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5th review of Greece's adjustment program

Key items in the agenda and timeline of events in the crucial six months ahead

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This report provides an overview of the key focus of discussions between domestic authorities and the troika in the context of the next (5th) review of Greece's adjustment program. In addition, it presents a brief timeline of key dates and events that deserve close monitoring in the crucial six-month period ahead.

Preparatory talks held in early September on key issues underlying Greece's 5th program review; official discussions on a new debt relief package expected to incept later this autumn

As a preparatory step ahead of the inception of the 5th adjustment program review, high-level government officials met with the troika mission heads in Paris in early September for an interim assessment of the progress made thus far in fulfilling a number of agreed prior actions. A joint ECB/IMF/EC statement issued after the completion of said discussions read that "productive" talks were held between the two sides and confirmed that the troika mission heads will return to Athens in late September. According to press reports, discussions focused on structural reforms and fiscal developments, with European Commission spokesperson for Economic and Monetary Affairs Simon O' Connor stating that debt sustainability and the potential for a new relief package were not included in the Paris meetings' agenda. As per a number of press reports, this issue will be addressed later this autumn, while other items to be discussed by then may also include the nature of and the creditor participation in the surveillance of the country's reforms program following the release of the last EFSF loan instalment (€2.9bn).[2,3]

5th program review: key items on the agenda and progress made thus far in fulfilling prior actions

This section provides some analysis on the issues expected to dominate the agenda of the 5th program review. According to local press, the Greek government's intention is to reach final agreement with the troika on key program milestones within 2-3 weeks after the inception of the next round of official talks. This is to allow discussions on a new debt relief package to commence soon after the announcement of the EU-wide stress test results (expected on 26 October 2014), with an intention to have them completed by year-end.

[2] A staff-level agreement on the core issues underlying the 5th program review is a key precondition for the release of additional funding to Greece, including: (i) the last EFSF loan tranche, amounting to €2.9bn (whereas the last IMF loan disbursement is due in Q1 2016); (ii) €3.4bn from the IMF under the Extended Fund Facility; and (iii) €2.1bn in ANFA and SMP profits, initially planned for Q3 2014.

[3] Speaking at the press conference following the September 12 Eurogroup, President Jeroen Dijsselbloem cited that once the key findings of the upcoming review become clear, euro area officials will initiate discussions on a number of "interrelated issues such as the arrangements to be put in place once the current programme expires at the end of the year".

Public administration reform agenda - key items

i. Mandatory exit of ca 6.5k public employees by the end of this year, so as to fulfil agreed target of 15k layoffs in 2013-2014.[4]

ii. Public sector employee evaluations for the year 2013, under a newly established system for assessing performance.

Comments

- According to reports, Greece's Minister of Administrative Reform and E-Governance has reassured the troika of the government's commitment to proceed with 6.5k mandatory exits by the end of this year. This will be attained through the mobilization of the following employee pools: (i) 1,050 redundant positions resulting from the merging, downsizing or closing down of certain private law entities; (ii) contractual staff, estimated at ca 1,800, who lost their legal appeal against the non-renewal of their temporary contracts; (iii) 3,600 who were placed in the mobility scheme for eight months and failed to be reappointed in the broader public sector to fill in vacant positions; and (iv) perjurer employees .
- Public sector employee evaluations are now expected to be completed with a one-month delay i.e., sometime in October 2014. In protest to the evaluation scheme, the Civil Servants' Confederation (ADEDY) had recently asked its members not to take part in the relevant process and appealed to the Council of State. In response, the Council of State announced earlier this month that ADEDY's appeal will be assessed in October 2014, and until then the evaluation scheme will have to be implemented as initially planned.[5,6]

Labor market reform agenda- Key items

i. Re-assessment of existing framework for collective dismissals.

ii. Identification of necessary legal changes in the regulatory framework dictating labor unions' operation, including the procedure applied for engaging in a strike against practices in other EU countries.

