11 October 2011

Statement by the European Commission, the ECB and IMF on the Fifth Review Mission to Greece

Staff teams from the European Commission (EC), European Central Bank (ECB), and International Monetary Fund (IMF) have concluded their fifth review mission to Greece to discuss recent economic developments. The mission has reached staff-level agreement with the authorities on the economic and financial policies needed to bring the government's economic program back on track.

Regarding the **outlook**, the recession will be deeper than was anticipated in June and a recovery is now expected only from 2013 onwards. There is no evidence yet of improvement in investor sentiment and the related increase in investments, in part because the reform momentum has not gained the critical mass necessary to begin transforming the investment climate. However, exports are rebounding—albeit from a low base—and a shift towards a more dynamic export sector, supported by a moderation of unit labor costs, should lead to more balanced and sustainable growth over the medium term. Inflation has come down over the last year and is expected to remain below the euro area average in the period ahead.

In the **fiscal area**, the government has achieved a major reduction in the deficit since the start of the program despite a deep recession. However, the achievement of the fiscal target for 2011 is no longer within reach, partly because of a further drop in GDP, but also because of slippages in the implementation of some of the agreed measures.

As for 2012, the mission believes that the additional measures announced by the government, in combination with a determined implementation of the adjusted Medium-Term Fiscal Strategy, should be sufficient to bring the fiscal program back on track and ensure that the deficit target of EUR 14.9 billion will be met.

Looking to 2013-14, additional measures are likely to be needed to meet program targets. Such measures should be adopted in the context of an update of the Medium-Term Fiscal Strategy by mid-2012. To ensure that the program is growth-friendly, and in view of the ambitious assumptions regarding improvement in revenue administration already embedded in the Medium-Term Fiscal Strategy, it is essential that such measures focus on the expenditure side.

In the area of **privatisation,** progress has been achieved with the creation of a professionally managed privatisation fund. However, delays in the preparation of the assets for privatisation, and to some extent worse market conditions, mean that revenues in 2011 will be significantly lower than expected. The government remains, however, committed to the revenue target of EUR 35 billion by the end of 2014. Ensuring that the privatisation fund remains independent from political pressures remains key for success in this area.

Banks have improved their capital base through market-based means. As evident from this weekend's resolution of Proton Bank, the recent amendment of the banking law ensures that non-viable banks can be wound down while protecting depositors' interest and preserving the stability of the financial system.

As to **structural reforms,** areas of progress include the transport sector, licensing procedures, and regulated professions. As overall progress has been uneven, a reinvigoration of reforms remains the overarching challenge facing the authorities. In this regard, the decision to suspend the mandatory extension of sector-level collective agreements to the firm level is a major step forward, as it will help ensure the flexibility in the labour market needed to boost growth and prevent high unemployment from getting entrenched.

Overall, the authorities continue to make important progress, notably with regard to fiscal consolidation. To ensure a further reduction in the deficit in a socially acceptable manner and to set the stage for a recovery to take hold, it is essential that the authorities put more emphasis on structural reforms in the public sector and the economy more broadly.

The success of the program continues to depend on mobilizing adequate financing from private sector involvement (PSI) and the official sector. Ongoing discussions on PSI together with assurances provided by European leaders at their July 21 summit suggest that the program remains fully financed.

Once the Eurogroup and the IMF's Executive Board have approved the conclusions of the fifth review, the next tranche of EUR 8 billion (EUR 5.8 billion by the euro area Member States, and EUR 2.2 billion by the IMF) will become available, most likely, in early November.