive growth in 2016. Economic activity is up in industry, the retail sector and tourism, while exports have also regained strength since the shock in 2015.

Real GDP growth is projected to have reached 0.3% in 2016 reflecting the improvement in business and consumer confidence since the conclusion of the first review of the ESM programme and the good progress that has been made in clearing public sector arrears, which has led to higher liquidity in the corporate sector. Contingent upon the timely completion of the second review of the ESM programme, Greece's economic recovery is expected to gather pace in 2017 with growth of 2.7%, on the back of improving financial conditions amid a gradual relaxation of capital controls. Private consumption and investment are projected to accelerate and the contribution of net exports to become positive. Real GDP is expected to continue recovering at a robust pace in 2018, with a growth rate of 3.1%.

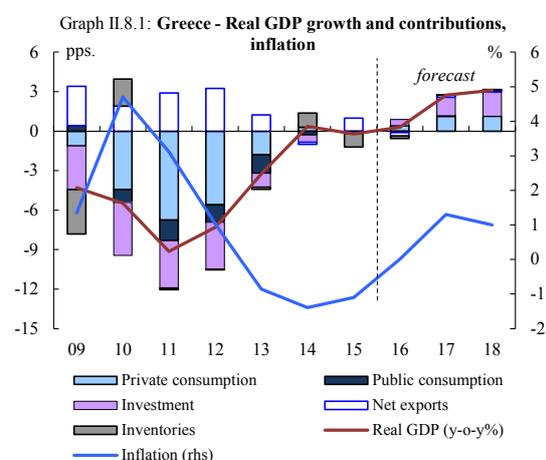
The labour market has been improving for the last two years. Employment grew by 2.4% on average in the first 10 months of 2016, and is projected to grow at a stable average rate of 2.2% until 2018. Unemployment is projected to have fallen to 23.4% in 2016, down from an annual average of 24.9% in 2015. Unemployment is set to decrease steadily over the forecast horizon, backed by the impact of labour market reforms supporting flexible forms of employment and wage setting.

The contribution of net exports to growth was likely still negative in 2016, since imports rose faster than exports amid higher domestic demand. Going ahead, net exports are expected to turn

positive, as improved competitiveness and higher investment in the tradable sector spur exports.

The decrease in the price level halted in 2016 on the back of higher indirect taxation and rising oil prices. These factors are also expected to underpin a moderate rebound of inflation in 2017 and 2018, along with strengthening domestic demand. Over the forecast horizon, wages are expected to increase along with recovering labour productivity.

Downward risks mainly relate to uncertainties over the completion of the second review of the ESM programme and external factors such as international and regional geopolitical and economic tensions, as well as the refugee crisis.



#### Strong revenue performance and ambitious reforms to improve fiscal outcomes

Greece is forecast to reach a general government balance of -1.1% of GDP in 2016. Having over-achieved its primary targets of the ESM programme for 2015, Greece is set to significantly – by about 1½% of GDP – over-perform the primary surplus target of 0.5% of GDP for 2016 according to the ESM programme definition.<sup>(49)</sup> The composition of the fiscal adjustment is tilted to the revenue side amidst restrained expenditure

<sup>(49)</sup> The programme definition of the primary balance excludes the one-off cost of bank recapitalisation, SMP and ANFA revenues and part of the privatisation proceeds.

growth. It follows the adoption of a major fiscal package in the context of the first review projected to yield 3% of GDP through 2018, bringing total fiscal consolidation since the ESM programme was launched to 4.2% of GDP. The stronger-than-forecast revenue primarily stems from dynamic growth in underlying tax bases, particularly for indirect taxes and the corporate income tax, but also several one-off factors related to clearing tax liabilities from previous years and stock-piling effects in view of the 2017 hike in the tobacco tax.

Taking into account the adopted measures (in particular personal income tax and pension reforms) and the 2017 Budget, Greece is projected to achieve the ESM programme primary balance target of 1.75% of GDP in 2017, even after allowing for the national roll-out of the Guaranteed Minimum Income scheme. The strong revenue performance observed thus far especially in 2016, supported by the ongoing revenue administration reforms, implies considerable upside risks to the forecast which augurs well for the achievement of the target also in 2018. Downside risks include the possibility that the 2017 fiscal reforms could yield less than expected due to implementation risks and the effects of uncertainties over the completion of the second review of the ESM programme.