Comments

- In the context of the last (4th) program review, an agreement was reached on the adoption of a new procedure for a trial period of six months regarding the approval of collective company redundancies in the excess of the current layoff limits.[7,8] Following the expiration of that period (i.e., September 2014), the effectiveness of the aforementioned procedure will have to be re-assessed. During the official talks in Paris earlier this month, the Greek side reportedly argued that under the existing procedure the Labor & Social Security Minister's earlier veto power has *effectively* been eliminated. On its part, the troika is said to have insisted that the Labor & Social Security Minister's veto power has to be abolished through a statutory law so as to further liberalize the domestic labor market and remove any political involvement in decisions relating to collective redundancies. The issue of collective dismissals is expected to feature high in the agenda of the upcoming official discussions, with final decisions to be reached upon consultation with the International Labour Organisation (ILO).
- According to press reports, the troika insists that a decision to engage in a strike should be reached by the absolute majority of all employees (50%+1) in a general meeting. This comes against the current trade-union law (Law 1264/82) which entails that the decision for calling a strike may be reached by either: (i) the absolute majority of participants in a general meeting; or (ii) the absolute majority of respective trade union Board members (dependent on the nature of the trade union). Any final decisions on the aforementioned issue will reportedly be based on a special study on the regulatory framework dictating labor unions' operation in other EU countries. The said study is being prepared by Greece's Ministry of Labor and Social Affairs and it is expected to be completed in a couple of weeks from now. Under the existing MoU conditionality, legislation relating to a revised operational framework for trade unions should be submitted to Parliament for approval by end-October 2014.

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[4] According to the latest available data, the total public sector workforce stood at 634.688 in May 2014, having declined by 23.275 and 307.937 since end-2013 and end-2009, respectively. These developments provide support to the government's argument that the overall public sector workforce is falling faster than expected initially, mainly thanks to a natural attrition, early retirements, the non-renewal of fixed, contracts and the application of a 1:5 hiring rule in the broader public sector through a meritocratic process.

[5] The evaluation system, estimated to involve ca 300k public employees, is initiated through the introduction of quota rating. Specifically, 25% of public sector employees in ministries, municipalities and other legal entities will be rated with top grades between 9 and 10, 60% of them between 7 and 8 and the remaining 15% between 1 and 6.

[6] According to the latest IMF report on Greece, mandatory exits so far "have been based on performance and constitutional restrictions", while "performance-based dismissals remain an impediment.

[7] According to the current labor regulation in Greece, the monthly limit of layoffs is a follows: (i) 5% of staff for companies with more than 150 employees (with an upper limit of 30 employees); and (ii) 6 employees for companies with 20-150 employees.

[8] According to the existing procedure for the approval of collective company redundancies which is in line with the relevant Council Directive 98/59 and has been approved by Greece's main employer organizations (SEV, ESEE, GSEVEE, SETE) and the General Confederation of Greek Workers (GSEE), final decisions on collective company redundancies rest with the Supreme Labour Council, which is headed by the General Secretary of the Labor & Social Security Ministry.

Projected fiscal gap in FY-2015

As per the latest MoU update (June 2014), a fiscal gap worth ca 1.0%-of-GDP (ca €2bn) is projected to arise in 2015, lower compared to a €1.8bn shortfall estimated in the context of the 3rd program review in July 2013.[9,10] On its part, the Greek side has adopted a relatively more optimistic stance, arguing that any fiscal shortfall arising in 2015 is not likely to exceed €0.9bn thanks to improved GDP growth dynamics and ongoing reforms aiming to strengthen the efficiency of the tax collection mechanism. Moreover, in view of the satisfactory execution of the State budget so far this year the Greek government is planning to implement certain tax reforms in the context of the preparation of the FY-2015 Budget.[11,12] In his keynote speech at the 79th Thessaloniki International Fair earlier this month, Greece's Prime Minister Antonis Samaras announced a number of tax reforms, including, inter alia [13], a 30% reduction of the special consumption tax on heating oil[14] and a cut in the solidarity surcharge rate applied on annual incomes above €12k.[15] In addition, Mr. Samaras announced an increase in the maximum number of monthly installments for overdue taxes and social security contribution payments from 48 currently. According to reports, the Greek side has already proposed an increase in the maximum number of tax and social security contribution installments to 72 or 100, facing strong opposition from official lenders.[16] Taking into consideration the aforementioned announcements, the two sides will need to revise accordingly their fiscal gap estimates for FY-2015 when official discussions commence in late September. Further complicating any such projections, the government has committed to proceed with the gradual restoration of the wages of armed forces and emergency services personnel after the Council of State deemed unconstitutional the salary and pension cuts imposed on unformed personnel and judges in mid-2012. Should the said salary and pension levels were fully restored, the ensuing financing shortfall would reportedly amount to ca €750-800mn plus €350mn/annum (in increased wage and pension expenditure payments) from 2015 onwards. In addition to that, the Hellenic Parliament approved earlier this month certain amendments to the implementation framework of the new uniform tax on real estate property (ENFIA), including an increase in the number of installments from five to six as well as lower tax rates for socially vulnerable groups and vacant properties which are not rented and/or not connected to the electricity grid. According to press reports, the ensuing budgetary shortfall is estimated at ca €200-300mn/annum. As per the same sources, the troika has already agreed on the proposed amendments on ENFIA, under the assumption that the projected receipts target of €2.65bn/annum will be met.

