HELLENIC PARLIAMENT

PARLIAMENTARY BUDGET OFFICE

QUARTERLY REPORT

OCTOBER – DECEMBER 2016

March 2017

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THE TARGETS AND THE SCIENTIFIC COMMITTEE OF THE OFFICE

The Parliamentary Budget Office (PBO) was established in accordance with article 30A of Parliament Rules (Part B', Article 21, Government Gazette 122/A'/30.06.2016) and with law 3871 (Government Gazette 141/A/17.8.2010). It is an independent fiscal institution within the Parliament and operates in accordance with the Special Regulations for the Internal Functioning and Organization, (Article 53, Government Gazette 122/A'/30.6.2016).

The Office is responsible for the monitoring of the State Budget implementation, the assistance to the workings of the two Committees of the Parliament (the Special Committee on the Financial Statement and the General Balance Sheet of the State and on the Control of the Implementation of the State Budget and the Standing Committee on Economic Affairs) and the drawing up and submission to the above committees of quarterly and annual reports in respect of the fiscal targets, as set in the Mid-Term Programs of Fiscal Strategy.

The Parliamentary Budget Office analyzes the main issues of the Greek economy based on the modern academic literature.

Mr. Panagiotis Liargovas (Professor of the University of the Peloponnese) is the Coordinator of the Parliamentary Budget Office and heads the Scientific Committee composed of the following members:

- Panos Kazakos, Emeritus Professor, University of Athens
- Spyros Lapatsioras, Assistant Professor, University of Crete
- Napoleon Maravegias, Professor, University of Athens
- Michael Riginos, Associate Professor, University of Athens

PREFACE

The current report monitors the evolution of the Greek fiscal aggregates in relation to the targets set in the State Budget and in the Mid-term Fiscal Strategy Frameworks. It focuses on the third quarter of 2016. The report was drawn according to the present policy framework, as it is formed by the Memorandum that the Greek Government has signed with the European Central Bank (ECB), the European Commission (EU) and the International Monetary Fund (IMF). Moreover, the report takes into account the current debate on the revision of economic governance, of the EU and the Euro zone in particular.

The Coordinator and the Members of the Scientific Committee of the Office recognize that there are many different approaches within economic policy and that something that is necessary on economic terms is not necessarily politically feasible. Furthermore, something that is politically desirable is not always efficient in economic terms.

Our effort is to present the problems and propose solutions to crucial issues, not only in the main body, but also usually in a special chapter at the end of each report.

The Coordinator of the Office

Professor Panagiotis Liargovas

EXECUTIVE SUMMARY

1. THE BROADER PICTURE

The year 2016 has not been easy for economic and fiscal policy. Likewise, neither 2017 is expected to be easy, as it has started with new delays in implementing the third MoU (=adjustment programme), also stalling review completion. The government has spoken of an "honorable compromise", mainly with EU partners, the term underpinning huge disparities of opinion not only between the government and the institutions, but also between institutions themselves (IMF, Eurogroup).

In October 2016, the Prime Minister had announced an upcoming swift completion of the second review within three weeks, thus sending an optimistic message both to businessmen and employees. It is our view that swift completion goal of Third MoU (adjustment program) Second Review was clear and rightly aimed, yet not achieved. Relations with partners have been aggravated, resulting to technical staff-representatives' of the institutions- departure from Greece, thus prolonging time for second review completion, obviously with the blame for this not lying only on the Greek government, as a prevailing factor was the IMF-EU dispute over the debt and primary surpluses.

<u>The virtuous circle as a promise</u>

There is still time for second review completion (which, nevertheless, should have taken place in the first weeks of December). If it is achieved in due time (the latest by the end of February), it will provide Greece with the opportunity to be included -as of Q1 2017 - (most possibly in March), to the ECB "quantitative easing" program, which will, in turn, allow for cheaper and more relaxed economy financing. Banks will be able to leverage liquidity from the ECB, while the government shall gradually withdraw capital controls. It would then be realistic for the government to pursue, or even try to access/enter markets. The country could avoid implementation of the "automatic mechanism for fiscal adjustment", that is, the primary expenditure cutting obligation (mainly State salaries and pensions). Moreover, review completion shall increase confidence in economic policy, also broadening economy's perspectives. Under conditions of gradual normalization of the economy together with increased trust, the issue of the non-performing loans would stand the chance of being resolved. Furthermore, some "cushions" shall be acquired from the ESM in case of need. As a final point, the three-stage debt relief plan, already agreed upon/approved within the Eurogroup, shall proceed. The ESM has already approved short-term relief measures implementation[1].

Review completion would also mean a closure of a whole series of sensitive issues, leading us to a rational expectation for returning in the next two years to steady (=sustainable) positive growth rates, which will facilitate fiscal consolidation. Unemployment shall decrease. To put it simply, ***MoU full implementation to the end gives the country the chance to overcome today's dead-ends.*** This does not mean that there is no need for negotiations, e.g. over realistic fiscal objectives. It does mean, though, that reforms are the key.

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1 See ESM Press Release, 23/01/2017, https://www.esm.europa.eu/press-releases/esm-and-efsf-approve-short-term-debt-relief-measures-greece.

Then, where is the problem?

The political-economic difficulties of adjustment

The third MoU(like the preceding ones) is a broad and basically liberal program for Greek economy modernization/reform, but also of the social state and policy, which is fully opposed to legacy structures, traditional clientelistic attitudes and incompatible views of the world and the country. Each chapter starts precisely with generic statements, advising and documenting its recommendations. In theoretical terms, it targets in a holistic way (Greek) state and closed markets failures.

However, several segments of the political world, as well as social groups defending their traditionally set interests, have not been convinced over the program's relevance and correctness, therefore not embracing it. According to the majority of surveys, over 80% of citizens have the view that the MoU points towards the wrong direction.

Delays, combined with negative trends being formed within the IMF over its participation and involvement in the Greek program, threaten to minimize the "ambient and surrounding" as well as the actual economic benefit we would expect from a final agreement. Obviously, the political leadership-to its degree of authority- finds it hard to convince various political and social pillars over the need for taking the necessary measures and legislative initiatives to be adopted upon completion of the program implementation agreement.

In other words: ***for Greece, the economic cost of delays and postponements in review processes, that is, a final agreement over the adjustment program, may prove greater than a potential benefit, which, moreover shall prove to be temporary.*** The most visible, although simple, indicator of economic cost, shall be the difference between "expected" growth rates for 2017 and 2018 and those that will actually be achieved. On December 17, 2016, the OECD forecasted a growth rate of 1.3% for Greece in 2017[2]. Hence, if ultimately the Greek government's and European Commission's optimistic forecast for growth rate of 2.7% are not fulfilled (due to multiple uncertainties), and a growth rate of 1% to 1.5% is yielded in 2017 (as forecasted by OECD:1.3% and the Intelligent deep Analysis of the University of Athens: 1.01%[3]), this would mean in absolute figures an initial loss of €2.2 to €3.1 bn for the Greek economy, just for the current year compared to target (2010 constant prices). The worst is that slowdown shall drag along other fundamentals, for example taxes. ***Therefore, a threat for new vicious circles and long-term stagnation is visible in the horizon.***

The danger of political turmoil and the rise of populism

Turbulences in the Eurozone and the EU are noteworthy as well (Brexit, Italian referendum and the 5-star rise to power, D. Trump election in the US, instability in the Balkans, tensions in Turkey etc.). Nevertheless, broader political turmoil does not seem to have significantly affected so far European economies' rise, therefore not affecting our economy as well. There is a clear political danger, stemming from austerity policies adopted in Europe, manifested as radical populism in the form of national voices with intense racist features, gaining ground

2 OECD Economic Outlook, Volume 2016, Issue 2, page 163.

3 According to November 2016 forecast, see. http://www.indeepanalysis.gr/oikonomia/provlepseis-2016-2021-noemvrios-h-ellhnikh-oikonomia-mexri-to-2021. (in Greek)

everywhere-in the Netherlands, Austria, France, Italy and elsewhere- and represents a version of "less Europe".

Populist movements denounce Europe and, mainly, their countries' political and economic elites, also proclaiming simplistic solutions for complex issues, cultivating illusions and extolling national sovereignty (better alone than with others as a team). Often, they turn against immigrants as a whole, without being interested in problem solving, while also contesting fundamental values of liberal democracies. Populism has no real interest in finding solutions to specific problems (already mentioned) in a way consistent with Age of Enlightenment traditions, but on the contrary cultivates illusionary alternatives such as raising walls for resolving the migration issue.

Confirmation of this trend in the frame of upcoming consecutive elections in the Netherlands, Germany, France and Italy within 2017, combined with developments outside the EU may act as a catalyst on the fragmented political and social system of Greece, thus encouraging forces willing to represent these trends at the political field here as well. ***In this case, adjustment shall become a Sisyphean task.***

The next, third stage of reviews

Completion of the second review does not signal the end of the third MoU implementation path or the smooth disbursement of envisaged loan agreement tranches for the following reasons:

- First, time will be needed for the full implementation of legislative measures already adopted to complete second review, as well as potential unfinished business to be transferred to the next stage
- Second, the third progress review comes right after the second; if the MoU is literally interpreted and following delays of preceding reviews, this shall have to be completed in too tight a timeline

This will possibly mean that ***political time for third review completion shall clearly be more restricted compared to preceding reviews' political timing.***

Additionally, further to potential unfinished business -among other things in the fields of energy, OECD Toolbox and privatizations- the next review includes only seemingly simple issues such as new privatizations, further regulation of social security-pension reforms, new tax policy reform and code drafting for the purpose of current legislation scheme simplification et.al (see Table I)

It is highly possible that difficulties in fulfilling Greek commitments shall be greater as we will be entering the 8th year of economic suffering and hardship.

Table I. The next review

Q1 2017			
I. Delivering sustainable public finances			
51	**Tax policy reform**. Simplify the income tax regime; revise the corporate tax law in ITC; develop collective investment vehicles; revise the tax legislation in conflict with TCP; revise TCP on cooperation on audits; review tax certificates extension; reform KEDE; modernise legislation addressing collection of tax on income generated from offshore portfolio.	2.2	January 2017
52	**Revenue administration**. Make the autonomous revenue administration fully operational.	2.3.1	January 2017
53	**Social security**. Full nationwide rollout of the GMI scheme	2.5.3	January 2017
II. Structural policies to enhance competitiveness and growth			
54	**Labour market**. Streamline the labour legislation through the codification into a Labour Law Code.	4.1	March 2017
Q2 2017			
I. Delivering sustainable public finances			
55	**Tax policy reform**. Align the property tax assessment values with market prices.	2.2	June 2017
Q3 2017			
I. Delivering sustainable public finances			
56	**Anti-smuggling**. Ensure the scanners in the three main international ports are fully operational.	2.3.2	September 2017
Source: *EC Compliance Report, June 2016.*			

We hope that even if the third review is delayed, this will not affect tranches' disbursement, in order to cover the country's gross funding needs which in 2017 Q1-Q4 shall mount to €16.2 bn -if all goes well. Only in 2018 shall financing needs become less (about €5.2 bn), therefore to ***less dependence from transnational loans.***

It is noteworthy that financing requirements may prove greater in case of failing to deliver various program's deliverables and objectives, such as revenue from privatizations for 2017 (€2.044 bn) and reduction of private debt to the public sector.

"Fourth MoU"?

Even after 2018, Greece will be needing loans to cover financing needs of the next period, or else it will be forced to stop servicing its obligations. Such loans may be drawn either from the markets, -on condition of a successful return to them-or the ESM. This is also an issue complicating review completion, due to the different approaches on part of the IMF, the EU and the Greek government.

Obviously a new request for loan from the ESM in 2018 shall be accompanied-in line with ESM rules- by a new economic adjustment program, the Fourth Memorandum[4]. Furthermore, adoption difficulties of a new program by our partners under significant political pressures, make the loan accompanying terms even more worrying.

4 This might happen earlier if the IMF pulls out from the Greek program.

If negotiations with the ESM (which is an intergovernmental institution and not a European Commission's instrument) fail to deliver an agreement, or if the country fails to return to the markets, then default/insolvency shall be inevitable, possibly resulting in expulsion/exit from the Euro. Resulting effects are easy to predict: new production shortfall, crisis in the banking sector, discontinuity of capital inflows from EU Structural Funds, uncertainty and, in case of exiting the single currency, devaluation of the national currency, sharp tendencies towards spirals of inflation and devaluations calling for a very restrictive monetary policy, and, what is more, external, public and private debt hanging over like the Sword of Damocles. Yet, pure economic analysis underlines the most important effect that ***default and exit from the Eurozone shall extinguish Greek policy "self-restriction" within and in milieu of the European system, with its rules (and opportunities)[5]. Any government then shall be drifting in the sea of claiming fragmented interests and mutual accusations, in a fragmentary political and social landscape looking for a new identity within the international environment from the worst standpoint, both inside and outside the country.***

2. DO ECONOMIC TRENDS HERALD RECOVERY?

Nevertheless, 2016 has demonstrated the Greek economy's resilience and stabilization capacity, against all odds, such as capital controls and economic policy instability. The new tension with the institutions that occurred in December is possible to generate additional negative effects, if it is not overcome soon.

Real GDP growth rate for 2016 is expected to form marginally around zero[6], following its sharp drop in the previous years, cumulatively mounting to about 25%. Q3 has presented an increase again. However, looking at performances for a longer period, for example since Q2 2014, stagnation trends are observed (see Graph I). The (already) low production of the manufacturing sector has further dropped by 6.9% in the twelve-month period November 2015-October 2016[7], while exports of goods and services decreased by 6.9% during the first six months, yet substantially increased in Q3; although very anemic, fixed capital investment increased by 3% in the first six months and by 12.6% in Q3[8].

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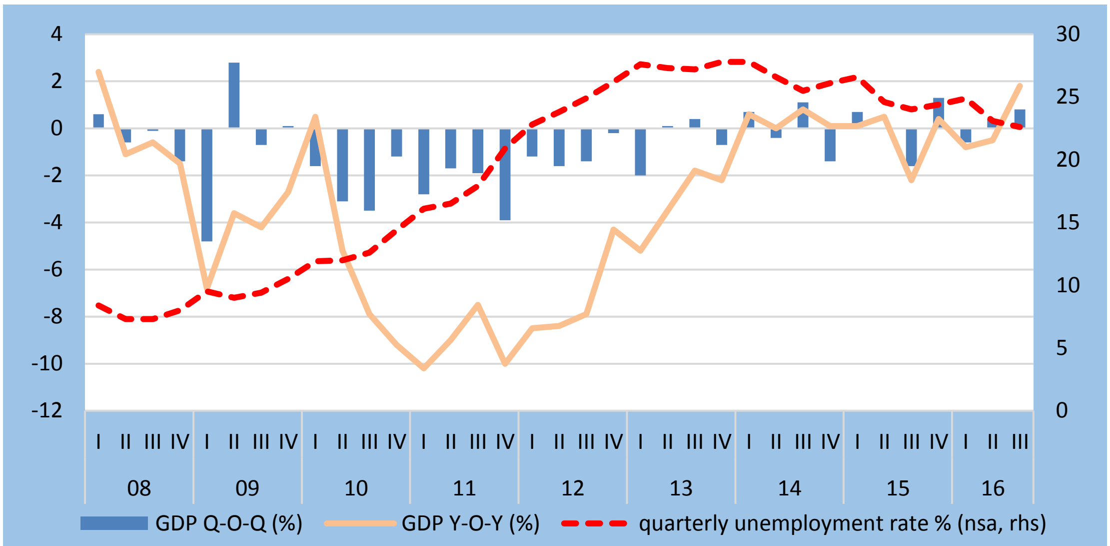
5 Kevin Featherstone of LSE proposed the term "external commitment" (vincolo esterno).

6 State Budget Report 2016: -0.7%, State Budget Report 2017: -0.3%, Bank of Greece, Interim Report 2016, December 2016 page 4: +0.1%, European Commission Winter Forecast: +0.3%.

7 ELSTAT, Turnover index in industry: October 2016, 20.12.2016.

8 ELSTAT, Quarterly National Accounts: 3rd Quarter 2016 (Provisional data), November 29, 2016

Graph I. Quarterly GDP and unemployment rate, q1 2018 – q3 2016.



Source: *ELSTAT*

A positive development is that unemployment has been reduced, although continuing to present relatively high levels. Q3 2016 sees ***a drop in unemployment rates to 22.6%[9],*** slightly lower than the 23.1% of Q2 and the 24% of Q3 2015. Moreover, employment has increased by 1.8% on an annual basis. Because of that increase and the average salary stabilization, compensation per employee has increased by 0.9% in Q3 2016, following a drop by 2.9% in 2015[10].

It must be noted, however, that ***the drop in unemployment rates on an annual basis is accompanied by a substantial spread in the so called "flexible" forms of employment[11].*** The European Commission in its Winter 2017 economic forecast estimates that unemployment rate stood at 23.4% in 2016, while in 2017 it is projected to drop to 22%.

The drop in unemployment in 2016 must not cover up the huge problem faced by the country in the long run: according to the bleak predictions of IMF Head of European department, it will take 21 years until unemployment in Greece returns to pre-crisis levels[12] (12 years for Italy, 10 for Portugal and 6 for Spain). Even if we accept the fact that IMF prediction have proved inaccurate often in the past, it will take a lot more on part of the current administration to achieve sooner a significant reduction- below 10%- in unemployment[13].

Furthermore, a primary surplus has been achieved, expected to reach 2% of GDP[14], thus exceeding the Program's target (0.50% GDP). The final data will be confirmed by Eurostat in April 2017.

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9 ELSTAT, Press Release, Labour force survey: Third Quarter 2016, 12/15/2016 (non-seasonally adjusted).

10 ELSTAT, Greek Economy, 5/01/2017, annual changes, non-seasonally adjusted data (for quarterly data).

11 ERGANI, employment flows in the private sector: NOVEMBER 2016.

12 http://greece.greekreporter.com/2017/01/19/it-will-take-21-years-until-unemployment-in-greece-returns-to-normal-imf-official-says/

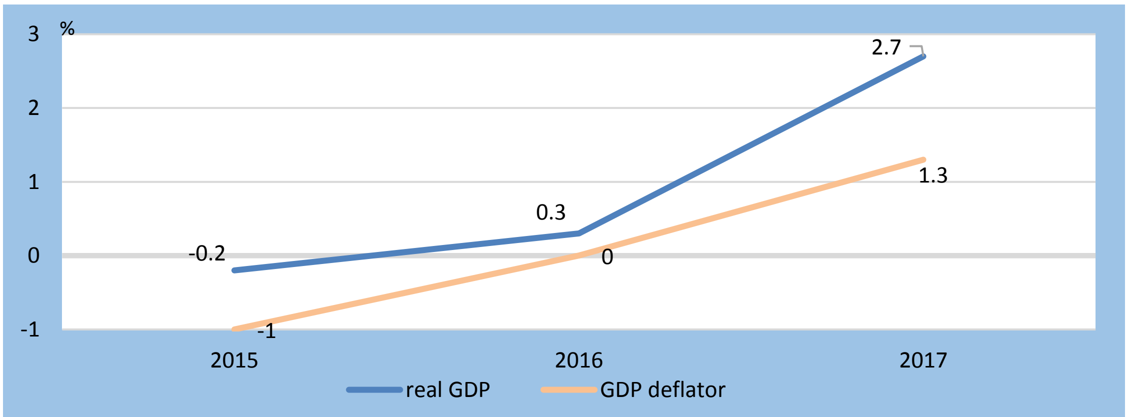
13 Similar results have come out in PBO's previous report, taking into consideration that in the previous twenty years before the crisis, Greek economy created on average 45.000 jobs a year. If this experience repeats itself in the future (which is very difficult), tackling unemployment will take many years and the current cyclical unemployment can turn into long-term unemployment with dramatic consequences for social cohesion. See PBO, Quarterly Report April-June 2013, page 12.

