EUROPEAN CENTRAL BANK

EUROSYSTEM

5 August 2010

PRESS RELEASE

STATEMENT BY THE EC, ECB AND IMF ON THE FIRST REVIEW MISSION TO GREECE

Staff teams from the European Commission (EC), the European Central Bank (ECB), and the International Monetary Fund (IMF) visited Athens from 26 July - 5 August 2010 for the first quarterly review of the Greek government's economic programme, which is being supported by a EUR 80 billion loan from euro area countries and a EUR 30 billion Stand-By Arrangement with the Fund. The strategy and key policies remain as described in the May 2010 Letter of Intent and Memorandum of Economic and Financial Policies: http://www.imf.org/external/pubs/ft/scr/2010/cr10111.pdf.

Our overall assessment is that the programme has made a strong start. The end-June quantitative performance criteria have all been met, led by a vigorous implementation of the fiscal programme, and important reforms are ahead of schedule. However, important challenges and risks remain.

The contraction in the economy is in line with May programme projections: GDP is expected to decline by 4 percent in 2010 and some 2½ percent in 2011. Inflation is higher than expected - we have revised our estimate for 2010 to 4¾ percent - pushed up by indirect tax increases. With no signs of second-round effects, inflation is expected to decline rapidly.

In the fiscal area, the authorities have kept spending significantly below budget limits at the state level. This has offset slippages caused by problems in controlling expenditures at the sub-national level (local governments, hospitals, social security funds), and the overall deficit target for end-June was met. Going forward, to address potential risks to fiscal targets, it is critical to tighten expenditure control and monitoring, in particular at sub-national levels. Another key challenge is to further strengthen tax administration, including to reduce tax evasion by high-income and wealthy individuals. This is essential to secure tax revenues and to promote the overall fairness of the adjustment programme.

In the financial sector, there has been a moderate deterioration in capital adequacy as non-performing loans have increased in line with expectations. Recently, the Committee of European Banking Supervisors stress tests covered more than 90 percent of Greek banking system assets and all but one state-owned bank passed, thus helping to reduce market volatility. We welcome that the government has commissioned a strategic review for the banking sector and a due diligence for state banks. The Financial Stability Fund (FSF), which is soon to become operational, will provide an important backstop to deal with potential capital shortfalls. In our view, the 10 billion euro earmarked for the FSF under the programme remains adequate. Continued close monitoring of the financial sector will be important in the period ahead.

Impressive progress is being made on structural reforms. The mission welcomes Parliament's approval of the landmark pension reform, which is far-reaching by international standards. Substantive labour market reform is also well underway. Implementation of recent tax reform and budget reform is key in order to consolidate fiscal consolidation. Other reforms that are scheduled for early implementation are transportation, where important progress has already been made with liberalisation of road haulage, and energy. Restoring competitiveness and boosting potential growth remains critical to the programme's success. The challenge facing the government in this regard will be to overcome resistance from entrenched vested interests to opening-up of closed professions, deregulation, implementation of the services directive, and elimination of barriers to development of tourism and retail.

The Greek government is still unable to access international capital markets except for placement of short-term T-bills. However, market sentiments appear now to be improving. Taking advantage of the breathing space afforded by the large-scale international financial support, the key challenge facing the Greek authorities remains to establish a strong track record of policy implementation in order to regain access to international capital markets.

Next steps: The staff-level agreement reached with the Greek authorities will pave the way for the conclusion of the first review under the loan facility agreement (euro area) and Stand-By Arrangement (IMF), subject to approval by the Commission, the Eurogroup, and the IMF's management and Executive Board. Such approval will allow the disbursement of EUR 9 billion (EUR 6.5 billion by the euro area Member States, and EUR 2.5 billion by the IMF).

The mission for the next programme review is scheduled for October 2010.