New framework to deal with private sector indebtedness

In line with internal best practice and in consultation with the EC/ECB/IMF, Greek authorities have established a Government Council for the Management of Private Debt to coordinate legal and institutional reforms aiming to enhance corporate and personal debt resolution frameworks. The major tasks of the Council are, among other, the following: i) *introduction of a binding Code of Conduct for banks* (*May 2014 structural benchmark*). The said Code has been approved by a Bank of Greece special committee and was published in the Government Gazette late last month specifying the principles, ethics and the terms of engagement between credit institutions and household and corporate debtors, regarding payment methods or final settlement of non-performing loans, with domestic banks being required to pilot and implement long-term debt restructuring tools by end-September 2014 (and be compliant with the Code by end-2014); (ii) *out-of-court restructuring tools for enterprises* (*July structural benchmark*). Greek authorities have nearly completed the said scheme aiming to facilitate the restructuring of viable commercial entities. Minister of Development and Competitiveness Nikos Dendias was quoted as saying in local press recently that the Greek government has reached an agreement in principal with the troika heads on the proposed restructuring scheme and certain

[9] Domestic authorities have committed to cover any projected fiscal gap next year mainly through the extension of a number of expiring measures including, among other, a solidary surcharge introduced in 2011.

[10] The solidarity tax has reportedly generated revenue of ca €1.4bn in 2013.

[11] According to preliminary data for the State Budget execution for the first eight months of the year, the Central Government primary balance recorded a surplus of €1.95bn on modified cash basis (ca 1.1%-of-GDP), outperforming by €0.96bn the respective target envisaged in the revised medium-term fiscal plan (MTFS 2015-2018). In a similar vein, the General Government primary balance recorded a surplus of €3.24bn in the first seven months of the year compared to a surplus of €1.77bn in the same period a year earlier.

[12] According to the updated MoU conditionality, "if there is sustained over performance of revenue, contingent on the fiscal targets being met, the Authorities will in consultation with the EC-ECB-IMF consider a reduction in the high statutory tax rates while aiming to broaden the tax bases".

[13] Longer-term, the government also plans a gradual reduction in the top income tax rate (to 32% from 42%, currently) and in the main corporate tax rate (to 15%, from 26%). That is, depending on the available fiscal space.

[14] In a written statement issued earlier this month, Alternate Minister of Finance Christos Staikouras said that the harmonization of the special consumption tax on heating oil with that on fuel for vehicles in November 2011 has proved to be "financially ineffective and socially unjust". According to the same official, the measure added to the burden of low-income social groups and increased environmental pollution, without succeeding in combating illegal oil trade or boosting State tax revenues. Heating oil consumption was reportedly reduced by 67%YoY and 71%YoY in the 2013-2014 and 2012-2013 winter seasons respectively, with generated tax revenue underperforming the agreed target by around €300mn/annum.

[15] According to press reports, the government intends to apply a 30% rate cut in the existing solidarity tax.

[16] Cumulative tax arrears accrued up to end-July 2014 stood at ca €68.5bn, out of which €15.2bn was accumulated in the first seven months of this year.

technical modalities will be specified in the context of the upcoming official discussions; and (iii) *changes to the personal and corporate insolvency law* (*June structural benchmark).* Greece's Ministry of Development and Competitiveness is currently in consultations with the Ministry of Finance and the Bank of Greece to present soon the necessary changes to improve the functioning of in-court (personal and corporate) insolvency procedures.[17] Following public consultation with relevant stakeholders the new framework is expected to be finalized and implemented by the end of October 2014. The aforementioned reforms will also address domestic banks' large stock of non-performing loans (NPLs) which were reported to have reached 33.5% of total loans in end-Q1 2014 (or €77bn) up from 31.9% in end-December 2013 with 55% (or €42bn) of them attributed to the corporate sector, 13% (€10bn) to the consumer sector and 32% (or €25bn) to the housing sector

For further analysis on the remaining prior actions to the 5th program review, see Greece Macro Monitor "Official discussions on Greece's 5th program review to incept in mid-September- Key items on the agenda", July 22, 2014, http://www.eurobank.gr/Uploads/Reports/GREECE%20MACRO%20FOCUSJuly%2022%202014.pdf

Calendar of key dates and events in the 6-month period ahead

On the basis of the most recent developments and the information we have collected from a number of sources, we present below an indicative timetable of key dates and events that deserve special monitoring in the period leading to the crucial parliamentary vote for the new President of the Hellenic Republic.

September 29, 2014

Troika mission heads are expected to return to Athens for the launch of official discussions in the context of the 5th program review.

October 6, 2014

Submission to the Hellenic Parliament of the FY-2015 draft Budget Law.