14 According to the European Commission, Winter Economic Forecast 2017.

From within the crisis, a new extrovert economic model is emerging, founded on exports of goods and services (internationally tradable). And this is the most important structural change in Greek economy. As mentioned by the Bank of Greece[15] "in the period 2010-2014, tradable activities have contributed to economic adjustment through the reduction in unit labor cost, thus resulting to restore to a large degree the Greek economy loss of competitiveness of the 2000-2009 period, in which unit labor cost had risen by approximately 45%. On the contrary non-tradable activities undermined that process, despite the fact that, similarly to the other countries of the Eurozone periphery, it has been the basic source for reducing cost competitiveness in the pre-crisis period". As mentioned in the same report, "the tradables' relatively better performance has led to an increase of their contribution in the total of the country's production in the period 2010-2014, strengthening the Greek economy's extrovert character. Tradable activities' share in the total gross added value has increased from 48.8% in 2009 to 53.1% in 2014, converging significantly towards the Eurozone of 18 average (55.8% in 2014). More specifically, compared to 2009, the gross added value of tradable goods and services has increased in 2014 in relation to non-tradable by 10.1% in terms of production volume and by 19% in nominal terms. Consequently, employment in the tradables' sector has increased by 8% compared to non-tradables. Nevertheless, internal devaluation has not yet been completed, because the drop in production costs due to salaries' reduction has not passed on to prices to the degree it should have.

In the second half of 2016, the Greek economy has demonstrated that through correct political signaling, it is capable of rapid recovery. A part of the Greek private businesses is able to withstand crisis, mainly because they have turned towards exports, in spite of difficulties in financing and capital controls.

Graph II. GDP and Prices: evolution and projections.



Source: *European Commission. European Economic Forecast. Winter 2017*

However, the banking sector presents significant weaknesses as liquidation of non-performing loans remains a problematic area, and Bank Administrations have been headless until the end of 2016 due to the already known disputes between the Financial Stability Fund (of the government) the Single Supervisory Mechanism and the banks. There is imminent danger for their insufficient capital adequacy, thus not being capable of smoothly financing production economy.

15 Bank of Greece, Governor's Annual Report 2015, February 2016, page 93-98.

The 2017 State Budget envisages acceleration of growth in 2017 (and 2018), yet, ***looking at the situation as a whole, we deem that outlook as uncertain and depending on various circumstantial and external factors, which make it more of an optimistic message than a documented assessment.*** Graph II illustrates ***the difference between documented trends of the past and wishful hopes for the future[16].***

<u>Budgetary - fiscal issues</u>

According to official data on state budget execution on a cash basis, in 2016 a larger primary surplus is achieved than the one originally projected. However, though not a Greek government obligation, still it is much less than the one required for public debt interest payments. The country, therefore, still depends on interstate lending (ESM loans) to cover the difference. Besides, the primary surplus[17] marked ***contains elements partially disproving the good image*** (state arrears, pending pension scheme, and court decision implementation).

The PBO deems a fiscal policy tending to achieve primary surpluses as correct in terms of its general approach, as potentially limiting borrowing requirements, yet it also presents problems due to the program's high ultimate target (3.5% GDP as of 2018). Moreover, the government's choice of policy mix (favoring tax increases instead of spending cuts) is open to criticism.

The fiscal dimension (as opposed to the reform dimension) of the program (as updated in June) is a source of threats regarding growth. The target of long-lasting primary surpluses after 2018 mounting to 3.5% GDP is counter-productive[18] although it is possible that the government will be forced to accept it[19].

New taxes for 2017 are expected to stall recovery. Yet, ***public dialogue over taxation is often characterized by exaggeration, while neglecting the issue of expenditure and taxes' distribution.***

The fact that tax burden deducts income from the income circuit, thus resulting to a ***potential*** recessive effect, is an economic analysis elementary conclusion. Moreover, tax competition conditions prevailing in our neighborhood may avert investments. But, generally speaking, ***the suggestion for less taxes per se is not a viable alternative. It may, though, be part of a larger reform measures' package, if weighted as part of the overall economic policy.***

Tax rates are just one of the many factors taken into consideration when it comes to investment decision-making[20]. Therefore "counter-balancing actions", mainly on part of the government, e.g. infrastructure expenditure rationalization, may limit significantly taxation's recessive effect, of course in combination to a growth and business friendly environment, such as

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16 PBO, Report on the Draft Budget 2017, November 2016. (in Greek)

17 On a cash basis.

18 The same is supported by the Governor of BoG Ioannis Stournaras in the Monetary Policy interim Report, November 2016. In particular the Governor considers that it is necessary to revise the budgetary target of 2% GDP from 2018 onwards. See similar estimates in PBO's previous quarterly reports.

19 See letter of Minister of Finance Euclid Tsakalotos to Institutions, naftemporiki.gr, 21.12.2016.

20 See among others World Economic Forum, Global Competitiveness Report, 2015-2016 and 2016-2017. From a business perspective, the following investment barriers are reported: access to funding, state's bureaucracy, unstable financial policy, tax legislation complexity and political instability etc. Note that the importance of tax rates increases in a period of deep recession.

one with a stable tax system, a long-term-oriented economic policy and a whole series of reforms in public administration (targeting bureaucracy), banks, spatial planning and the field of justice where time consuming processes burden –mostly small and medium sized-businesses, legal certainty, labor markets etc. In the long run, education may play a crucial role, as a well-trained labor force may act as a motivational factor for investment in new fields. In such a frame, reducing tax rates could be meaningful.

Besides tax rates, unfinished business is present in the field of taxation. ***On-going and continuous changes in taxation have to stop*** as causing uncertainties and not allowing for long-term planning to individuals, free-lance professionals and businessmen, thus discouraging serious investors and also encouraging tax evasion, which the government tries to limit using other measures (e.g. electronic transactions).

Legislation is complex. Tax evasion remains policy programmatic objective. We will evaluate the various measures already taken by the government judging from the final outcome. At this stage, we note that ***tax outperformance is an indication of progress in combating tax evasion.*** It remains to be seen if this will continue in 2017 as hoped by the government.

The PBO sticks to its view[21] that upwards trends in taxation must be reversed. They, furthermore, cause new problems in fiscal management, increasing private arrears to the public sector. More specifically in November 2016, they mounted –cumulatively- to €12.63 bn from €11.74 bn in October and €10.34 bn in September. ***Within eleven months-January 2016 to November 2016- there has been an increase of €1.15 bn per month.***

In summary, ***the level of tax burden is high, not in itself, but in combination to other structural failures-***unpredictable changes in economic policy, legal uncertainty, poor infrastructure, difficulties in financing businesses, bureaucracy, tax instability etc. Such circumstances overstate the negative effect of tax rate increase in businesses.

State tax revenue distribution review

Given the fact that drastic cuts in taxation are not feasible, what is the alternative?

To start with, focus should shift to tax burden and expenditure ***redistribution/review.*** Both issues are beginning to move little by little.

In negotiations, tax-free income band reduction is being debated upon, yet safeguarding vulnerable social groups, in other words, protecting the poor. In Europe, this correlation is exactly the opposite than in Greece. Specifically, in Germany the tax free income band is €8,354, with a poverty threshold of €11,004, in Austria €11,000 and €13,956 respectively, while in the Netherlands, Italy and Portugal there is no tax-free income band; in Greece, the “indirect” tax-free income band ranges from € 8,636 to €9,500 depending on the marital or family status for employees, pensioners and farmers, with a poverty threshold of €4,512 per tax payer[22].

[21] See PBO’s previous quarterly reports.

[22] ELSTAT, Press Release, Poverty Risk, Survey on Income and Living Conditions 2015 (Reference period income 2014), 23 June 2016.

Reversing trends towards increasing tax burdens of the same individuals may be achieved through more effectively combatting tax evasion and avoidance, together with the tax system radical reform.

The government is trying to limit tax evasion via a series of measures (electronic transactions etc.). 2017 has started with a whole chain of new tax burdens (special tax on consumption, VAT increase in the Aegean islands, duties on telecommunications etc.) that had been approved by vote in 2016. Further taxes in 2018 remain a possibility.

It is evident that state tax revenue distribution revision is imperative. Speaking in terms of social criteria, it is inappropriate to increase indirect taxes' percentage in relation with direct taxes, something that has been acknowledged right from the start. Therefore, ***reversing this trend, would constitute a first step towards state revenue reorganization.***

<u>Spending review</u>

With regard to public expenditure, we note that ***debate over spending*** should not be reduced to horizontal cuts in public expenditure as a whole, or in major categories (such as salaries). Indeed, expenditures as GDP percentage are among the highest in Eurozone, mounting to 55%, that is above Eurozone average (49%). Only Finland and France present higher percentages[23]. However, what must be examined thoroughly and in depth, is not their reduction, but how they can become growth-friendly or serve social causes, for example through a better distribution. It is interesting that comparative analysis shows that ***countries with lower GDP percentage spending present better economic performance (and service quality), something that suggests, even in an indirect way, that there must be room for improvement in Greece.*** In other words, what must be sought is not less, but better state!

Furthermore, the way things are, it is our view that ***radical public spending review is becoming increasingly important.*** The main objective would be ***to achieve savings where appropriate, or, even better spending efficiency.*** Of course, growth and investments are the key to overcoming vicious circles.

In that connection, the issue of mismanagement and waste remains open. ***We share the view of many (both in government and major opposition) that there is still room for targeted savings, e.g. public procurement, public works and state consumption expenditures.***

Spending review is imperative, not only because of magnitude, quality and poor distribution, but also because of Greece's commitments for achieving fiscal management deliverables and particularly the target for primary surplus 3.5% GDP until 2018, as well as the possibility of fiscal adjustment mechanism. In this regard, the government is obliged to implement the agreed upon automatic correction mechanism all the way until MoU end, in case of primary surplus target divergence[24]. Moreover, the government seems to have finally accepted the

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[23] European Commission, Quality of public finance, Note to the Eurogroup, 05.09.2016.

[24] *Supplemental Memorandum of Understanding*, 16.06.2016, paragraph 2.1.

fiscal mechanism prolongation, at least for 2019-2020, without currently proceeding to specific legislative measures. They would accept, however, *"to describe measures that would possibly be necessary"[25].*

In this context, it is very important to mention the alternate Minister's for Economy Mr. Houliarakis' initiative to guarantee the smooth implementation of the 2017 Budget. In case of positive response, ministries shall have to review spending, examining expenditures to be retained and those to be reduces or abolished. In other words, ***2017 Budget ceilings may bring about some kind of spending rationalization.*** This, of course on condition of abandoning "political reasoning".

More specifically, in December 2016, Mr. Houliarakis sent a circular to all ministries calling them to sign a "memorandum of cooperation", thereby committing to

- Implement corrective interventions in cases of obvious target divergences
- Operate internal systems and mechanisms for monitoring budget implementation, in order to guarantee sound financial management
- Not undertake any obligation if not ensuring funds for its coverage
- Sign memoranda with supervised bodies, for taking all appropriate and necessary measures, such as spending reduction associated to revenue received
- Take all necessary measures towards a more realistic assessment, estimate and monitoring of revenue and expenditure of general government supervised bodies/entities.

The aforementioned initiative is of particular interest. Its outcome remains to be seen, as it is fully opposite from the existing fiscal management culture[26]. The circular proposes a spending review within major categories, such as "subsidies to supervised bodies/entities" which do not play a substantial role –an issue pending for 20 years- or funding undersecretariats without any objective or competence.

Another example of spending review within a category (that of social expenditures) already under way are welfare benefits. These are already under review in combination with the gradual implementation of the Social Solidarity Income. The World Bank has published a relevant study that may constitute the basis for specific decisions towards Welfare sector reorganization.

In general, spending structure in Greece presents particularities as compared to that of OECD countries, something that gives rise to further thoughts.

<u>Trade-offs</u>

Similarly, alternatives should be explored in depth prior to expenditure announcement. ***The case of the special grant to low-level pensioners*** is characteristic. Certain taxes' "outperformance", and the associated ***expectation*** that 2016 shall close with a surplus larger than the one anticipated, gave to the government the opportunity to use part of revenue for ***low-level pensioners' support.*** In this case we will focus on the substance, overlooking procedural issues

[25] Interview of the Minister Euclid Tsakalotos in the Greek newspaper *Kathimerini,* 31.12.2016.

[26] www.ethnos.gr , 29.12.2016.

concerning possible time pressures for materializing the initiative or the resulting complication in relations with the institutions.

First, it seems that the prioritization of social needs was not realistic. Indeed, the special grant to low-level pensioners only covered part of social needs and, certainly not in the best way, as ***ignoring other categories of vulnerable social groups (such as the long-term unemployed) with an income below the limit of €850, thus repeating malpractices of the past.***

Second, it is our view that we were reminded of the pending in-depth debate over ***available resources distribution choosing between allowances and social services.*** Instead of giving the grant, it could have been investigated which ***social services*** are in need of support, for spending the €617 mn (or part of it, given that expenditure would be less through introducing processed income criteria) on improving social services, e.g. for the operation of intensive care units in hospitals, for correcting shortages of medicines and addressing needs in chemotherapy departments, for establishing living centers for individuals with special needs that are not capable of living independently, for supporting second-chance schools where excellent and dedicated schoolteachers work, for directly employing healthcare staff, etc. ***Improving social services' quality has multiplying growth effects for society's weaker sections than lump-sum grants.*** Of course, extending and modernizing social services requires time and institutional support.

Lastly, our social security system is not sustainable. This is a stark reality. It currently absorbs 11% GDP while in the other European countries an average of 2.25% GDP[27]. This percentage is expected to drop only marginally in the next years. The social security system suffers pressures from ageing population and high unemployment rates. Therefore, it needs serious scrutiny in order to explore ways for becoming sustainable.

In the meanwhile, re-calculation of 2.6 mn main pensions has started, the redemption value of credited pensionable service years is increased, new cutbacks are made to the Social Solidarity Allowance for Pensioners (EKAS) etc. The contribution of all the aforementioned to system stabilization remains to be seen. In any case, an organized, in depth debate should start right away in order to abandon the philosophy of last-minute dealing with situations as "extraordinary". ***Any policy resisting the necessary structural reforms for social security system sustainability, actually surrenders the system to luck and the markets.***

3. POSITIVE STEPS AND REFORM DELAYS

We do not underestimate the many positive steps of the previous period: investments in infrastructure, especially of major roads, have revived after the Government's agreement with manufacturers and concessionaires. In this regard, the pursuing of increasing public investment that will affect private investment, is encouraging.

Moreover:

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[27] Poul M. Thomsen "The Case for Making the Greek Budget More Growth Friendly" in http://www.imf.org/external/np/blog/2016/pdf/Greece-TN-121216.pdf.

- There is a decrease in public debt to private individuals in November 2016, compared to October 2016. However, ***the public sector seems to continue creating debts***, otherwise such a small drop cannot be explained, taking into account that the Government has received €1.8 bn from its partners for debt repayment.

- Social welfare has started to show a structural improvement in order to reach European standards with the application of ***Social Solidarity Income (SSI)*** and the simultaneous rationalization of welfare allowances. This reform will ensure SSI funding, while, combined with a reformed protection of the unemployed, it would support the required greater flexibility in labour markets. It is well noted that the previous Government had started a pilot implementation of the measure.

- Efforts towards the limitation of tax evasion have become more systematic

- In the field of public administration, laws were adopted in 2016, providing, inter alia, for a new mobility system as well as for civil servants' assessment. Interestingly, the President of the Hellenic Parliament, Mr N. Voutsis, launched the assessment of formal and substantive qualifications of the Parliament's employees[28].

- In implementation of the Memorandum, an Independent Authority for Public Revenue, replacing the SG for Public Revenue has finally been founded, as well as the Single Institution for Social Insurance (EFKA) and also the process for an "integrated approach" of independent authorities etc. has begun.

In general, steps to the right direction are being realised or, to paraphrase the title of a recent book, institutional Greece is changing[29].However, in some reforms, difficulties and delays lurk in the details. It is indicative that there are pending circulars concerning implementation of the pension reform, while in the health sector, the pre-approval plan of referrals to private providers based on "e-referrals" (Memorandum commitment) has not yet been drafted, while public hospitals continue to lose over €100 mn because of supplies' mismanagement[30]! In public administration, although the laws on mobility have been adopted, their implementation depends on drawing up organizational charts of ministries and supervised private law entities and local authorities so as to identify existing "gaps". Nevertheless, there is a delay at the relevant procedures and the original completion deadline of December 31, 2016 expired without satisfactory results, thus the new deadline was set for February 16, 2017. Also, the application of the new evaluation system for civil servants is pending. Those who have experienced the turbulence accompanying the setting up of organisations e.g. in universities, are well aware that it is a major project requiring to move away from political ties, party affiliations as well as personal networking logics. ***In sectors calling for structural changes rather than "cement", the situation is blurry or presenting stagnation.***

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[28] *Greek Newspaper "Newspaper of Syntakton"*, 1.12.2016. The relevant decision was published on Parliamentary Transparency.

[29] Skalkos D., *Does Greece Changes;* Publications Epikentro, Thessaloniki 2016.

[30] For the Public Health sector see, among others, the article of Athina Dretta (ex General Secretary of Social Security) in the Greek Newspaper Kathimerini, 24.12.2016. In the example of the Public health sector it can be easily demonstrated how the reforms reduce pressure for increased public spending.

Experience gained from the implementation of the current but also of the previous two Memoranda reveals the distance between formal adoption of reforms and their effective implementation. According to the regular OECD report (OECD Economic Surveys, 2016), Greece presents the smallest percentage of reforms' implementation as compared to other countries implementing adjustment programmes. In addition, there is always the danger of distortion in practice, or even of abandonment of reforms over time. A special reference should be made for privatizations. Certainly the main goal is not funds collection. Privatisations can increase economic efficiency under certain conditions, also generating jobs and sending positive signals to the investment community. All these yield potential public revenue, in case of annual revenue losses on part of non-privatized units being less than privatization revenue, the possible burden undertaken through privatization procedure (e.g. subsidies) and the revenue from the economic functioning of the privatised unit, and thus reduce the pressure for new taxes or for other revenue sources in general. But there are delays.