The authorities are expected to adopt the Medium-term Fiscal Strategy for 2018-2021, including any adjustments in fiscal policies needed, to ensure the achievement of the 2018 programme primary balance target of 3.5% of GDP.

Overall, the general government balance is projected to reach -1.1% of GDP in 2017 before improving to 0.7% of GDP in 2018. In structural terms, given the still-large output gap, the general government balance is forecast to reach 2½% of GDP in 2017 and 2½% of GDP in 2018.

On the back of the fiscal outturn projected for 2016 and the stock-flow adjustment related to the clearance of arrears, Greece's debt-to-GDP ratio is expected to increase from 177.4% in 2015 to 179.7% in 2016. The improved fiscal position and stronger GDP growth are expected to put the debt-to-GDP ratio on a declining path starting in 2017. Interest expenditure is projected to decrease over the forecast years because old loans are replaced with new financial assistance loans with lower interest rates. The implementation of short-term debt measures in 2017 and 2018 will increase interest expenditure in the short run but will lower it in the long term and smoothen the debt repayment schedule.

Table II.8.1:

**Main features of country forecast - GREECE**

	2015			97-12	Annual percentage change					
	bn EUR	Curr. prices	% GDP		2013	2014	2015	2016	2017	2018
GDP	175.7		100.0	1.0	-3.2	0.4	-0.2	0.3	2.7	3.1
Private Consumption	122.8		69.9	1.1	-2.6	0.4	-0.2	0.6	1.6	1.6
Public Consumption	35.3		20.1	1.2	-6.4	-1.4	0.0	-0.6	0.2	0.0
Gross fixed capital formation	20.3		11.5	-1.1	-8.4	-4.6	-0.2	4.0	12.0	14.2
of which: equipment	8.3		4.7	0.6	-4.5	21.0	-1.5	1.8	13.4	15.2
Exports (goods and services)	56.1		31.9	5.3	1.5	7.8	3.4	0.7	3.9	4.7
Imports (goods and services)	55.8		31.8	3.1	-2.4	7.6	0.3	1.5	3.2	4.2
GNI (GDP deflator)	176.3		100.3	0.9	-4.0	0.7	-0.1	0.1	2.7	3.0
Contribution to GDP growth:		Domestic demand		1.1	-4.3	-0.6	-0.2	0.7	2.6	2.9
		Inventories		-0.1	-0.1	1.1	-1.0	-0.2	0.0	0.1
		Net exports		0.1	1.2	-0.2	1.0	-0.3	0.2	0.1
Employment				0.0	-2.6	0.0	0.5	2.2	2.1	2.2
Unemployment rate (a)				11.6	27.5	26.5	24.9	23.4	22.0	20.3
Compensation of employees / head				4.5	-7.5	-2.1	-2.9	0.2	1.0	2.0
Unit labour costs whole economy				3.5	-6.9	-2.4	-2.2	2.1	0.4	1.1
Real unit labour cost				0.5	-4.6	-0.6	-1.2	2.0	-0.9	0.0
Saving rate of households (b)				-	-	-	-	-	-	-
GDP deflator				2.9	-2.4	-1.8	-1.0	0.0	1.3	1.2
Harmonised index of consumer prices				3.3	-0.9	-1.4	-1.1	0.0	1.3	1.0
Terms of trade goods				-0.3	1.7	0.9	0.6	-4.4	0.0	-0.1
Trade balance (goods) (c)				-14.7	-9.8	-10.8	-9.1	-9.0	-9.5	-9.5
Current-account balance (c)				-9.7	-2.2	-2.6	0.0	-0.7	-0.7	-0.6
Net lending (+) or borrowing (-) vis-a-vis ROW (c)				-8.1	0.2	-0.6	2.1	1.3	1.1	1.2
General government balance (c)				-7.8	-13.2	-3.6	-7.5	-1.1	-1.1	0.7
Cyclically-adjusted budget balance (d)				-7.9	-6.2	2.3	-2.2	3.7	2.3	2.6
Structural budget balance (d)				-	2.3	2.3	1.8	3.7	2.3	2.6
General government gross debt (c)				115.3	177.4	179.7	177.4	179.7	177.2	170.6

(a) as % of total labour force. (b) gross saving divided by adjusted gross disposable income. (c) as a % of GDP. (d) as a % of potential GDP.