October 13, 2014

Eurogroup meeting. Main issues of discussion include, inter alia: (i) financial and macroeconomic developments in the euro area, (ii) update on Greece's 5th program review; (iii) preparation of the October European Council; and (iv) banking union - economic and legal aspects.

October 23, 2014

European Council Meeting

October 26, 2014

EU-wide stress test results are reportedly expected to be announced. The EU-wide stress test, initiated and coordinated by the EBA, in coordination with national supervisory authorities, the ECB, the ESRB, and the European Commission, is carried out on a sample of 124 EU banks from 22 EU Member States, including Greece's four systemic banks, Eurobank, Piraeus Bank, National Bank and Alpha Bank. The resilience of EU banks will be assessed under a common baseline and adverse macro-economic scenario covering the period 2014-2016. In terms of capital thresholds, 8.0% Common Equity Tier 1 (CET1) will be the capital hurdle rate set for the baseline scenario and 5.5% CET1 for the adverse scenario.

November - December 2014

A number of key votes in Greek Parliament are expected during the last two months of the year. Among others, these include:

i. New household and corporate insolvency frameworks.
ii. Extension of the solitary surcharge in 2015, albeit with reduced applied tax rates.
iii. Social security reforms incorporating (a) integration of all funds providing supplementary pensions and fall under the ESA95 definition of General Government in the Unified Supplementary Insurance Fund (ETEA); and (b) all supplementary pension funds to be solely financed by own contributions.
iv. Budget Law for FY-2015.

[17] These will include, among others, establishing a regulated profession of insolvency administrators, not restricted to any specific profession and in line with best practice in EU.

According to Article 67 of The Constitution of Greece, Parliament cannot resolve without securing an absolute majority (50%+1) of the attending MPs, which cannot be less than 1/4ths of the total number of parliamentary deputies). With regards to the parliamentary vote on the Budget, which is traditionally tantamount to a confidence vote on the government, the voting procedure is based on Article 84 of the Constitution. This specific Article entails that the vote on a motion of confidence (or censure) cannot be adopted unless it is approved by an absolute majority of the attending MPs, which cannot be less than 2/5ths of the total number of parliamentary deputies (*i.e.,* 120 in favor votes). However, in practice the number of in-favor votes on the new Budget must be higher than 120 and at least 151 in the 300-seat Greek Parliament, so as for the government to continue enjoying its legitimacy. As a reminder the ruling coalition enjoys the support of 154 lawmakers; New Democracy controls 126 and socialist PASOK 28 seats.

November 6, 2014
Eurogroup meeting

November 21, 2014
Eurogroup meeting (confirmation pending)

Moodys is scheduled to publish its revised assessment on Greece's long-term sovereign credit rating. It currently assigns Greece a Caa3 rating with a stable outlook, two notches below both S&P and Fitch (B).

November 28, 2014
Fitch is scheduled to publish its revised assessment on Greece's long-term sovereign credit rating.

December 8, 2014
Eurogroup meeting

December 11, 2014
The second ECB Targeted Long-Term Refinancing Operation (T-LTRO) is scheduled to take place, part of a new stimulus package the Central Bank recently announced. Funds will have 4-years maturity and a fixed rate equal to the main refinancing operation rate (MRO) 0.05% plus 10bps. In the first T-LTRO operation held on September 17, 2014 the ECB handed €82.6bn, lower compared to market consensus of ca €160bn, out of which, ca €5bn was reportedly absorbed by Greece's four systemic banks.

December 18, 2014
EU Council Meeting

Parliamentary election for the new President of the Hellenic Republic to take place **at least one month before the expiration of the tenure of the incumbent**
Procedure for the election of the President of the Hellenic Republic likely to commence. According to the Constitution of Greece (Article 32, paragraphs 1, 3 & 4), the vote in Parliament for the election of the President of the Hellenic Republic should take place at least one month before the expiration of the tenure of the incumbent (*i.e.*, 4 February 2015). The relevant procedure incorporates three separate ballots in Parliament. In the first two, a 2/3rd majority of the total 300 MPs is required (*i.e.*, 200 in-favor votes). If both fail to produce a decisive outcome, a third ballot takes place where a majority of 3/5th is needed (*i.e.,* 180 in-favor votes). Should it also fail to produce a qualified majority, Parliament has to be dissolved within ten days, and elections for a new Parliament shall be called. In his keynote speech at the Thessaloniki International Fair earlier this month, Greece's Prime Minister Antonis Samaras played down once again the prospect of snap elections stressing that such a development "would be political suicide for Greece".

February 12, 2015
European Council Meeting

March 19, 2015
European Council Meeting

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