Domestic halting factors still affect ***many reform areas presenting ambiguity*.** Although multi-bills with all kinds of changes have been voted, unfinished business burdens relations with the Institutions. The list does not seem long, but certainly contains critical folders: employment relations, privatizations with no progress (Ellinikon Airport, Hellenic Gas Transmission System Operator, TRAINOSE etc.), social insurance of doubtful viability, non-performing loans etc. ***Practically, the overall balance of the programme is at stake. How or how much delays, inertia and contradictions in the front of memorandum deliverables, as well as the low levels of confidence, prevent the Greek economy from moving ahead is still unclear.***

Considering the current situation, ***the Greek economy might undergo a stress test via one more economic shock*** that could be caused either from negotiations' failure with the partners (ESM and ECB) or from an open conflict between EU and IMF resulting in the latter's withdrawal, without a backup plan for the continuation of the programme. Future outlook: Probably, there will be frictions and rear-guard actions in 2017; official expectations for growth will be put to test. However, ***Memorandum implementation will probably continue, as evidently, neither the Government nor the Opposition would want the bomb of bankruptcy to burst in their hands.***

Overall Assessment of the PBO

Even achieving the most optimistic forecasts over a growth rate of 0.3% in 2016[31] is not enough, especially considering that the eighth year of the crisis has just been left behind; yet, it would still be a positive development. The question remains ***whether conditions for a strong recovery have been created***[32] (as the Government and everybody hopes) and especially over time ("sustainable recovery"). ***In our opinion, data show that these conditions have not been created*** and questions remain unanswered as to which internal and external factors would hopefully give such impetus. ***In our opinion, only a daring reform effort that will establish the appropriate economic, business and social environment would create grounds for the creation of such preconditions together with a potential upward trend for the country.***

31 European Commission, Winter Forecast 2017.

32 PBO, Report on the Draft of the State Budget 2017, November 2016. (in Greek)

1 CURRENT ECONOMIC CONDITIONS: Signs of fragile recovery with several uncertainties.

Based on the data by ELSTAT[33], the Greek economy during the third quarter of 2016 recorded a positive GDP growth rate (1.8%) y-o-y (2010 constant prices, s.a.), as shown in Table 1 and Graph 1. On a quarterly basis, in the third quarter of 2016 Greece's GDP (2010 constant prices, s.a.)recorded a positive growth rate of 0.8%, as well. Also during the third quarter, there was a significant increase in the GDP in current prices (s.a.) by 1.3% y-o-y and 0.6% q-o-q. ***However, as regards the growth rate of the third quarter of 2016, it is appropriate to take into account the very low comparison basis (third quarter 2015), due to the peak of uncertainty, the bank holiday and the capital controls.***

Table 1 GDP & main components of Greece.

	2014	2015	2016 q1		2016 q2		2016 q3	
% change			y-o-y	q-o-q	y-o-y	q-o-q	y-o-y	q-o-q
Private Consumption	0.4	-0.2	-0.8	-0.2	-1.2	-0.1	5.1	0.3
Public Consumption	-1.4	0	-2.1	0	-0.9	0.7	-0.6	0.2
Gross Fixed Capital Formation	-4.6	-0.2	-9.5	-15.8	17.9	9.7	12.6	1.7
Exports of Goods & Services	7.8	3.4	-10.5	-3.1	-3.2	6.4	10.2	3.7
Imports of Goods & Services	7.6	0.3	-8.7	-1.3	4.9	9.1	12	-10.2
GDP								
Current Prices (€ bn)	177.941	175.697	43.506		43.912		44.188	
Growth rate (%)	-1.5	-1.3	-1.1	-0.8	0.1	0.9	1.3	0.6
2010 Constant Prices (€ bn)	184.873	184.468	45.915		46.078		46.428	
Growth rate (%)	0.4	-0.2	-0.8	-0.6	-0.5	0.4	1.8	0.8
Source: *ELSTAT*								

For the whole year 2016, the State Budget Report for 2017 and the European Commission in its autumn forecasts estimate a further contraction of the Greek economy by 0.3%[34]. For 2017 there is an ambitious forecast of 2.7%[35], due to the recovery in private consumption, exports and investment. But in order to achieve this target, the Greek Government should make significant efforts to restore confidence and to reduce uncertainty, to avoid long delays in the completion of the second review, to successfully implement structural reforms and privatizations and to smoothly repay the arrears to the Private Sector (without accumulating new arrears). Finally, the return to a sustainable recovery requires immediate action for the full and proper functioning of the banking system.

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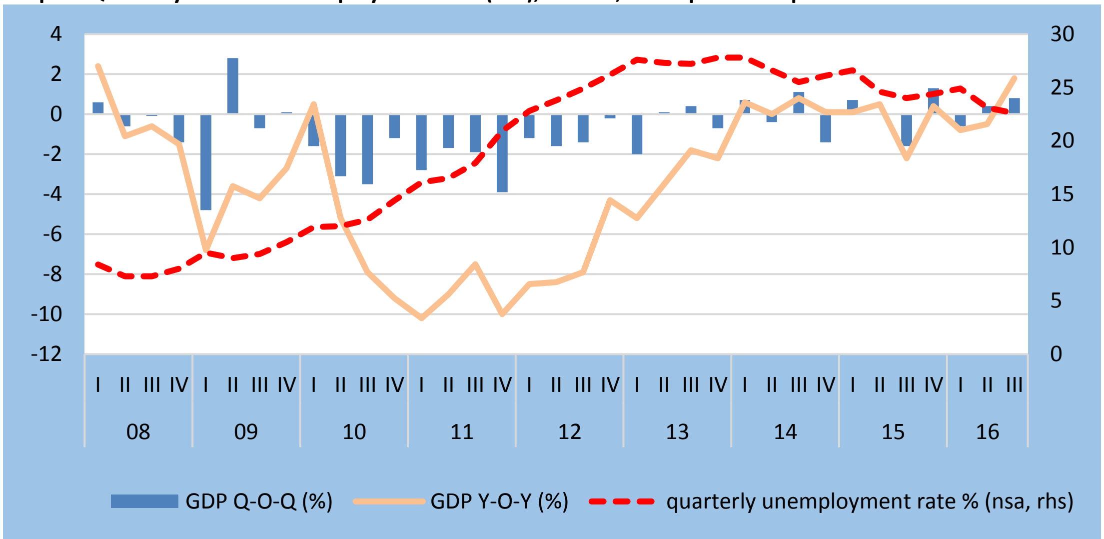
33 ELSTAT, Press Release, Quarterly National Accounts, 3rd Quarter 2016, 29.11.2016.

34 However, the growth rate for 2016 is estimated to be around zero. See also Bank of Greece, Interim Report December 2016: +0.1%, University of Athens Intelligent Deep Analysis: +0.24%, according to November projections.

35 Apart from the projections of the Greek Government and its creditors, other institutions and international organizations appear less optimistic about the growth rate of 2017 (OECD Economic Outlook, Volume 2016, Issue 2:+1.3% and University of Athens Intelligent Deep Analysis:+1.01% according to November projections).

Graph 1 Quarterly GDP and unemployment rate (nsa), Greece, 2008 q1 – 2016 q3.



Source: *ELSTAT*

In the third quarter of 2016, ***the unemployment rate in Greece fell to 22.6%***[36], slightly lower compared to 23.1% in the previous quarter and 24% of the corresponding quarter of 2015 (Graph 1). Employment also increased by 0.9% q-o-q and by 1.8% y-o-y. Note that, based on the research, women, and young people (15-24) face a higher unemployment rate than the general, 27.2% and 44.2% respectively. However, a significantly lower rate face holders of postgraduate degrees (M.Sc.'s and Ph.D.'s 18.1% and 11.5%, respectively). ***Note finally that the decrease in the unemployment rate on an annual basis is primarily due to increased employment in the categories "Public administration and defense. Compulsory social security", "Manufacturing", "Transportation and Storage" and the category" Accommodation and food service activities".*** Also, due to the significant expansion of flexible forms of employment[37]. The State Budget Report for 2017 estimates a rate of 23.7% in 2016 and 22.6% in 2017 (Labour Force Survey), while the European Commission in its autumn forecasts estimates that the rate will stand at 23,5% in 2016, while in 2017 it is projected to fall to 22.2%.

Table 2 illustrates the major difficulties that enterprises in Greece still face. In 2014 there was a marginally negative balance (-134), a positive balance was recorded in 2015 (+2107, primarily due to the first half of the year), while in 2016 there was a strongly negative balance (-6528). ***Although this brief analysis includes only quantitative rather than qualitative information, the findings are particularly worrying for an economy that tries to recover from a prolonged recession.***

The Economic Sentiment Indicator (ESI) by European Commission showed an improvement in Greece in December, standing at 94.6 points, which is the highest level since April 2015, but remained at a lower level than 2014 and first quarter of 2015. In November the ESI declined, after the improvement in October, standing at 92.4 points, down from 93.8 in October and 91.4 in September (Graph 7 in the annex). Regarding the individual components of ESI, all of them have recovered compared with the period with the peak of uncertainty in the summer of 2015 except for consumer confidence, which stood at -64.4 points, even lower compared

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36 ELSTAT, Press Release, Labor Force Survey, 3rd quarter 2016, 15.12.2016 (non-seasonally adjusted data).

37 ERGANI data, November 2016.

to the summer of 2015, ***reflecting the extremely negative expectations of households for the evolution of their disposable income.*** Finally, in the Euro Area, since August 2016 (103.5 points) there has been continuous improvement of ESI and in December stood at 107.8 points, which is higher compared with the previous year, and compared with the corresponding period of 2014.

Table 2 establishments and closures of corporations in Greece.

	Jul-Dec 2014	Jul-Dec 2015	Jul-Dec 2016	2014	2015	2016
Establishments	16495	12489	12742	37026	30331	28566
Closures	18803	15223	17097	37160	28224	35094
Balance	-2308	-2734	-4355	-134	2107	-6528
Source: *GEMH (data until Thursday 19/1/2017, 12:00:10)*						

The ***Harmonized Index of Consumer Prices (HICP)***[38] in December 2016 recorded a marginally positive y-o-y change (+ 0.3%), while in November its y-o-y change was marginally negative (-0.2%), after a positive y-o-y change + 0.6% in October (Graph 10 in the Annex). The PBO highlights that the increases in indirect taxes, especially those on fuels, along with the acceleration in economic activity are expected to have an upward impact on the index. Already "Transportation" showed a significant y-o-y increase in November (+ 2.2%) and December (+ 1.3%) and the "Alcoholic Beverages and Tobacco" as well (+ 0.9% and + 1.8% respectively). Also in December there was an increase in the group "Hotels –Cafes- Restaurants (+ 1.4%) and "Housing" (+1.9%). It should be also stressed that in December 2016 the National Consumer Price Index recorded a non-negative change (0.0%) for the first time since February 2013. Under the State Budget Report for 2017, the HICP in 2016 is estimated to have no change from -1.1% in 2015, while in 2017 it is projected to recover marginally (+ 0.6%). In contrast, in the Euro Area[39] December 2016 (+ 1.1%) was the seventh consecutive month with a positive y-o-y change of the index, although it still remains below the target of 2%.

The ***banking deposits of households and corporations***, according to the data from the Bank of Greece, do not seem to recover substantially. Specifically, in November 2016 amounted they to € 124.804 bn., increased by € 172 mn. compared with October (Graph 8 in Annex). This increase was due to an increase of € 512 mn. in "Non-Financial Corporations", as the remaining categories recorded a decrease compared with the previous month. In particular, banking deposits of "Households and Private Non-Profit Institutions" decreased by € 294 mn. compared with the previous month. In October the banking deposits of households and corporations had recorded a significant increase of € 1.16 bn., compared with the previous month, mainly due to the increase in "Households and Private Non-Profit Institutions" and in " Insurance companies". However, the banking deposits of the private sector in November 2016 were higher by almost € 4 bn. compared to the low of July 2015 ***reflecting the much slower than expected recovery of confidence in the Greek economy.*** In these severe liquidity conditions, ***banking financing to the domestic private sector*** in November fell by 1.3% y-o-y from -1.6% in October. Also, the monthly net flow of total financing in November was positive by € 62 mn. compared with a negative net flow of € 308 mn. In the previous month.

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38 ELSTAT, Press Release, Harmonised Index of Consumer Prices, December 2016, 04.01.2017.

39 Eurostat, *Flash Estimate - December 2016*, 1/2017, 4 January 2017.

The ***General Index of the Athens Stock Exchange*** in the fourth quarter of 2016 moved upwards from 569 to 643 points, closing in 2016 near the peak of the whole year. Although it has rebounded strongly from the low of February 11 (440 points), it is still at a very low level and significantly lower than in 2014 and the first months of 2015. Due to the stagnation and the uncertainties in the Greek economy and the banking system, the valuation of banking stocks, although they have rebounded, are still lower than the prices in the last recapitalization in November 2015. ***In other words, despite the moderately upward trend of the Index, the overall assessment of the Athens Stock Exchange does not seem to directly anticipate significant positive developments in the Greek economy.***

The ***average monthly yield of the ten-year Greek government bonds***, based on figures from the Bank of Greece in December 2016 fell (for the first time since 2014) below 7% (6.94%), following a downward path since September 2016. Although it has recovered from a double-digit rate in February 2016, (10.41%, peak for 2016), the yield on Greek ten-year bond is well above compared to other countries of southern Europe (Spain, Portugal, Italy), showing the difficulty of the country to return to the international markets. The deceleration of the ten-year bond yield in the last quarter of 2014 was mainly due to the announcement of short-term measures for the debt, but substantial further improvement is expected in the medium-term measures for the debt and the country's access to the ECB's quantitative easing program. The evolution of prices and yields on Greek ten-year bonds and the negative relationship between them is shown in Graph 11 in the Annex.

In the third quarter of 2016, ***the compensation per employee***[40] increased by 0.9%, for the second consecutive quarter after a significant increase in the second quarter by 2.7% y-o-y. ***Unit labor costs*** in the third quarter of 2016 increased for the third consecutive quarter by 0.6% y-o-y, after a significant decline in the five year period 2011-2015. In this context, ***labor productivity*** declined further by 0.3% in the third quarter of 2016, continuing its sharp decline in recent years. This development is a serious concern both for the competitiveness of the Greek economy and for the medium-term growth to the extent that it does not result in the reduction of profits to amortise the pressure on prices. The cumulative fall in the above mentioned figures during the crisis is reflected in Graph 9 in the Annex.

In this context, a further increase in ***total new arrears towards the Public Sector***, based on the official data from the Ministry of Finance, in the eleven- month period January - November 2016 (Graph 12 in the annex), highlights the exhaustion of tax paying capacity, while raising reasonable doubts about the effectiveness of the new measures. Specifically, in November 2016 they cumulatively amounted to € 12.63 bn, up from € 11.74 bn in October and € 10.34 bn in September. ***On average in the eleven- month period January - November 2016 they increased by € 1,15 bn per month.*** The recovery rate against these debts increased gradually, from 13.1% at the end of June, to 15.4% at the end of September and to 18.7% at the end of November. Moreover, the old arrears towards the Public Sector cumulatively amounted in November to € 81,56 bn, while receipts against this debt increased at the end of November to € 2.33 bn. Therefore, ***private debt (to banks, tax authorities, social security funds, stet owned enterprises etc.) may be destabilizing, if not treated promptly and effectively.*** Specifically, based on the official data at the end of November 2016 a total of 4,312,287 taxpayers

[40] The figures of this paragraph are non-seasonally adjusted. Source: ELSTAT e-publication The Greek economy, 05.01.2017.

have arrears towards the Public Sector, increased by 7.535 compared with October, when there was the significant reduction by 69 723 compared with the end September 2016. Indeed, under forced collection measures are already 826 211 taxpayers, increased by 22 408 compared with October 2016. Thus, the percentage of debtors under forced collection measures amounted in November to 49.06%, while this seems to be the main reason for the above performance in the collection of arrears.

2 FISCAL MANAGEMENT

2.1 The Execution of the State Budget (SB) in the twelve month period of 2016 (on a cash basis)

The State Budget (SB) in the twelve month period of 2016 presents a primary surplus of € 4.44 bn or 2.54% of GDP and a total deficit (including interest payments of € 5.58 bn) of € 1.14 bn or 0.7% of GDP. The Ordinary Budget (OB) presents a primary surplus of € 6.55 bn and the Public Investment Program (PIP) a deficit of € 2.1 bn.

The Primary Surplus of the SB is higher by 95.4% y-o-y and by 123.8% compared with the target of the SB 2016. The Primary surplus of the OB is higher by 70.3% y-o-y and higher by 50.3% compared with the target of the SB 2016, while the PIP surplus is higher by 34.0% y-o-y and lower by 11.2% compared with the corresponding target of the SB 2016.

In conclusion, the Primary Surplus of the SB in the twelve month period of 2016 presents an increase both y-o-y (by 95.4%) and in comparison with the target of the SB 2016 (by 123.8%). This improvement can be attributed, on the expenditure side, to the reduction of the OB expenditures by € 0.33 bn (compared with the target), and specifically to the reduction of the Primary expenditures of the OB by € 0.22 bn (compared with the target) and of the Guarantees called, while on the revenue side, to the increase of the Revenue before Tax Refunds by € 1.88 bn (compared with the target and by € 3.76 bn on an annual basis). **Finally, to the over performance of the Primary Surplus of the SB compared with the target contributes the significant reduction (by € 0.46 bn compared with the target) of the PIP expenditure.**

The Revenue of the SB

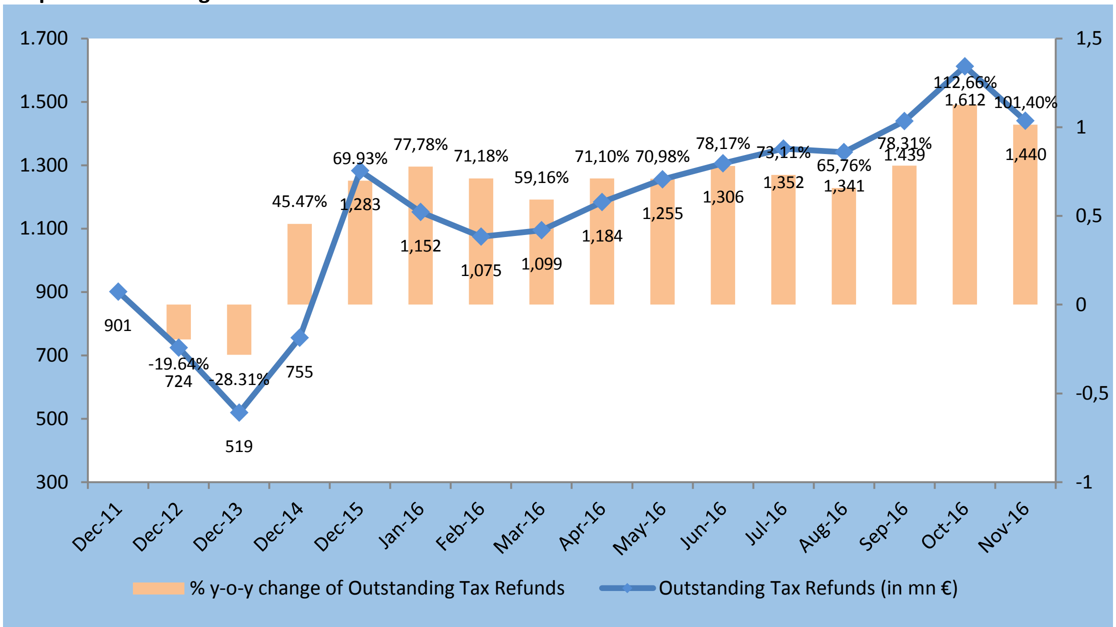
The Net Revenue of the SB has been increased in the twelve month period of 2016 by 5.1% y-o-y and by 3.2% compared with the target of the SB 2016. This increase (y-o-y) can be attributed mainly to the increase of the Net Revenue (revenue - tax refunds) of the OB by € 3.76 bn or by 7.64% y-o-y (exceeding the corresponding target of the SB of 2016 by € 1.88 bn or by 3.7%).

However, as can be concluded from the level and the rate of the continuous increase of the tax arrears of the private sector towards the public sector the citizens' tax-paying capacity has been exhausted. The tax arrears of the private sector towards the public sector amounted in November 2016 to € 94.2 bn or 53.85% of GDP, from which € 12.6 bn are "new debts", i.e. created in 2016.

The revenue from Privatizations showed a decrease in the twelve month period of 2016 by 58.27% on an annual basis and a decrease by 13.8% compared with the target in the SB 2016.

Tax Refunds have been increased by 11.67% y-o-y and reduced by 0.7% compared with the target of the SB 2016. ***It should be noted that the pending Tax Refunds of the Public Sector towards the Private sector have been increased by 101.4% in November 2016 compared with November 2015 amounting to € 1.44 bn*** **(see Graph 2).**

Graph 2 Outstanding Tax Refunds



Source: *Ministry of Finance*

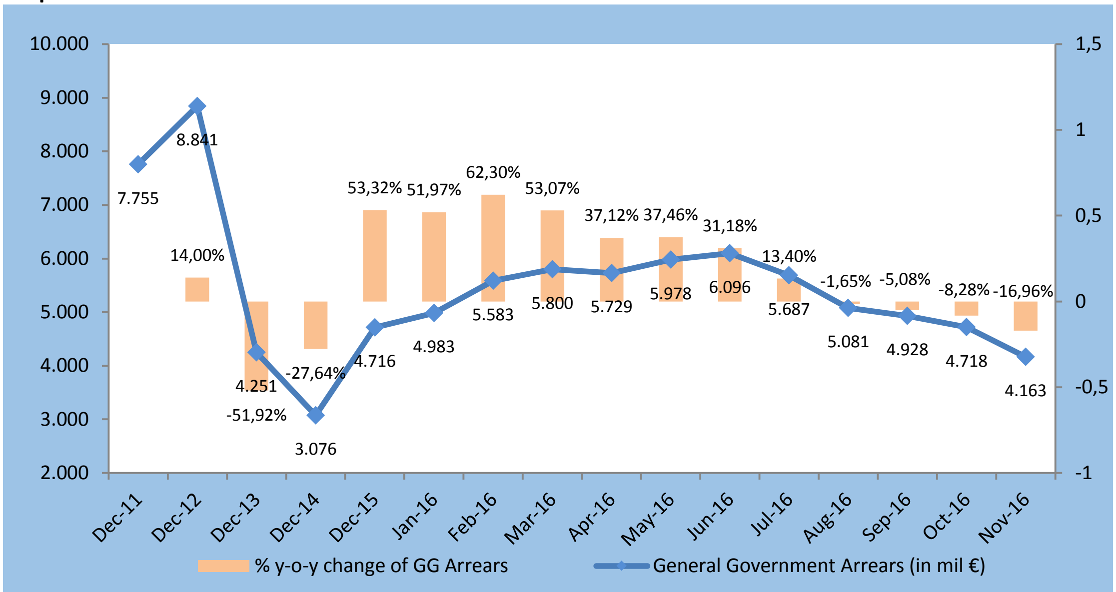
The Expenditure of the SB

In the twelve month period of 2016 the total expenditure of the SB increased by € 0.23 bn or by 0.41% y-o-y and reduced by 1.4% compared with the target of the SB 2016. The increase y-o-y is due to the OB expenditure increase by € 0.95 bn or by 2.31% (reduced by 0.5% compared with the target of the SB 2016) which exceeds the observed sum of decreases of the other categories of the OB expenditure and the PIP expenditure.

Specifically, the expenditure for the Guarantees Called have been reduced by € 0.29 bn or by 41.4% (reduced by 18.4% compared with the target of the SB 2016), the interest payment expenditure appear to be lower by € 0.22 bn or by 3.84% y-o-y (and by 0.4% compared with the target of the SB 2016) and the Loan disbursement fee to EFSF, banking fees and other public debt expenditures appear to be lower by € 113 mn or by 63.48% y-o-y (increased by 18.2% compared with the target set in the SB 2016).

However, the Primary Expenditure increase should be assessed by taking also into account the level and the rate of increase of the tax arrears of the public sector towards the private sector. The General Government Arrears towards the Private sector amounted to € 4.16 bn in November 2016 showing a y-o-y reduction by 16.96% (see Graph 3).

Graph 3 General Government Arrears



Source: *Ministry of FInance*

Concerning the repayment of the Public Sector arrears towards the Private Sector, of the pending tax refunds and the payment of outstanding pensions, a special funding from the ESM is planned for 2016 and 2017 of a total amount of € 6.6 bn. By the end of June 2016 an amount of € 1.8 bn had been disbursed from the ESM in a special account which was created for that purpose. Until the end of September the General Government entities have been funded with a total amount of € 1.97 bn and from this amount overdue obligations to third parties amounting to € 1.77 bn have been cleared. The previous amounts include an amount of € 420 mn which was offset in full by third parties debts to the Public Sector, without requiring a corresponding funding. Also, in the period July - September 2016 a funding of € 152 mn for the repayment of outstanding tax refunds was made and tax refunds amounting to € 107.3 mn were repaid. Nevertheless, due to the continuous accumulation of new arrears of the Public Sector their rate of decline due to the funding from the ESM is not yet sufficient and is not expected to fundamentally address the problem of the arrears of the Public Sector towards the Private sector, even more if the total estimated amount of € 6.6 bn will not be disbursed in full in 2016-2017.

2.2 High Primary Surpluses: Historical Experiences

The achievement of high (at least 3%, 4% or 5% of GDP) Primary Surpluses for many years (5, 8 or 10 consecutive years) is recorded as empirically and historically feasible but it is an exception.

Barry Eichengreen και Ugo Panizza[41] by looking at countries which had achieved surpluses averaging at least 3% of GDP for 5 years –have found that surplus episodes are more likely when growth is strong, the current account of the balance of payments is in surplus (savings rates are high) and the debt-to-GDP ratio is high (heightening the urgency of fiscal adjustment).

41 "A Surplus of Ambition: Can Europe Rely on Large Primary Surpluses to Solve its Debt Problem?" NBER Working Paper No. 20316, July 2014.

Small countries and economies heavily open to trade are more likely to exhibit large, persistent primarily surpluses.

However, excessively restrictive policies that reduce growth in the short run and lead to political turmoil and instability may backfire, amplifying investors' concerns. In its downgrades of European sovereigns, Standard & Poor’s mentioned that restrictive policies may have a negative effect on debt sustainability (Standard & Poor’s, 2012).

Moreover, when tax revenues rise, legislators and their constituents apply pressure to spend them. In 2014 when Greece, after years of deficits and fiscal austerity, enjoyed its first primary surpluses; the government came under pressure to disburse a “social dividend” of € 525 mn to 500 thousand low-income households (the Greek newspaper Kathimerini called these transfers “primary surplus handouts”). More recently, in December 2016, based on the estimation for the achievement of a Primary Surplus for 2016, the Government announced its decision for a social distribution of part of the revenue of the SB that resulted from its over performance compared with its target. This “social dividend” was estimated to amount € 617 mn distributed to 1.6 mn pensioners from a total of 2.7 mn. Budgeting, as is well known, creates a common pool problem, and the larger the surplus, the deeper and more tempting is the pool. Only countries with strong political and budgetary institutions may be able to mitigate this problem.

From an economic point of view, a global or a European recession could distort the efforts even of the most dedicated to fiscal targets Government for the achievement of high Primary Surplus even in the medium or long run (e.g. for 5 or 10 years). The reduction of the economic activity, i.e. a recession, consequently leads to a reduction of the Government expenditures and thus to a further self-sustaining recession.

These findings are not very encouraging and supportive of the view that Greece will be able to achieve high and sustained primary surpluses as those recently agreed with the Institutions. There exist both political and economic reasons which cast doubt on the possibility of achieving high primary surpluses.

Barry Eichengreen and Ugo Panizza define a primary surplus episode as large when the average value of the primary surplus during the episode is, alternatively, greater than 3, 4, or 5 per cent of GDP. They define it as persistent when it lasts at least 5, 8, or 10 years. They thus have a total of 9 definitions of large and persistent surpluses. In several cases, a series of overlapping periods satisfies one or more of the above definitions. Belgium, for instance, had an average primary surplus greater than 3 per cent of GDP for each five-year period from 1989-93 to 2004-08 and for each ten-year period from 1987-96 to 2000-09. Since these overlapping episodes would be problematic for the corresponding statistical analysis, they build a dataset of non-overlapping episodes by selecting, among all possible candidates, the episode with the largest average primary surplus in any given 5, 8, and 10 year window. Tables 3, 4 and 5 below rank in a per year period (5, 8 and 10 years) the countries that meet the above definitions.

The results (Tables 3, 4 and 5) show that large and persistent primary surpluses are relatively rare. Out of 235 non-overlapping five-year periods in their dataset, there were 36 five-year non-overlapping episodes with an average primary surplus of at least 3 percent of GDP (15 per cent of the sample), 18 five-year episodes with an average primary surplus of at least 4 per cent of GDP (8 per cent of the sample), and 12 five-year episodes with an average primary surplus of at least 5 per cent of GDP (5 per cent of the sample).

Eight-year periods of large primary surpluses are even more exceptional. Out of 185 non-overlapping episodes, they find 17 episodes with an average primary surplus of at least 3 per cent of GDP (9 per cent of the sample), 12 episodes with an average primary surplus of at least 4 per cent of GDP (6 per cent of the sample), and 4 episodes with an average primary surplus of at least 5 per cent of GDP (2 per cent of the sample).

Finally, out of 113 non-overlapping ten-year episodes, there are 12 episodes with an average primary surplus of at least 3 per cent of GDP (11 per cent of the sample), 5 episodes with an average primary surplus of at least 4 per cent of GDP (5 per cent of the sample), and 3 episodes with an average primary surplus of at least 5 per cent of GDP (2.5 per cent of the sample).

Thus, large primary surpluses for extended periods are possible, but they are the exception.

Table 3 **Non-overlapping primary surplus episodes, 5-year periods**

$\geq$ 3% of GDP		$\geq$ 4% of GDP		$\geq$ 5% of GDP	
BEL1998	5.97*	BEL1998*	5.97	BEL1998*	5.97
BRA2004	3.58*	CAN1997*	5.05	CAN1997*	5.05
CAN1997	5.05*	CHL2004	5.33	CHL2004	5.33
CHL1991	3.54	DNK1985*	5.49	DNK1985*	5.49
CHL2004	5.33	DNK2004	4.76	IRL1996*	5.34
DNK1985	5.49	FIN1998*	4.75	NOR1981	5.39
DNK1997	3.50*	IRL1988*	4.78	NOR2004	13.71
DNK2004	4.76	IRL1996*	5.34	NZL1993	5.69
FIN1976	3.39	ITA1996*	4.81	PAN1994*	6.77
FIN1998	4.75*	NOR1981	5.39	SGP1991*	12.26
GRC1996	3.91*	NOR2004	13.71	SGP2004	6.48
HKG2007	3.23	NZL1993	5.69	SWE1986*	5.43
IRL1988	4.78*	NZL2002	4.17		
IRL1996	5.34*	PAN1994*	6.77		
ISL2003	3.71	SGP1991*	12.26		
ISR1986	3.14*	SGP2004	6.48		
ITA1996	4.81*	SWE1986*	5.43		
KOR1988	3.16	TUR2002*	4.48		
KOR1999	3.77				
LUX1997	3.39				
MEX1991	3.78				
NLD1996	3.48*				
NOR1981	5.39				
NOR2004	13.71				
NZL1993	5.69				
NZL2002	4.17				
PAN1994	6.77*				
PAN2005	3.35*				
PER2004	3.01				
PHL2004	3.47*				
SGP1991	12.26*				
SGP2004	6.48				
SWE1986	5.43*				
SWE1997	3.45*				
THA1991	3.65				
TUR2002	4.48*				
Average	**4.81**		**6.15**		**6.91**
N. Episodes	**36**		**18**		**12**

Note: The year refers to the beginning of the episode (for instance, in column 1, BEL1998 indicates an episode that starts in 1998 and ends in 2002). The numbers report the average primary surplus over the period. * Denotes episodes which overlap with periods of high or rapidly growing debt.

Table 4 Non-overlapping primary surplus episodes, 8-year periods

≥ 3% of GDP		≥ 4% of GDP		≥ 5% of GDP	
BEL1997	5.51*	BEL1997*	5.51	BEL1997*	5.51
CAN1997	4.01*	CAN1997*	4.01	NOR2001	11.57
CHL1991	3.02	DNK1984*	4.24	SGP1990*	10.93
CHL2001	3.26	DNK2000	4.02	SGP2005	5.84
DNK1984	4.24*	FIN2000*	4.12		
DNK2000	4.02	IRL1993*	4.72		
FIN2000	4.12*	ITA1995*	4.04		
GRC1994	3.27*	NOR2001	11.57		
IRL1993	4.72*	NZL1993	4.46		
ITA1995	4.04*	SGP1990*	10.93		
KOR1995	3.38	SGP2005	5.84		
NOR2001	11.57	TUR1999*	4.11		
NZL1993	4.46				
SGP1990	10.93*				
SGP2005	5.84				
SWE1984	3.82*				
TUR1999	4.11*				
Average	**4.96**		**5.63**		**8.46**
N. Episodes	**17**		**12**		**4**

Note: The year refers to the beginning of the episode (for instance, in column 1, BEL1997 indicates an episode that starts in 1997 and ends in 2003). The numbers report the average primary surplus over the period. * Denotes episodes which overlap with periods of high or rapidly growing debt.

Table 5 Non-overlapping primary surplus episodes, 10-year periods

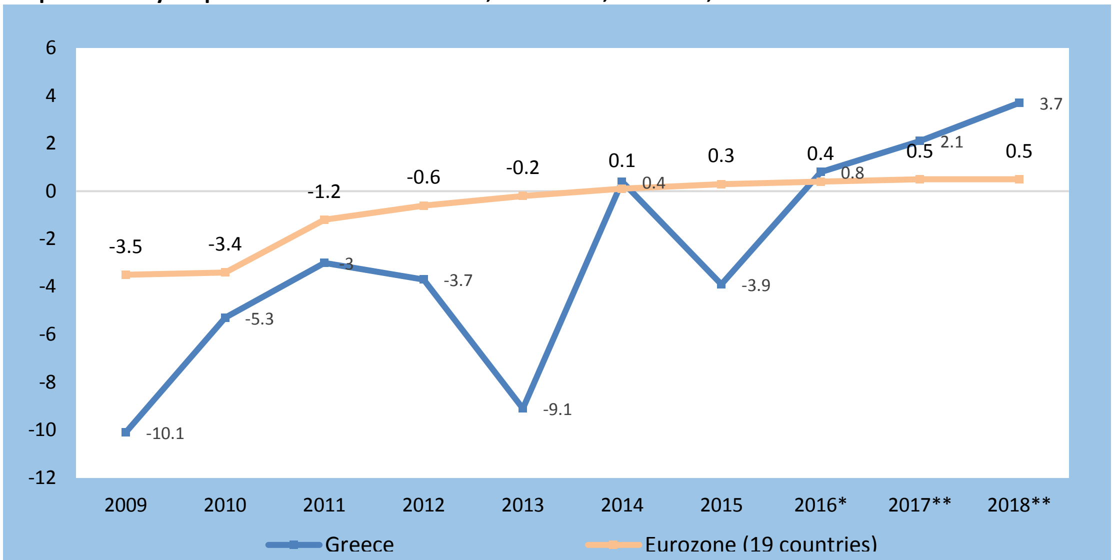
≥ 3% of GDP		≥ 4% of GDP		≥ 5% of GDP	
BEL1995	5.19*	BEL1995	5.19*	BEL1995	5.19*
CAN1996	3.72*	IRL1991	4.70*	NOR1999	11.07
DNK1984	3.44	NOR1999	11.07	SGP1990	9.30*
DNK1999	3.97	NZL1994	4.14		
FIN1999	3.95	SGP1990	9.30*		
IRL1991	4.70*				
ITA1993	3.60*				
KOR1993	3.33				
NOR1999	11.07				
NZL1994	4.14				
ς SGP1990	9.30*				
TUR1999	3.74*				
Average	**5.01**		**6.88**		**8.52**
N. Episodes	**12**		**5**		**3**

Note: The year refers to the beginning of the episode (for instance, in column 1, BEL1995 indicates an episode that starts in 1995 and ends in 2004). The numbers report the average primary surplus over the period. * Denotes episodes which overlap with periods of high or rapidly growing debt.

Primary Surpluses of the EA-18 Countries in the Period 2009-2016

As can be observed in Table 6Table 5, in the Euro Area, since the start of the recent crisis and until 2016 (estimation) there hadn't been a Eurozone country to achieve a Primary Surplus (according to ESA 2010) higher than 2.3% of GDP (cases of Italy and Germany only in 2012 and of Cyprus only in 2016 as estimation) and for a period of time greater than 1 year. However, many Eurozone countries achieved a significant fiscal adjustment as reflected from the evolution of their GG Primary Surplus. Greece, undoubtedly achieved a huge fiscal adjustment in the period 2009-2016, while for the years 2013 and 2015 the high primary deficit as a percentage of GDP (-9.1 and -3.9 correspondingly, according to ESA 2010) is a result of the expenditures due to recapitalization costs and the support program of the Greek financial institutions.

Graph 4 Primary Surplus of General Government, 2009-2018, % of GDP, ESA 2010



* Estimation, ** Forecast
Source: *European Commission, European Economic Forecast, Autumn 2016*

Table 6 Primary Surplus (+) or Deficit (-) General Government (Excessive Deficit Procedure), % of GDP, ESA 2010

YEAR	BE	DE	EE	IE	EL	ES	FR	IT	CY	LV	LT	LU	MT	NL	AT	PT	SI	SK	FI	EA-19
2008	2.9	2.5	-2.5	-5.7	-5.4	-2.9	-0.4	2.2	3.4	-3.6	-2.4	3.7	-0.8	2.3	1.4	-0.7	-0.3	-1.1	5.6	0.8
2009	**-1.6**	**-0.6**	**-2**	**-11.8**	**-10.1**	**-9.3**	**-4.8**	**-0.9**	**-3.1**	**-7.5**	**-7.9**	**-0.3**	**0**	**-3.4**	**-2.2**	**-6.8**	**-4.6**	**-6.4**	**-1.2**	**-3.5**
2010	**-0.4**	**-1.7**	**0.3**	**-29.3**	**-5.3**	**-7.5**	**-4.4**	**0**	**-2.7**	**-6.7**	**-5.1**	**-0.2**	**-0.1**	**-3.2**	**-1.6**	**-8.2**	**-4**	**-6.2**	**-1.3**	**-3.4**
2011	**-0.5**	**1.5**	**1.3**	**-9.3**	**-3**	**-7.2**	**-2.5**	**1**	**-3.5**	**-1.6**	**-7.1**	**1**	**0.6**	**-2.5**	**0.2**	**-3.1**	**-4.8**	**-2.7**	**0.3**	**-1.2**
2012	**-0.6**	**2.3**	**-0.1**	**-3.9**	**-3.7**	**-7.5**	**-2.2**	**2.3**	**-2.9**	**0.8**	**-1.2**	**0.9**	**-0.6**	**-2.2**	**0.5**	**-0.8**	**-2.1**	**-2.6**	**-0.8**	**-0.6**
2013	**0.3**	**1.8**	**-0.1**	**-1.4**	**-9.1**	**-3.5**	**-1.8**	**2.1**	**-1.8**	**0.6**	**-0.9**	**1.5**	**0.3**	**-0.9**	**1.2**	**0**	**-12.5**	**-0.8**	**-1.4**	**-0.2**
2014	**0.2**	**2.1**	**0.8**	**0.1**	**0.4**	**-2.5**	**-1.8**	**1.6**	**-6**	**-0.1**	**0.9**	**1.9**	**0.8**	**-0.8**	**-0.3**	**-2.3**	**-1.9**	**-0.8**	**-1.9**	**0.1**
2015	**0.5**	**2.2**	**0.2**	**0.7**	**-3.9**	**-2**	**-1.5**	**1.5**	**1.7**	**0.1**	**1.3**	**2**	**1.2**	**-0.6**	**1.3**	**0.2**	**0.3**	**-1**	**-1.6**	**0.3**
2016*	**-0.5**	**2**	**0.6**	**1.5**	**0.8**	**-1.8**	**-1.5**	**1.6**	**2.3**	**0.3**	**0.9**	**1.7**	**1.6**	**0.3**	**0.7**	**1.7**	**0.4**	**-0.7**	**-1.2**	**0.4**
2017**	0.1	1.6	-0.3	1.7	2.1	-1.1	-1.2	1.4	2	0	0.7	0.4	1.5	0.7	0.8	2.2	0.7	-0.1	-1.4	0.5
2018**	-0.2	1.4	-0.1	1.7	3.7	-0.7	-1.3	1.1	2.5	-0.3	0.7	0.5	1.4	0.8	1	1.8	0.9	0.8	-1	0.5

*Estimation, **Forecast
Source: *European Commission, European Economic Forecast, Autumn 2016*

3 STRUCTURAL REFORMS

3.1 Delays and revenue shortfall in the privatizations program

In general, privatizations can have a positive impact on the economy by attracting investment, technology cluster, revenue creation for the State and also through the consolidation of stability and confidence. On the other hand, as already highlighted by the PBO, privatizations- in order to serve the public interest- should be transparent, and should also take into account the market conditions to make deals at sensible prices and ***avoid to transform public monopolies into private.***

In mid-December 2016, 24% of ADMHE was transferred to the bidder company from China, making ADMHE the second largest Chinese investment in Greece. On the contrary, the Greek side and the company from Azerbaijan did not eventually reach an agreement for the sale of 66% of DESFA. Note, however, that energy issues, apart from the economic, have a geopolitical dimension, as well. However, as mentioned in previous quarterly reports by the PBO, significant privatizations have been completed lately, while the HRADF has a very important portfolio under way[42].

Furthermore, according to the Eurogroup statement on Greece (5/12/2016), "the appointment of the members of the Board of Directors of the Hellenic Corporation of Assets and Participations (HCAP) should be implemented before the end of January 2017 to make the fund fully operational[43]."

As regards revenue from privatizations[44], based on the State Budget Report 2017, it is expected to stand at € 123 mn in 2016, against an initial projection of € 1,802 bn in the State Budget Report 2016, recording significant lag. Also, the revenue in 2016 is estimated to be 51.5% lower compared to 2015. The State Budget Report 2017 provides for revenues from privatizations of € 2,044 bn in 2017, which is 1561.4% higher than the estimate for 2016. ***The great lag in 2016 (-93%), along with the difficulties of the government to further implement the privatizations program, make the aforementioned target (€ 2,044 bn in 2017) rather ambitious.*** According to the "Supplemental MoU", the implementation of the privatizations' program aims to generate further annual revenue (excluding bank shares) for 2016, 2017 and 2018 of € 2.5 bn, € 2.2 bn and € 1.1 bn, respectively, on top of € 0.4 bn collected in 2015. Note, however, that the figures in the Supplemental MoU are not comparable to the figures in the State Budget Report 2017, as calculated under a different methodology.

3.2 Delays in the labor market reform.

Labor market reform is still a critical issue in the negotiations of the second review. The Greek Government insists on the reinstatement of collective bargaining, the scalability of sectoral

42 http://www.hradf.com/en/portfolio and State Budget Report 2017 page 141 (in Greek).
43 http://www.consilium.europa.eu/en/press/press-releases/2016/12/05-eurogroup-statement-greece/
44 European System of Accounts (ESA).

employment contracts, in the non-reset of lock out,[45] protection of collective dismissals and the non-increase of the threshold for the definition of collective dismissals from 5% to 10%. The Greek Government considers that there is no strong argument for changing the limit of collective dismissals while the restoration of collective bargaining can achieve worker's protection. This opinion is consistent with ILO and moreover is expressed in the Review of Greek Labor Market Institutions from the Expert Group.[46] Furthermore, the Minister of Labor argues that a control mechanism of collective dismissals is necessary in order to safeguard workers' rights.[47]

The decision Court of Justice of the European Union states that the Greek legislation is not opposed to European Directive 98/79EK and also that its application in the case of AGET IRAKLIS, should not cancel the EU directive.[48] More specifically, the Greek law may place restrictions on the condition that the principle of the EU for the freedom of firms' establishment is not violated. The decision emphasizes that the Ministry of Labor has the power to prevent layoffs on the grounds of public interest **but the criteria are not clear**.[49] The Directive on collective dismissals may be inefficient because of the criteria used and can prevent the employer from doing them. Therefore it is necessary to have clear criteria. However it is desirable to achieve a balance between workers' protection and employment and freedom of employers as part of their business activities.[50] It remains to be seen how the decision will be evaluated by the institutions.

PBO,[51] has noted in the past, that governments' main concern is to resolve labor market pathologies, increase employment and establish institutions to promote both flexibility and workers' security. Regarding the effects of collective dismissals, a social project and various alternatives are required in order businesses and workers to survive in the new working conditions.

3.3 Public Administration: expecting important developments

During the last semester of 2016, the most important development on the legislative field concerning public administration was the law 4440/2016 on the mobility scheme in the public sector. PBO had expressed its views on this issue in its previous quarterly report, during the relevant bill's public consultation.[52] On 19.12.2016, the ministerial decision for its application was issued.

The same date, ministerial decree on the conduct of structured interviews for the selection of public sector's directors was issued, in view of the beginning of the selection of general directors, directors and heads of departments. Structured interviews have already been applied for many decades in the private sector and it is a valuable and crucial "tool" for the selection of

45 L.1264/1982.
46 Recommendations Expert Group for the Review of Greek Labor Market Institutions, 27/09/2016.
47 See. Naftemporiki, Efi Axtsioglou, A control mechanism of collective dismissals is needed, 12/23/2016, at http://www.naftemporiki.gr.
48 EU Court of Justice Decision of December 21, 2016, Luxembourg, In Case No C-201/15, (AGET, IRAKLIS)
49 Three criteria: 1. Interest of national economy, 2. Enterprise Status, 3. labor market conditions. Criteria 2 and 3 are unclear.
50 See. above Footnote.
51 See also the PBO Quarterly Report, July-September 2016, pp.16-18 & 36-47.
52 See Quarterly Report of PBO (July-September 2016, p. 26).

candidates for managerial posts in the public sector. Apparently, the implementation of this process will be beneficial for the public administration, provided that the principles of objectivity, transparency and meritocracy are applied.

The number of people registered in the Registry of Senior Officials of Public Administration has increased and currently stands at about 900 persons. However, selection according to this system has not started yet. The relevant procedures must begin as soon as possible with the issuance of the Presidential Decree for the duties and the qualifications of the officials who will be selected. Furthermore, on 22.12.2016 the ministerial decision (provided for in l. 4369/2016 on the evaluation of public employees)[53], on the format and the content of the public employees evaluation reports has been issued.

Another important development, which is also a country's obligation under the memorandum, is the creation on 4.11.2016 of a committee that will draft a bill to establish basic rules of organization and operation of the Independent Administrative Agencies; the task is to strengthen their independence and make their operation more efficient.

The Independent Administrative Authorities were initiated in Greece at the beginning of the 1990s when the Greek National Council for Radio and Television was created at first and later, the Supreme Council for the Selection of Public Employees and the Greek Ombudsman. Today there are five (5) constitutionally established[54] and another twenty four (24), which were created either by national or by EU law. They cover a broad range of fields ranging from human rights to whole sectors of the economy such as the energy or telecommunications. Although the reason for the creation of the Authorities varies from case to case, at the basis of their creation is the political decision that a) some issues must be solved by people with the necessary technical expertise in the field of each Authority, and b) the decision making procedures must not be affected by political motivations and influence.

Of course, an analytical and specialized reference to the issues of selecting the leadership of the Authorities, their competences and their operation is out of the scope of this report. However, at this stage, the PBO finds it useful to express certain thoughts, contributing to the ongoing public debate in light of the pending revision of their legal framework.

First, it must be noted that since their creation, the **governments have shown an ambivalent position towards the Independent Administrative Authorities**. On the one hand, they have created a large number of such Authorities assigning them a lot of power. On the other hand, they do not seem to have been accustomed to the idea that once an Authority is created, it must be left undisturbed to carry out its tasks. This contradiction had created several problems so far.

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53 Official Journal 33A΄/27.02.2016.

54 Hellenic Data Protection Authority (article 9A of the Constitution), Hellenic Authority for Communication Security and Privacy (article 103 par. 3 of the Constitution), Supreme Council for the Selection of Public Employees (article 103 par. 7 of the Constitution), Greek National Council for Radio and television (article 15 par. 2 of the Constitution) the Greek Ombudsman (article 103 par. 9 of the Constitution).

Once it is decided that an Independent Administrative Authority must be created with a task which normally belongs to the executive power, the State must provide the necessary framework which will ensure the Authority's independence. This independence necessarily includes the following elements:

i. Selection of persons with the necessary qualifications, regardless of political convictions. This is guaranteed to a considerable degree in the case of the 5 constitutionally established authorities because of the constitutional requirement that these persons will be selected by a majority of at least 4/5 of the Parliament's Speakers' Committee,[55] but it is not always secured in the case of the other Authorities. Thus, several certain solutions should be examined such as requiring a parliamentary majority of 3/5 or selecting the members of the Authorities by organs who are independent themselves, such as ASEP or the Authorities themselves.
ii. The term of the selected persons must be guaranteed (with the exception of members who commit serious crimes) so that these persons are not influenced in their judgment by the political impressions that their decisions or opinions will create.
iii. The members of the Authorities must have no other occupation during their term, provided of course that their salaries correspond to their status and qualifications. Parallel employment to the public or the private sector is against the independence of the Authorities.
iv. Oversight of the Authorities should belong to the legislative and not the executive power. Issues such as their annual budget and programming must be reviewed and approved by the relevant parliamentary committees and should not be decided by the relevant Minister from whom they should not be dependent. It would be useful to issue medium term programs of activities which will be updated each year.
v. Accordingly, parliamentary control of the Authorities should be addressed directly to them who should also respond directly to the relevant parliamentary organs. Addressing to a Minister questions concerning an Authority and letting the Minister respond to them is institutionally inappropriate.

3.4 Reforming an obsolete and inefficient welfare state.

The economic crisis has not only economic but also social impacts as strongly affects vulnerable groups while also has rendered ineffective the welfare system. A series of humanitarian measures already been taken by the government, in order to have access to basic goods and services those in need.[56] Boosting employment could contribute more to the citizens' welfare and particularly the long-term unemployed[57] who are experiencing poverty conditions (précarité) and deprivation. The role of active policies is necessary according to the third memorandum as well. The government has committed to implement active policies that link work and motivation of individuals[58] both for the long-term unemployed and those that are eligible

[55] See article 101A par. 2 of the Constitution and article 14 par. d of the Standing Orders of the Hellenic Parliament.

[56] Electricity, rent and food subsidies. Furthermore in 2014/2015 was implemented the GMI program in 13 regions covering the 5% of the total population and finally will apply for the whole country in 2017.

[57] According to the third memorandum the government should create jobs for 52.000 people.

[58] In the context of active employment policies, it is stated that 43.000 people will be covered.

for the minimum guaranteed income.[59] Until December 2016 the government has committed to create more jobs through wage subsidies and apprenticeship for about 90,000 participants. ***The availability of employment is the driving force not only for economic growth but also for the overall social welfare.***

On the other hand, the welfare state takes responsibility for needs such as employment, health, education, housing and social care. The welfare state is based on the principles of social justice and collective action designed with the main objective to achieve citizens' well-being[60] and the elimination- or the reduction- of social inequality.[61] The welfare state is required to play the role of social buffer. It is known that the Greek welfare state is a residual welfare state[62] and is based on the idea that the needs must be covered by the free-market mechanisms and the family.[63] The methods used by the residual welfare model, are of selective coverage. Another main feature of the operation of the Greek welfare state was the clientelistic system between the state and the citizen that played a key role in the previous years. ***Direct consequence of the above was that the welfare system could not respond effectively in reducing inequalities that still exist.***

The Greek welfare state, as the PBO has mentioned [64] needs reforming. The main feature of social benefits in Greece is the fragmentation in various categories which protects certain social groups and leaves out others (selectivity of social protection). Also, the practice of lump-sum payments, such as social welfare benefits, because of strict eligibility criteria did little to alleviate poverty and instead exacerbated the "gaps" in the social safety net. Entities that undertake the granting of benefits often do not have the qualifications to do that. For instance the benefits granting by OGA to families with many children, the employee family allowances from OAED and finally the subsidy of low employee contributions from IKA.[65] ***In short, the social protection system in Greece is complex, fragmented and without specific target.***

Already in 2013, the OECD emphasized the need to reform family benefits, the extension of unemployment benefits and the strengthening of active employment policies. The International Monetary Fund proposes the abolition of number of benefits and their replacement by the GMI.

According to the World Bank,[66] Greece spends more on social protection than the average for the rest of the EU and covers only formal sector workers. Expenditures basically are oriented to the pension pillar, with under 11% of overall social protection expenditures allocated to

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59 Supplemental Memorandum of Understanding, 16.06.2016, pp.19-20.

60 Quantitative and qualitative.

61 Olga Stasinopoulou, Welfare state, Historical evolution- Contemporary and theoretical approaches, Library of Social Science and Social Policy, Gutenberg, pp.23-26.

62 Classification of Social protection models with the criteria of state's intervention extent according to R. Titmuss (1990). The residual model, which is based on the philosophy of Laissez-faire (residual welfare state), the Institutional-redistributive (industrial-redistributive model) and the performance model (industrial achievement- performance model). See. Olga Stasinopoulou, Welfare state, Historical evolution- Contemporary and theoretical approaches, Library of Social Science and Social Policy, Gutenberg, pp.23-26.

63 It acts as a safety net for those groups experiencing problems of survival and its role is ancillary to that of the family.

64 See. PBO, INTERIM REPORT: "MINIMUM IMCOME SCHEMES IN THE EU AND GREECE: A COMPARATIVE ANALYSIS", October 2014, pp.25-26.

65 M. Matsaganis, social solidarity and contradictions, The role of minimum income in a modern social policy, Publication Kritiki, 2004 pp.84

66 Social Protection and Labor Global Practice The World Bank, Greece Social Welfare Review, Weathering the crisis: Reducing the gaps in social protection in Greece, Administrative Agreement of 14 December 2015, October 7, pp. 7., 2016.

non-contributory social welfare programs. However, no reduction in poverty rate was observed, which is not explained, because during the period 1995-2008 Greece was characterized by improvement of citizens' living standards due to the considerable economic growth. It can, however, be initially explained by the fragmented social system and secondly by the fact that the largest part of transfers is oriented to pensions.[67]

The report mentions that the consolidation of benefits, the implication of GMI and the rationalization of poorly designed policies, can increase the share of social welfare benefits from 18% to 54% for the poorest decile. As a result, the poverty headcount would fall by 2% and there would be an important reduction in the poverty gap. Greece, is the last European country to implement[68] GMI policies.[69] The rationalization of benefits will create fiscal space for the effective implementation of social solidarity Income started in July 2016. There are three main criteria:

1. The main goal of the programs should be those who are really in need, but proper recognition of the need is also required.
2. The provision of benefits should satisfy equitable and fair treatment of similar groups. For example, all people with disabilities should have the same access to benefits and services.
3. A few large programs designed in such a way to meet their objectives with transparency and efficiency. Any possibility of error and fraud should be reduced.

In Greece, pension coverage of people aged 65 is 87.8% but is lower than in the rest of the EU (94,8%) and the Eurozone (92,9%). Early retirees in Greece of people aged 50 to 59 is around 19% while in EE and in the rest of Eurozone is 10%. A 17% of GDP is spent on pensions pillar with the 9% of GDP concerning the deficit. [70]

The family benefits, the unified child benefit and the large family benefit have good targeting but there are still gaps in terms of coverage. The report of the World Bank suggests the consolidation of the mentioned benefits in order to meet the above criteria. They recommend 4 scenarios but they suggest scenario 4 because they think that it will save result in significant savings. In scenario 1 and 2 the amount varies depending on the number of children in the family. Obviously scenario 2 favors large families, while the scenarios 3 and 4 maintain a fixed monthly amount for each child (Table 7).

[67] INE/GSEE, policy Texts /1, The Paradox of Social Policy in Greece: Why the increase in expenditure on social protection didn't reduced poverty?, Ioannis Dafermos and Christos Papatheodorou, Economic and Social Observatory, July 2011, pp.1-5.

[68] In July 2016 began the delivery of social solidarity benefit. Since January 2017, the Social Solidarity Income will be implemented throughout the country (Article 235 of Law. 4389 / 2016_A'94).

[69] See. PBO, Interim Report 2014, pp.23-30.

[70] Social Protection and Labor Global Practice The World Bank, Greece Social Welfare Review, Weathering the crisis: Reducing the gaps in social protection in Greece, Administrative Agreement of 14 December 2015, October 7, 2016, pp.23.

Table 7: Unified Child Benefit, Amounts for the status Quo and for three reform scenarios.

Scenarios	Monthly benefit amount for first income tier
Status quo	EUR 40 per child.
Scenario 1	EUR 50 for the First child. EUR 60 for the Second child. EUR 80 for the third child. EUR 90 for each child and fourth child onwards.
Scenario 2	EUR 90 for first and second child. Third child and on-wards, EUR 90 each.
Scenario 3	EUR 70 per child.
Scenario 4	EUR 60 per child.
Source: *World Bank*	

To conclude, it is proposed to eliminate large family benefit and to remove the unified child benefit from families in the third income tier. Furthermore it is proposed to use the GMI equivalence scale to target the benefit based on family income so as to adjust the equivalized thresholds for tiers 1 and 2 to € 5.000 and € 10.000.[71] The result will be the simplification of family benefits by giving more attention to dependent children[72] who are more likely to live in poverty due to the economic crisis. In addition, families whose incomes are in upper deciles will not take the benefit. If the equivalized thresholds were adjusted, scenario 1 would be fiscally neutral, scenario 4 would generate savings of € 35 mn and the other two scenarios would increase expenditure by € 53 mn and € 60 mn respectively.

Moreover, in the report are presented recommendations for the elimination of tax expenditures to release fiscal space for the first phase of roll-out of the GMI. More specifically:[73]

- Eliminate medical expenses that potentially will increase up to € 86.8 mn the revenues that could be reallocated to the GMI with only a minimal negative impact potentially on those at the bottom of the distribution.
- Eliminate the 1.5% withholding tax credit, that disproportionately benefit those at the top of the distribution in relative and absolute terms. This elimination will have the benefit of around € 54.7 mn.
- Gradually increase the income tax rate for seafarers and crewmen to the standard rate. The beneficiaries of these special rates are in richest 20% of the gross market income distribution. The elimination will increase revenue by € 88.7 mn.
- Reducing diesel refunds for heating oil can increase revenue by € 64 mn.
- Increasing the excise rate on alcoholic beverages but at the same time take into consideration the potential losses that might occur for small producers.[74]
- Expanding the tax base.[75] By reducing the tax credit and expanding the tax base to a degree that is in line with the rest of the region. Likewise if there is a better targeted family benefit, this can lead to a more equitable, fiscally sustainable system. All the above eliminations can yield up to 17% of GDP.

71 Social Protection and Labor Global Practice The World Bank, Greece Social Welfare Review, Weathering the crisis: Reducing the gaps in social protection in Greece, Administrative Agreement of 14 December 2015, October 7, 2016, pp.61.

72 Specifically those aged 18 to 24.

73 Social Protection and Labor Global Practice The World Bank, Greece Social Welfare Review, Weathering the crisis: Reducing the gaps in social protection in Greece, Administrative Agreement of 14 December 2015, October 7, 2016, pp.77-78.

74 Producers of raki, ouzo and tsipouro.

75 The expansion of the tax base would reduce the tax rates and thus the tax burden.

As for disability benefits it is proposed to reform planning, management and evaluation of the disability benefit system. In Greece, the evaluation and the definition of disability is associated with "medical impairment" rather than with the ability to overcome the problem and the type of assistance needed. Instead the medical committees make the final decision relying on medical criteria. But the main problem is the insufficiency and the non-coverage of those in need.

Moreover, the World Bank proposes to abolish benefits related to holiday benefits for the unemployed, elderly and public sector pensioners. Camp programs and generally all social tourism programs and benefits for free transportation should be abolished.

The unemployment benefit for people over 20 years old and students that is provided without income criteria is considered to be a passive benefit. Beneficiaries are few and the administrative burden of OAED is increased. They recommend the consolidation of unemployment benefit into a larger program for the unemployed and to be associated with more active elements.[76] The rationalization of welfare benefits could save € 760 mn. But it is a difficult task because there will be a price for the most vulnerable social groups. The savings that will occur will be permanent[77] and according to the World Bank, they will not cover only 2017 but also the coming years.

Spending on social protection is not aimed only at mitigating the social problems but also contributing to economic growth.[78] The system's support to the weaker social groups is essentially an "investment" in the potential improvement of people's social life. In difficult economic situations reforms are needed to protect the weak. But necessary conditions are: strong institutions, cooperation between parties and the government to promote the reforms, training employees in public services and reducing bureaucracy. In addition, it is essential to computerize and register the beneficiaries. It should be realized that social protection is an important policy tool.

3.5 Greece continues to lag behind in matters of Social justice.

Greece ranks as the worst- performing country in terms of Social Justice in comparison with all the 28 EU member states in all six dimensions[79] that compose the social justice Index (Graph 5). From Table 8, we see that in relation with the previous two years there is no significant positive change in the position of Greece.

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76 Social Protection and Labor Global Practice The World Bank, Greece Social Welfare Review, Weathering the crisis: Reducing the gaps in social protection in Greece, Administrative Agreement of 14 December 2015, October 7, 2016, pp.35.

77 Greek Republic, Ministry of Finance, Draft State Budget 2017, October 2016, pp. 35

78 Ioannis Dafermos, Christos Papatheodorou, The contribution of social protection to economic growth, Economic and Social Observatory, Social policy research unit, poverty and inequality, Studies 26 December 2013.

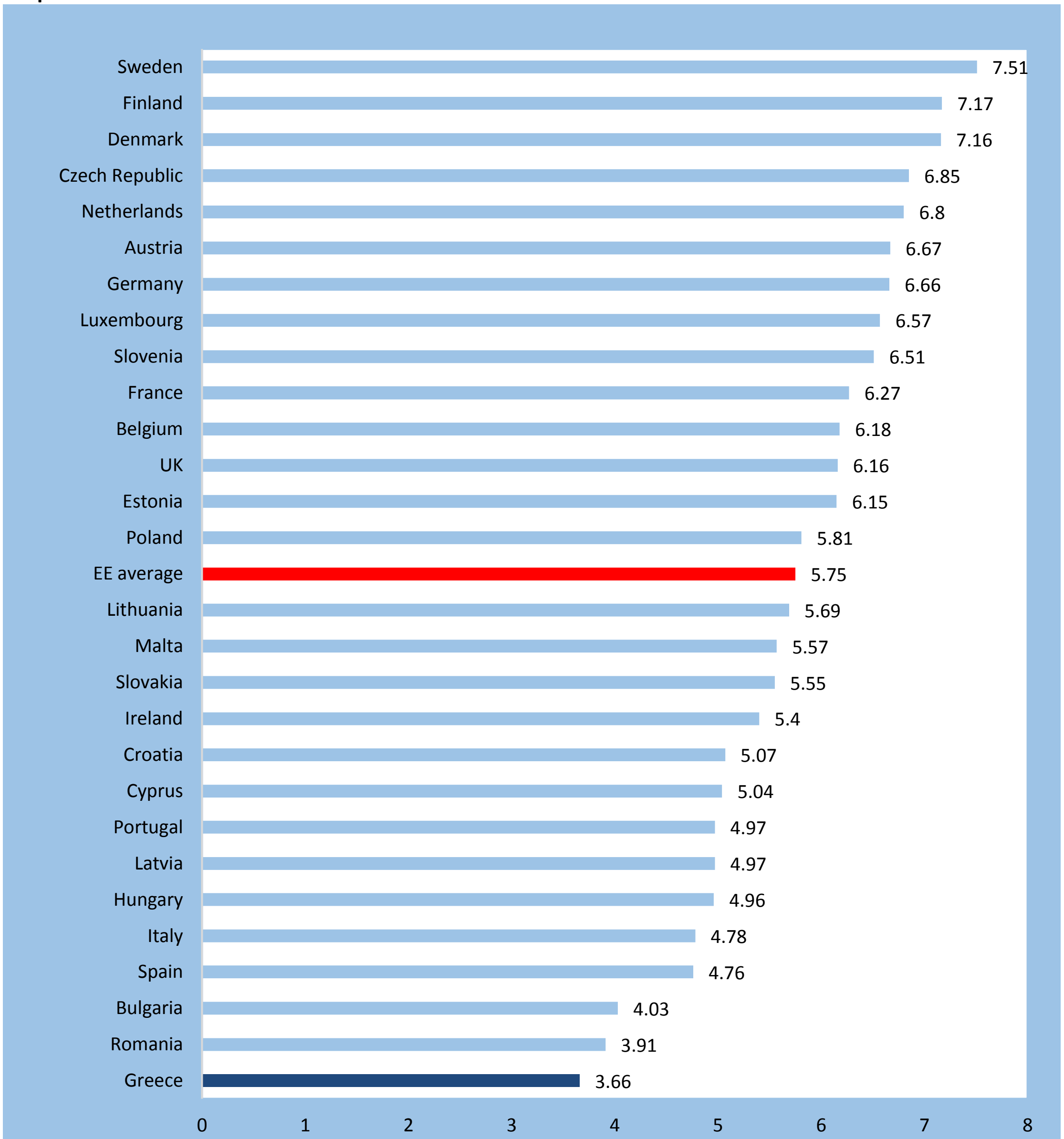
79 Poverty prevention, Intergenerational justice, Health, Social cohesion and non- discrimination, **Labor** market access, Equitable education.

Table 8 Greece's ranking on the index of social justice among the 28 countries of the European Union. Comparison of ranking positions for the years 2014, 2015, 2016.

Dimensions of Social Justice Index	2014	2015	2016
Poverty prevention	25th	26th	26th
Equitable education	28th	25th	24th
Labor market access	28th	28th	28th
Social cohesion and non- discrimination	28th	28th	24th
Health	24th	24th	26th
Intergenerational justice	28th	28th	28th
Source: *Bertelsmann Stifttung*			

In particular, Greece comes in place 28 with a score of 3.66, when the EU average for the social justice index is 5.75 (Graph 5).

Graph 5 EU Social Justice Index 2016.



Source: *Bertelsmann stiftung.*

Greece is the worst performing country in terms of ***labor market access and in terms of intergenerational justice.*** Since 2015 Greece had the lowest proportion of workers with only 50.8% being employed.[80] The number of unemployed is still more than 15 percentage points higher than it was in 2008 and far higher than EU average. The share of the long-term unemployment remains high (18.3%) and the long-term unemployed are at greater risk of poverty and unemployment. 83.3% of Greek people working in temporary employment could not find a permanent placement. Moreover, young people seem to face more uncertainty for their working future.

Youth unemployment rate has doubled since 2008, to 49.8%. Furthermore, Greece has the second highest NEET rate. This, in the long term can have negative consequences for both the economy and the social cohesion. Nowadays, youth unemployment is the main factor of poverty incidence. Young people are the main driver for development and therefore government's main concerns should be: young people's training, better link between education and labor market and finally reducing the percentage of young people leaving school. In addition, the combination of work and family life should not be ignored. Furthermore, it is important to pay attention to labor mobility,[81] which can contribute to efficient distribution.

Apart from young people, special treatment is needed for women, migrants and children. We can say that, ***specific social groups*** are affected more by the deep economic crisis**.** In Greece, the risk of poverty and social exclusion is 35.7%. The percentage for children stands at 37.8% and for the people over 65 is 22.8%.[82] We should note that 25.7% of children in Greece are facing severe material deprivation.[83] Namely, before the year 2011 a high level of deprivation experienced by single[84] and extended families. However, the impact of the recession in the child welfare will be evident in the coming years. With the existing data, appears the need to strengthen social investment.[85] In the sense of social investment,[86] is implied the development of children's knowledge in order to cope with the future risks and challenges.[87]

In terms ***of poverty*** Greece is at place 26. The social effects of the economic crisis made it clear that policy has been rather ineffective so far.[88] Predominantly the burden is borne by the Greek family and voluntary organizations. But it is uncertain how long they can provide assistance when the remaining resources are reduced due to successive cuts and raising taxes.

80 Daniel Schraad-Tischler and Christof Schiller, Social Justice in the EU-Index Report 2016, Social Inclusion Monitor Europe, Bertelsmann Stiftung, pp.34-46.

81 Already by 2013, Greece in the context of memorandum obligations upon to apply the mobility of human resources (mainly in the public sector). The mobility can be professional/inter-branch, the same branch/sectoral and geographical. In no way is considered as personal cleanup tool but a tool of labor market support and development of human resources.

82 Daniel Schraad-Tischler and Christof Schiller, Social Justice in the EU-Index Report 2016, Social Inclusion Monitor Europe, Bertelsmann Stiftung**,** pp.18-26.

83 The level of material deprivation essentially reflects the economic weakness to acquire goods needed for a decent life. Severe material deprivation is defined as the absence of four of the nine commodities (electricity, water, heating, telephone, TV, car, meat, rent and holidays).

84 The situation of children in Greece 2016, Children at risk, UNICEF Greek National Committee pp.28-37.

85 The concept of social investment refers to children and families and it is at the heart of political debate in Europe.

86 Esping-Andersen, Gøsta 2005 Children in the welfare state. A social investment approach (Barcelona: Universitat Pompeu Fabra).

87 The situation of children in Greece 2016, Children at risk, UNICEF Greek National Committee pp.28.

88 Sotiropoulos, Dimitris A., Kevin Featherstone and Roy Karadag (2016): Country Report Greece, Sustainable Governance Indicators 2016. Available at: www.sgi-network.org.

Greece also ranks at the bottom in terms of intergenerational justice. Geographically is one of the countries with the most unfavorable demographics and with the highest public debt (178.4%). The fiscal burdens don't refer only to today's generation but also to the future generations. Investment in research and development that are crucial for economic growth is only 0.8% of GDP. From the above it is realized that it is important to reduce public debt while the policies should be more equally distributed between the young and the elderly. Simulations of the redistributive effects among individuals and generations would be useful as well.[89]

As for ***social cohesion and nondiscrimination,***[90] Greece has a score of 4.44 for 2016 (in 2008 it was 4.57). The economic crisis and the inequalities in the Greek society negatively affect social cohesion. The recent refugee crisis intensified the negative effects and this contributed to the fact that Greece seemed to be unprepared for such a development. Having a properly designed model for the refugee crisis would result in huge benefits in fields, such as social security and demography. Moreover, the existence of effective legislation could contribute to maintaining social cohesion. The reconstruction of the Greek institutional framework is a prerequisite for the return to growth.

Also, Greece's performance in ***education*** is particularly disappointing in terms of basic skills and participation in adult learning and training processes. The most important problems of Greek education is the lack of teaching staff, efficiency and equity in education and the lack of financing. More specifically, Greece on the financing of early childhood education is ranked in 27th place (0.1% of GDP). Another important issue is the formation of a stable modern legislative framework that applies to all levels of education and addresses the issues of tuition, transparency, social accountability and social justice.[91]

Finally, the ***national health system*** has been significantly affected by the economic crisis. Main features of the current system are, the large increase in mortality rates, staff shortages and a lack of basic equipment. The health expenditure during the crisis suffered significant cuts. Specifically, in 2012, the reduction in costs was around 1% of GDP[92] while in 2013 the costs were estimated at 8.65% of GDP when the EU average was 9.8%.[93] The health system faces a severe shortage of financing with the percentage of public health expenditure[94] to be the worst in comparison with other developed countries. Equally important is the reduction of total public pharmaceutical expenditure, which in 2011 remains lower than the EU average. ***However, the proportion of private health spending is still among the highest in the OECD.*** Note that the annual family income has been fivefold burdened by health costs and in particular among low income groups.[95]

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89 Platon Tinios, Report to the Task Force for Greece, The Greek pension system: Towards a social contract, May 2015, pp.1-10.

90 Daniel Schraad-Tischler and Christof Schiller, Social Justice in the EU-Index Report 2016, Social Inclusion Monitor Europe, Bertelsmann Stiftung, pp.46-56.

91 European Commission, Monitoring Report Education and training 2016 for Greece, November 2016.

92 Over € 2 bn.

93 Research & Analysis Agency diaNEOsis, The Health of Greeks in crisis, a mapping of the state of Greeks health and the health structures of the country's, Institute of Social and Preventive Medicine, March 2016, pp.7-8.

94 For the year 2015, public expenditure on health does not exceed 5% of GDP.

95 Research & Analysis Agency diaNEOsis, The Health of Greeks in crisis, a mapping of the state of Greeks health and the health structures of the country's', Institute of Social and Preventive Medicine, March 2016, pp.8.

It is obvious that the economic, political and social forces are affecting and determining the living and death conditions. The performance of our country in social indicators continues to be disappointing. High-risk groups such as the unemployed, single parent households, non-economically active, women, people with low educational level, immigrants and children are the main victims of the crisis and fiscal adjustment.[96] It is obvious that we need to redefine and strengthen social policies and improve the targeting and effectiveness of social expenditures.

[96] Theodore M. Mitrakos, Fiscal Adjustment: Distributional effects of austerity, Fiscal Adjustment: How fair is the distribution of the burden? Parliamentary Budget Office, Athens 2014, pp.45-53.

4 SPENDING REVIEWS

4.1 The spending reviews in the agenda of EU[97]

The Eurogroup has at his meeting of 16 September 2016 decided to improve the quality of public expenditure in the Euro Area through the use of the spending reviews basically in the fields of growth and job creation.

The use of spending reviews is necessary to support fiscal responsibility and economic growth through the public spending. For that reason, the exchange of «**good practices**» among the member-states is a positive step along with the Commission's proposals to set common principles which will dominate the Spending Review. The implementation of spending reviews should take into consideration the specific characteristics of each Member-State.

The Commission's general conclusion is that the spending reviews are useful for:

- To improve the quality of public finances.
- To complement the support of financial responsibility through overview over the priorities in public spending.
- To make the State Budget more growth friendly.
- They are particularly important in the Euro Area (in terms of convergence of policies in the EU).
- Contribute to the restoration of taxpayer's confidence regarding the efficiency of taxes in a period with high public debt and low economic growth.

As regards the common principles, the Eurogroup based on the experience of other Member States argues that the application of spending reviews must have the following elements[98]:

- Strong and sustained political commitment at high national level, throughout the project, and implementing their findings into meaningful reforms.
- The design and implementation of spending reviews should follow best practices that include elements like:
  - Clear strategic mandate specifying the objectives, the scope and a center of coordination,
  - The use of pilot programs to build expertise,
  - The provision of adequate resources and access to data,
  - The use of guidelines for consistency in producing diagnosis, reform options and implementation roadmap,
  - The use of fact–based analysis linking the spending across budget and administrative structures to policy outcomes.
- Monitoring and communication to the public on the progress and outcomes of reviews.
- Spending reviews should be subject to independent ex-post evaluation to learn lessons for future reviews.

[97] Eurogroup The President, ecfin.cef.cpe(2016)5654465, Brussels, 16 September 2016
[98] Annex I (Bratislava, 09/09/2016) in Eurogroup, The President, ecfin.cef.cpe(2016)5654465, Brussels, 16 September 2016

- The conclusions of a spending review should be consistent with annual and multiannual budget planning.

4.2 International experience

Based on proposals of international organizations like OECD, the main characteristics of spending reviews are[99]:

- Scope: Discretionary or mandatory expenditures – Sectors reviewed –Level of Government.
- Level of review: All of government – Sector programs –Organizations –Horizontal policies.
- Time frame / Periodicity: Fixed period or rolling basis
- Resulting saving options: In terms of staff or funding, in absolute or percentage terms.

All approaches of international organizations and the EU aimed at improving fiscal discipline and efficient allocation of expenditure, where evaluation mechanisms exist in outputs level and rarely in outcomes level. There is no one-size fits-all methodology for spending reviews[100], as each country has its own characteristics of public finances, in organization environment, in financing of the economy (high debt as percentage of GDP, small or large public sector, different strategic and political priorities, or the benefits of financial assistance from other countries).

4.3 Good practices of spending reviews

Slovenia[101]

Slovenia's fragile fiscal situation which stems from the upward trend of public debt and the increase in public spending by 5% as a percentage of GDP by 2008 threaten its financial stability in the long-term. Fiscal consolidation measures so far have largely concentrated on one-off measures and across the board spending of the budget.

Therefore Slovenia implemented spending reviews in the areas of Health, Education and Social Welfare in order to save € 200 mn every year. In the health sector Slovenia had the support of the World Health Organization. In Social Welfare sector the fiscal problem is big due to the rapidly ageing population.

The space for further across the board horizontal cuts, such as continuing indexation freezes and hiring freezes is limited in an environment where the general population has already witnessed five years of austerity measures. Targeted measures can better address inefficiencies and be used to introduce necessary structural reforms.

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99 OECD, Better Policies for Better Lives, "Proposals for Analysis of Spending Reviews", Edwin Lau, Budgeting & Public Expenditures Division OECD, 7th Annual meeting of SBO Network on Performance & Results 09-10 November 2011.

100 European Economy, Economic Papers 525/July 2014, "Public Spending Reviews: design, conduct, implementation", Caroline Vandierendonck, p.5, Brussels 2014

101 IMF, Fiscal Affairs Department, Republic of Slovenia "Technical Assistance Report -Establishing a Spending Review Process" by Brian Olden, Jasson Harris, Amanda Sayegh, Duncan Last, and Chris Uregian, IMF Washington, D.C., June 2015

Identifying potential areas where spending can be rationalized requires a structured spending review process.

Key objectives of the spending review process is to provide higher quality measures which stem from continuous measurements of the largest spending areas.

The objectives of spending reviews are three:

- Assist the government's medium-term fiscal consolidation task by identifying a list of high quality potential savings measures.
- Improve the efficient allocation of expenditure by identifying potential shifts of them from lower priority sectors both within and across portfolios.
- Improve value for money, by identifying areas of inefficient spending, where similar outcomes can be better achieved with reduced inputs.

The identification of saving options is in the heart of spending reviews, as these will be necessary to offset expenditure pressures, and the creation of fiscal space for new policies. In order to identify these options, the spending reviews should evaluate existing projects based on the following criteria:

- How well the objectives of the program are aligned with the government' policy priorities?
- Available evidence on the performance of the program, including how well the program meets its policy objectives and its cost-effectiveness.
- When there is a scope to better meet the government's policy objectives?

The spending reviews should identify a range of saving options in order to feed into a ministerial decision making process. These should include medium term financial impact, rationalization of policies, affected groups.

The spending reviews should identify high priority spending areas and work up some new offsetting policy where a part of the savings could be redirected. This will have the benefit of improving the allocation's efficiency, as well as helping to provide further policy justification for saving options by redirecting spending towards socially disadvantaged groups that may otherwise have been impacted by the overall savings.

The spending review may need to focus on assessing the largest programs, or those that are identified as most promising. The team of IMF undertook a high level international benchmarking assessment using economic and functional spending data drawn from Eurostat's Government statistics database.

The proposals of the IMF team focused not only on the finding of the comparative analysis of the level of expenditure per sector (education) but also to structural changes in the area of policies, for example strengthening of primary education personnel and fewer staff in secondary education, establishing a working group in education and social welfare, in addition to the existing in the health sector to undertake program evaluations, identifying a list of savings options and high priority spending alternatives within their portfolios. They propose also a range of structural reforms in the above mentioned areas.

Establishing the spending review process requires:

- The objectives of the review should be established at the outset.
- Clear saving targets are provided to review teams.
- A medium-term perspective has been adopted.
- A decision making committee has been put in place to arbitrate disputes.
- The review has been integrated into the annual budget processes.

What should be avoided in designing a spending review program based on the experience of Slovenia

- Do not set specific Ministry spending ceilings and saving targets at the start of the process even if they are indicative. The Ministry of Finance should set the framework of the review by setting the spending ceilings and associated saving targets (baseline scenario) by the line ministry which is consistent with the aggregate General Government spending targets. Without specific spending ceilings the Working Groups will likely spend most of their time discussing and at the end the solution will be the horizontal spending cuts. Line ministries always choose the time schedule which suits them to move on for their spending reviews and the following spending cuts.
- Allowing line ministry officials to use Working Group discussions to re-open their ministry's targets.
- While ministries tend to suggest measures that require little adjustment, the Ministry of Finance should seek to counter-propose deeper reforms, based on international practices in countries with similar institutions, living standards and demographics.
- The entities supervised by the ministries and will undertake actions to make savings should be "moderately" quantified as there will be several delays in their implementation. For that reason, their commitment should be part of their annual budget. Let there be a provision for compensatory financial interventions.

In the spending reviews process it is important to set from the beginning a strong agreement on the objective, if for example the target is the establishment of a permanent review mechanism for expenditure reprioritization or for an overall reduction. According to the IMF proposals, in Canada the strategy of the Spending Review process required each agency to present saving options of at least 5% by year three from their lowest-priority and worst-performing spending program.

Respectively in France the Révision Générale des Politques Publiques (RGPP)[102] during 2010-2011 set a target for a 10 % reduction in non-salary administration costs by year three and institutionalized the policy of non-replacement of one in two retiring civil servants.[103]In the Netherlands the Comprehensive Spending Review required each review team to develop saving options capable of delivering at least a 20% reduction, over four years.

[102] A program started in 2005 was extended in 2007 and 2010 with new interventions for the revision of public policies implemented in France to improve the effectiveness and efficiency of public administration and rationalization of expenditure savings and achieving financial stability (Direction de Information légale et administrative:"Révision générale des politiques publiques : un "coup d'accélérateur" pour la réforme de l'Etat". P.1.

[103] OECD, Public Governance and Territorial Development Directorate Public Governance Committee, Working Party of Senior Budget Officials, 3th Annual Meeting of OECD Senior Budget Officials "Spending Reviews", OECD Conference Centre, Paris, 3-4 June 2013, p.9.

Also in order not to lose the opportunity of the reviews and of course their central objective, the working group from each entity participating in the program should provide a minimum amount of expenditure savings' options or allow them this percentage to be used on other priorities .

Many of the targets for spending options will not go ahead, so the menu for each spending review should be considerably larger than the final saving target required for fiscal consolidation. As a guide, in Greece, around half of the options identified by reviews were either not adopted or were rejected by the Council of State.[104]

The size of the savings measures should be clearly higher than the target of fiscal consolidation and should take into account the required medium-term savings rather than focus on a single year.

The spending review that is currently being established in Slovenia will operate in two levels. The first in technical level and the second in political level to decide which of the saving options should be implemented.

In the working groups could participate representatives of the Ministry of Finance, the line ministries responsible for the spending areas and external experts. Representatives of the office of the Prime Minister could also participate to add additional weight to the process. The working group will be chaired by a senior official from the budget Directorate in the Ministry of Finance. The Ministry of Finance provides the overall guidance to the working groups on the timetable, the outputs for the review, the setting of the review criteria and the development of templates for policy submissions.

In final decisions any final proposal made by the coordinating body should include the following information: [105]

- The fiscal impact for the Budget and three forward years, with costing to be made using consistent methodologies and assumptions across programs.
- The public policy rationale for the proposal.
- The impact of the policy proposal on affected groups (social and economic consequences).
- The legislative requirements for the implementation of spending review process, and the process for consultation if required.

When one of the review could have maximum impact, the absolute benefit increases when it becomes a permanent part of the annual budget of line ministries.[106]

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104 IMF, Fiscal Affairs Department, Republic of Slovenia "Technical Assistance Report -Establishing a Spending Review Process" by Brian Olden, Jasson Harris, Amanda Sayegh, Duncan Last, and Chris Uregian, IMF Washington, D.C., June 2015, p.24.

105 IMF, Fiscal Affairs Department, Republic of Slovenia "Technical Assistance Report -Establishing a Spending Review Process" by Brian Olden, Jasson Harris, Amanda Sayegh, Duncan Last, and Chris Uregian, IMF Washington, D.C., June 2015, p.29.

106 European Economy, Economic Papers 525/july 2014, "Public Spending Reviews: design, conduct, implementation", Caroline Vandierendonck, p.5, Brussels 2014,p19.

Ireland

In Ireland, international standards appear in the design and implementation of spending reviews. The choice of review models has not been limited to regular functional, effective, bottom-up, top-down, joint review, hybrid review,[107] but their primary focus was to establish the measures that will help to reduce expenditures and the periodical integration of the expenditure reviews in the annual budget process.

Three comprehensive reviews have been made. In 2009 the consolidation path defined a € 3 bn reduction for the years 2010 and 2011 in current spending, as well as further € 1.75 bn in capital. The special Group identified € 5.3 bn savings but they emphasized that these proposals did not represent an exhaustive list of available policy options.

Under the EU/IMF Program of Financial Assistance and the Excessive Deficit Procedure, there was a medium-term expenditure framework (MTEF) created and multi-annual Ministerial ceilings in their expenditures were included.

The 2014 Comprehensive Expenditure Report was the first Irish spending review to ask spending departments to identify a certain volume of savings 5% of the expenditure ceiling for 2015.[108]

The original aim of setting the ceiling, was to give the Government the necessary time to achieve its immediate fiscal targets and potentially allow it to create fiscal space for new expenditure proposals. Given the high growth rate of the economy, the expenditure cuts were not made, but the spending review will continue to support better policy choices by broadening the Government's toolkit within the budgetary process.

Netherlands

The government of Netherlands made a "Comprehensive Expenditure Review" in 2010. The Review examined 20 policy topics, and each topic was carried out by a working group. In the working groups participated representatives of the Ministry of Finance (MOF), the Prime Minister's Office, ministries and external experts. They had technical assistance from the MOF, and they were chaired by senior officials from the ministries under review. Uniform terms of reference establishing the guidelines and procedures for the review were developed by the MOF and agreed by the Cabinet.

A clear saving objective was specified at the outset, which required each working group to develop options capable of delivering at least **20%** reduction in spending or tax expenditures in the area under review, over a four- year period.

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[107] IGEES (Irish government economic& Evaluation Service), Department of Public Expenditure and Reform, Staff Papers 2016:"Spending Reviews in Ireland:Lessons for the Future", By John Howlin and Fiachra Kennedy, October 2016 p.11.

[108] Most states which implemented spending reviews followed this approach for all ministries and all programs in the budget-planning framework and implementation of their budget, in OECD, Public Governance and Territorial Development Directorate Public Governance Committee, Working Party of Senior Budget Officials, 3th Annual Meeting of OECD Senior Budget Officials "Spending Reviews", OECD Conference Centre, Paris, 3-4 June 2013, p.8,9.

Working groups were responsible for generating a menu of savings options sufficient to meet the savings targets. There was no right of veto on any policy issue being considered. The list of savings' options were provided to the Cabinet which was responsible for taking the final decisions. A significant proportion of the saving measures proposed by the reviews has been incorporated into the budget.

4.4 The Spending Reviews Pilot Program in Greece

The topic of the spending review started to be implemented in Greece with the establishment and the appointment of the Coordination Committee for the expenditure review.[109] It was preceded by the contact of officials of the Ministry of Finance with the British Treasury and the Dutch Ministry of Finance to provide technical assistance. In the pilot program participated the Ministry of Finance, the Ministry of Development, the Ministry of Tourism and the Ministry of Culture and Sports.

The primary aim of the project is in addition to the coordination of working groups of the reviewed line ministries, the collection and evaluation of the proposed savings policies, creating fiscal space for new policies, analyzing elements of the budgets from 2013 onwards. Reducing the tax burden on individuals and companies and creating indicators to monitor the effectiveness of public expenditures and the strengthening from 2018 onwards the Minimum Guaranteed Income.

The project is pilot and coordinator of the project and the steering committee is a senior official of the General Accounting Office in the Ministry of Finance. In the working group participated members from the General Accounting Office, the three line ministries, the Prime Minister's Office and the Council of Economic Experts[110]. The staffing fulfills international standards recommended by international organizations and followed by other countries in the introduction of spending reviews.

<u>The progress of the project</u>

The progress of the project according to the evidence provided by officials of the line Ministries (Ministry of Finance, the Ministry of Development, the Ministry of Tourism and the Ministry of Culture and Sports) to the Parliamentary Budget Office is satisfactory for the following reasons:

- This is a positive initiative which should have been started many years ago in Greece, taking actions in two levels, the first is the rationalization of public expenditures and the second is the fiscal reflection of the management of all actions of the General Government.
- It creates conditions for the development of a system to connect expenditures with actions and perhaps in the future to connect expenditures with outcomes.

[109] Decision 2/61561/0004/25.7.2016 του Secretary General of Fiscal Policy Fragiskou Koutendaki.
[110] CEE, Council of Economy Experts in Ministry of Finance

- Reinforces efficiency putting fiscal responsibility in the center of decisions.
- Quantifies administrative action figures and economic data and their classification.

The options for the working groups are limited in scenarios for spending cuts for the year 2018 and onwards. All the scenarios of spending cuts should not affect the wage bill. But the problem could be the size of the final savings for 2018, so that actually could be funded the Minimum Guaranteed Income from 2018 onwards.

As a part of these process the Ministry of Development sent questionnaires to public bodies to determine a rate of 6% of their public expenditures to reach savings for 2018 annual budget excluding the wage bill. The reviewed public bodies responded more or less positively after internal consultation. A positive aspect of the whole project is that all participated public entities were in a process of self-evaluation of the public money management which finances their operation and work. Deviation of +/- 3 percentage points is expected for the year 2019 and 2020, but in general the objective of savings will be achieved. A similar positive trend existed also in the Ministry of Tourism and Sport, where the selective data are sufficient in management, and it' s waiting on the classification and evaluation from the reviewed line ministry.

Maybe in the next step of the project the reviewed public entities should focus on the qualitative characteristics of expenditures and their effectiveness based on measurable targets and their indicators and probably their integration in programs/actions to be associated with their outcomes. We are waiting for the quantification of savings from the three ministries and the continuation of the pilot program implementation to all bodies of general government. International experience as presented by the study shows that in Greece several interventions are necessary to display specific items in the scope of the analysis and evaluation of public expenditure, so in addition to the creation of fiscal space for new policies with multiplier characteristics for society and economy, public expenditure and their disbursement have to meet mostly the principles of performance based budgeting.

5 PUBLIC DEBT

5.1 Short-term measures

In early December 2016, the Eurogroup announced the short-term relief measures for the Greek debt which were based on ESM proposals. These measures – in accordance with the 25 May 2016 agreement – are:

a) Smoothing Greece's repayment profile for EFSF loans (to 32.5 years)
b) Reducing interest rate risk. Three schemes are included:
    - bond exchange (floating notes are exchanged with fix interest rate notes and their maturity is extended)
    - ESM swap arrangements (thus mitigating the risk of higher market rates) and
    - matched funding for future disbursements to Greece under the current programme
c) Waiving the step-up interest rate margin for 2017

Based on ESM estimates, these measures could **potentially** reduce Greece's debt-to-GDP ratio by about 20% till 2060 (respectively the GFN could be reduced by 5%) without incurring any cost for the other member states. Out of the proposed measures, in terms of reducing the debt burden, the bond exchange will have the biggest impact (**Table 9** and **Table 10**).

Table 9 Impact of short-term relief measures on Debt to GDP ratios under baseline scenario

	2016	2017	2018	2019	2020	2022	2030	2040	2050	2060
1. Smoothening the EFSF repayment profile under the current WAM	0	0	0	0	0	0	-0.4	-1	-2.4	-3.6
2a. Bond exchange (floating notes are exchanged with fix interest rate notes), with BtB extension	0	0	0.1	0.2	0.2	0.2	-1.2	-3.7	-5.7	-7.1
2b. ESM swap arrangements	0	0	0.1	0.2	0.3	0.4	-0.4	-2.9	-5.1	-6.9
2c.Split on the pool with match funding	0	0	0	0	0	0	0	-0.4	-1.1	-1.3
3.Waiver of the step-up interest rate margin (Debt buy-back),2017	0	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.2	-0.3
Second Round effect on market rates	0	0	0.1	0	0	-0.1	-0.4	-1	-1.8	-2.6
Source: *European Stability Mechanism (Draft notes)*										

These measures, rather than having an immediate impact on the Greek debt burden, offer relief in the long term. Once more, resolving the Greek debt issue is postponed by debtors for the future, when their domestic political climate will be more suitable; on the other hand Greece's economy remains trapped. However, as the time horizon is extremely long and conditions are uncertain even the expected benefits may not be realized. ESM possible scenarios for the Greek debt sustainability clearly depict this uncertainty: only in the favorable scenario does the Greek debt-to-GDP ratio decreases to 62.6% in 2060 (in the baseline scenario debt-to-GDP amounts to 104.9% in 2060). On the other hand, according to the unfavorable and negative scenarios (lower growth rates, higher interest rates and reduced privatization revenues) **debt-to-GDP rises to 183.8% and to 258.3% respectively.** Moreover, in medium and long-term level, the necessity for further debt relief becomes evident from the GFN forecasts. GFN remain below the defined threshold (15% of the GDP till 2040 and below 20% thereafter) only in the favorable scenario (the respected GFN in the baseline, unfavorable and negative scenarios are 24.3%, 43.5% and 62.8%).[111] However, we should bear in mind two major facts: first, throughout the present Greek economic crisis favorable scenarios have hardly been confirmed, while negative revisions are frequent. Secondly, ESM scenarios assume an interest rate for Greece of more than 5% from 2019. However, as the PBO has underlined in previous report,[112] **such increased borrowing cost requires – just for interest payments, so as not to create new debt – extremely large primary surpluses, which constitutes an unachievable target.**

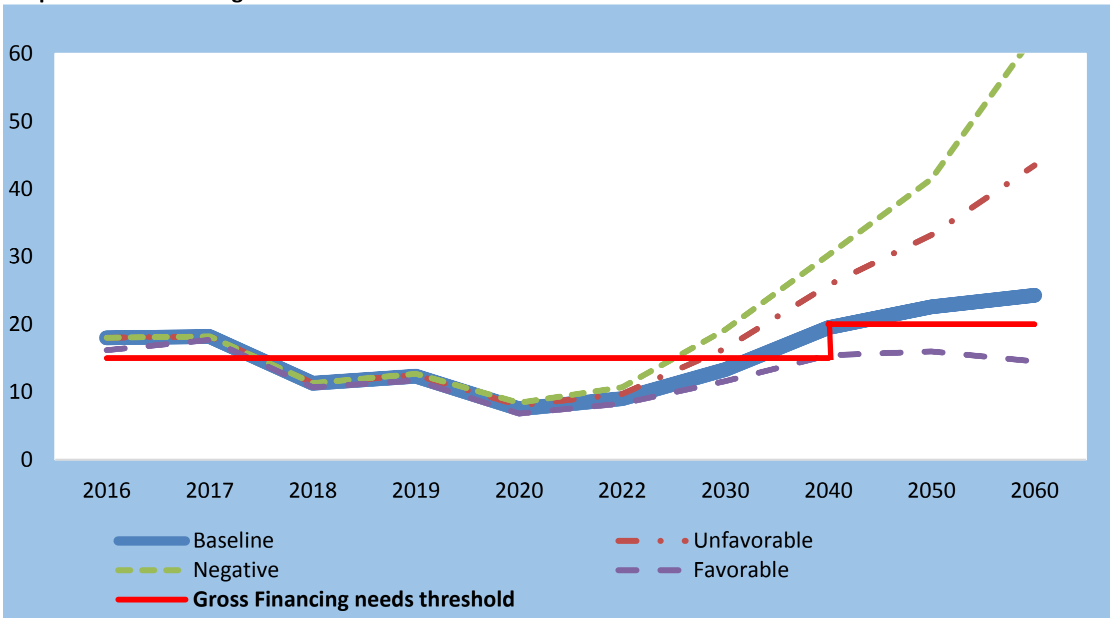
Table 10 Impact of short-term relief measures on Debt to GDP ratios under baseline scenario

	2016	2017	2018	2019	2020	2022	2030	2040	2050	2060
1. Smoothening the EFSF repayment profile under the current WAM	0	0	0	0	0	0	-0.1	-1.3	-0.8	-0.8
2a. Bond exchange (floating notes are exchanged with fix interest rate notes), with BtB extension	0	0	0	0	0	0	-0.4	-0.9	-1.2	-1.6
2b. ESM swap arrangements	0	0	0.1	0.1	0.1	0.1	-0.2	-0.7	-1.2	-1.5
2c. Split on the pool with match funding	0	0	0	0	0	0	0	-0.3	-0.3	-0.3
3. Waiver of the step-up interest rate margin (Debt buy-back),2017	0	-0.1	0	0	0	0	0	0	0	-0.1
Second Round effect on market rates	0	0	0	0	0	-0.1	-0.1	-0.3	-0.4	-0.6
Source: *European Stability Mechanism (Draft notes)*										

Overall, the PBO argues that the proposed short-term measures, while being in the right path, do not provide a terminal solution for Greece's huge debt burden; neither do they address the main problems of the Greek economy (uncertainty, lack of funding etc.) which still remains in a "debt trap".

111 ESM (Draft notes, November 2016)
112 PBO, Quarterly Report, April – June 2016, pp.54-55

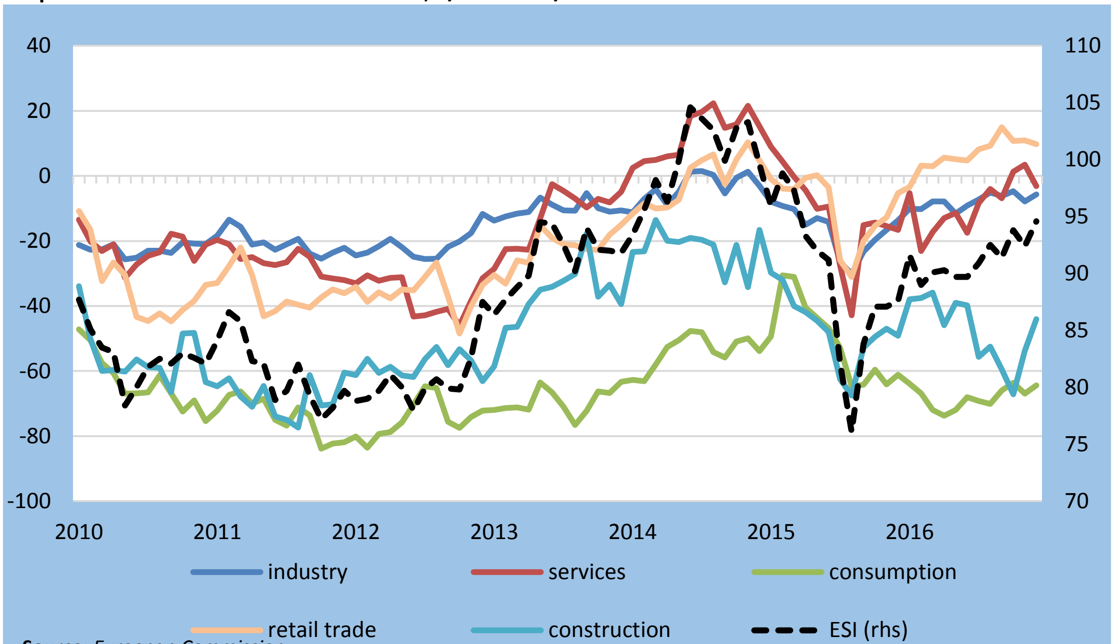
Graph 6 Gross Financing needs as % of GDP



Source: *European Stability Mechanism (Draft notes)*

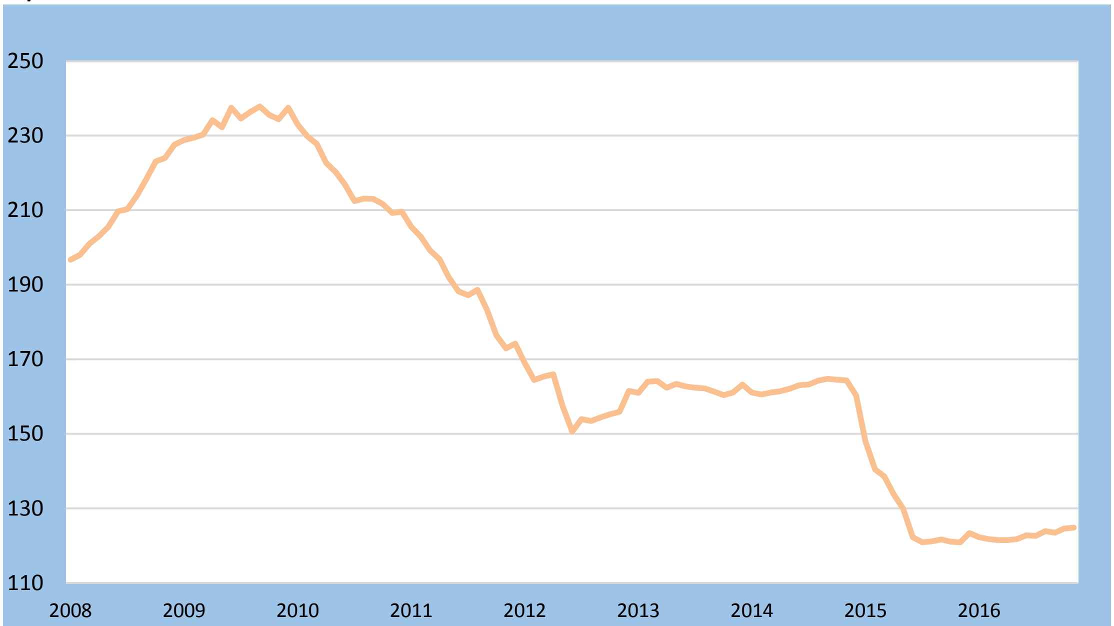
ANNEX

Graph 7 The evolution of the ESI in Greece, 1/2010 – 12/2016.



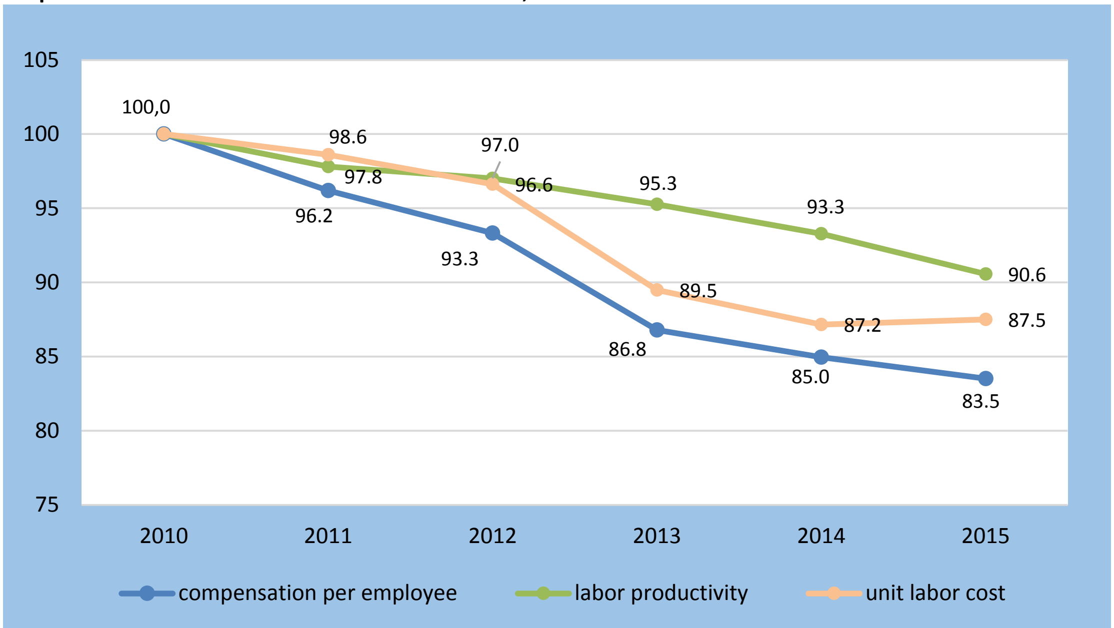
Source: *Euroepan Commission*

Graph 8 Evolution of banking deposits (€ bn) of Households & Corporations in Greece, monthly data, 1/2008 – 11/2016.



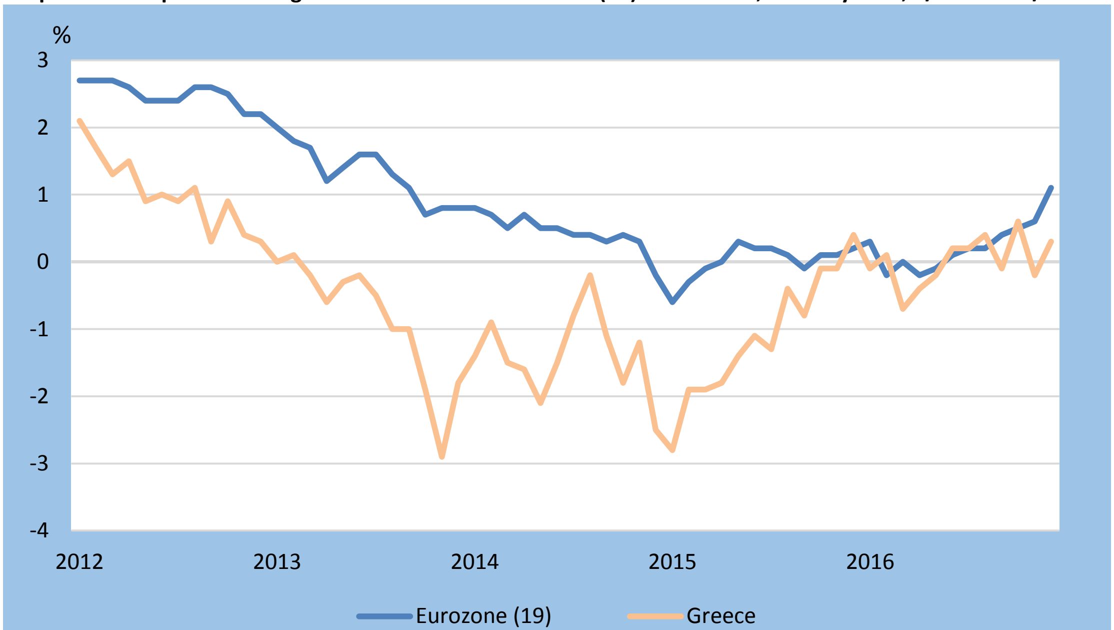
Source: *Bank of Greece*

Graph 9 Cumulative decline between 2010 and 2015, Greece.



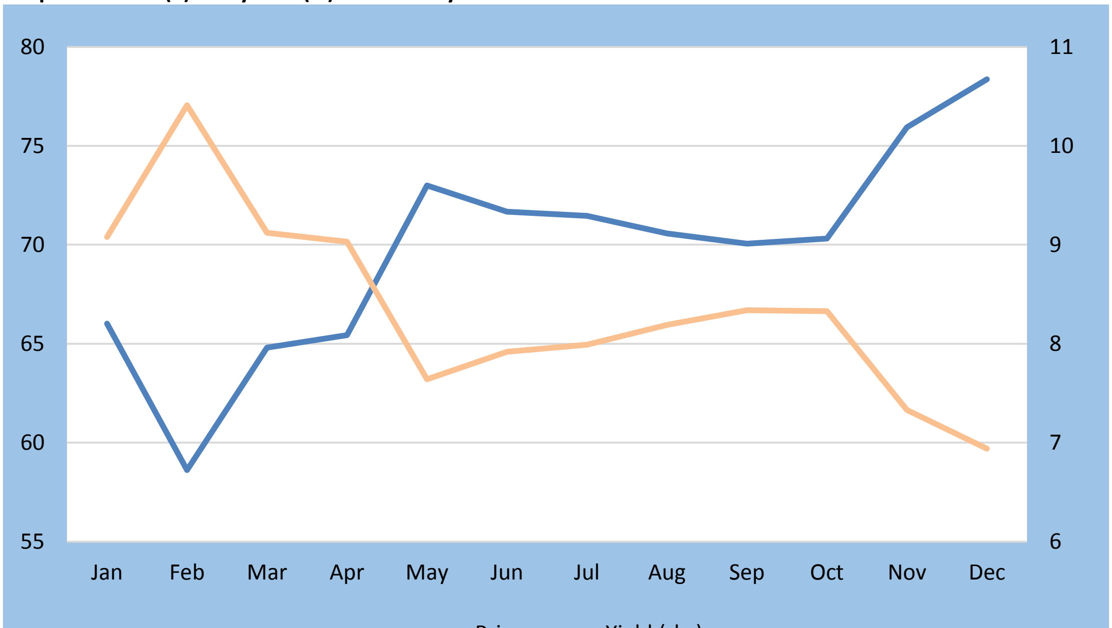
Source: *ELSTAT and PBO calculations*

Graph 10 Y-O-Y percent change of the HICP in the Eurozone (19) and Greece, monthly data, 1/2012 – 12/2016.



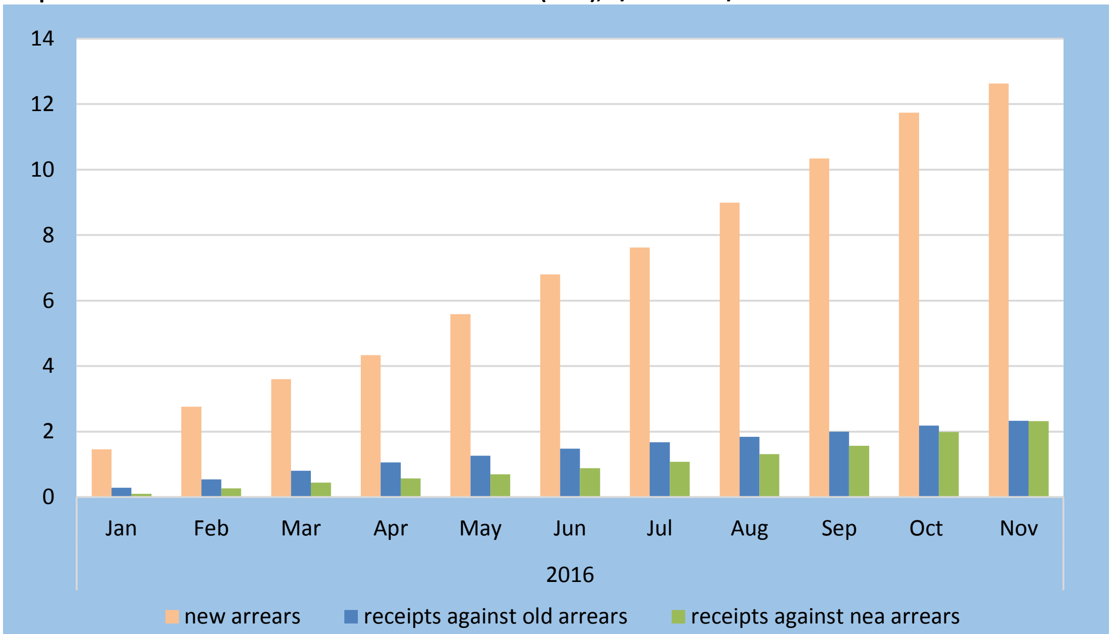
Source: *Eurostat*

Graph 11 Prices (€) and yields (%) of the ten-year Greek Government Bonds.



Source: *Bank of Greece*

Graph 12 Arrears towards the Public Sector in Greece (€ bn), 1/2016 – 11/2016.



Source: *Ministry of Finance*