COMMISSION OF THE EUROPEAN COMMUNITIES

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COMMISSION OPINION

on the existence of an excessive deficit in Greece

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THE APPLICATION OF THE STABILITY AND GROWTH PACT IN THE CURRENT CRISIS SITUATION

1. Many EU countries are presently facing general government deficits above the 3% of GDP reference value set in the Treaty. The often strong deterioration in the deficit as well as the debt positions must be seen in the context of the unprecedented global financial crisis and economic downturn. Several factors are at play. First, the economic downturn brings about declining tax revenue and rising social benefit expenditure (e.g. unemployment benefits). Second, recognising that budgetary policies have an important role to play in the current extraordinary economic situation, the Commission called for a fiscal stimulus in its November 2008 European Economic Recovery Plan (EERP), endorsed by the European Council in December. The Plan explicated that the stimulus should be timely, targeted and temporary and differentiated across Member States, with more room for manoeuvre for those Member States that have achieved sustainable public finance positions and improved their competitive positions. The Plan also called for structural reforms that support demand and promote resilience in the short term, while paying special attention to actions in the four priority areas of the Lisbon Strategy. Finally, several countries have taken measures to stabilise the financial sector, some of which impact on the debt position or constitute a risk of higher deficits and debt in the future, although some of the costs of the government support could be recouped in the future.

2. The Stability and Growth Pact requires the Commission to initiate the excessive deficit procedure (EDP) whenever the deficit of a Member State exceeds the 3% of GDP reference value. The amendments to the Stability and Growth Pact in 2005 aimed at ensuring that in particular the economic and budgetary background was taken into account fully in all steps in the EDP. In this way, the Stability and Growth Pact provides the framework supporting government policies for a prompt return to sound budgetary positions taking account of the economic situation and thereby ensuring long-term sustainability of public finances.

LEGAL BACKGROUND

3. Article 104 of the Treaty lays down an excessive deficit procedure (EDP). This procedure is further specified in Council Regulation (EC) No 1467/97 “on speeding up and clarifying the implementation of the excessive deficit procedure”[1], which is part of the Stability and Growth Pact.

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[1] OJ L 209, 2.8.1997, p. 6. Account is also taken of the Opinion of the Economic and Financial Committee on the “Specifications on the implementation of the Stability and Growth Pact and guidelines on the format and content of stability and convergence programmes”, endorsed by the ECOFIN Council of 11 October 2005, available at: http://ec.europa.eu/economy_finance/other_pages/other_pages12638_en.htm.

4. According to Article 104(2) of the Treaty, the Commission has to monitor compliance with budgetary discipline on the basis of two criteria, namely: (a) whether the ratio of the planned or actual government deficit to gross domestic product (GDP) exceeds the reference value of 3% (unless either the ratio has declined substantially and continuously and reached a level that comes close to the reference value; or, alternatively, the excess over the reference value is only exceptional and temporary and the ratio remains close to the reference value); and (b) whether the ratio of government debt to GDP exceeds the reference value of 60% (unless the ratio is sufficiently diminishing and approaching the reference value at a satisfactory pace).

5. Article 104(3) stipulates that, if a Member State does not fulfil the requirements under one or both of these criteria, the Commission has to prepare a report. This report also has to "take into account whether the government deficit exceeds government investment expenditure and take into account all other relevant factors, including the medium-term economic and budgetary position of the Member State".

6. On the basis of the data notified by the Greek authorities in October 2008[2] and subsequently validated by Eurostat[3] and taking into account the Commission services' January 2009 interim forecast, the Commission adopted a report under Article 104(3) for Greece on 18 February 2009[4].

7. Subsequently, and in accordance with Article 104(4), the Economic and Financial Committee formulated an opinion on the Commission report on 27 February 2009.

8. Article 104(5) of the Treaty requires the Commission to address an opinion to the Council if the Commission considers that an excessive deficit in a Member State exists or may occur. In order to reach a conclusion on whether an excessive deficit exists or may occur, the Commission considers that account should be taken of: (i) the conclusions of its report under Article 104(3) and (ii) the opinion of the Economic and Financial Committee on this report. On the basis of these elements, the Commission has established a number of considerations for Greece.

CONSIDERATIONS CONCERNING GREECE

9. An EDP for Greece was initiated in May 2004 by the Commission with the adoption of a report under Article 104(3) in view of a deficit of 3.2% of GDP in 2003, i.e. above the reference value. The Council, upon the corresponding Commission recommendation, placed Greece in excessive deficit on 5 July 2004 and, according to Article 104(7) of the Treaty, addressed its recommendations with a view to bringing the excessive deficit situation to an end by 2005. On 18 January 2005, the Council decided in accordance to Article 104(8) that Greece had not taken effective action in response to these recommendations. On 17 February 2005, upon a Commission

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2 According to Council Regulation (EC) No 3605/93, Member States have to report to the Commission, twice a year, their planned and actual government deficit and debt levels. The most recent notification of Greece can be found at: http://epp.eurostat.ec.europa.eu/portal/page?_pageid=2373,58110711&_dad=portal&_schema=portal.

3 Eurostat news release No 147/2008 of 22 October 2008.

4 All EDP-related documents for Greece can be found at the following website: http://ec.europa.eu/economy_finance/netstartsearch/pdfsearch/pdf.cfm?mode=_m2.

recommendation in accordance with Article 104(9), the Council decided to give notice to Greece to take measures for the deficit reduction judged necessary to remedy the situation at the latest by 2006. The Council established the deadline of 21 March 2005 to take effective action to comply with this Decision. On 6 April 2005, the Commission adopted a communication to the Council concluding that action taken until then was consistent with the Council decision and that, while the budgetary situation remained vulnerable, no further steps under the EDP were necessary at that stage. In its meeting of 12 April 2005, the Council concurred with this assessment. On 5 June 2007, the Council adopted, upon a corresponding Commission recommendation, a Decision abrogating Decision 2004/917/EC on the existence of an excessive deficit.

10. The abrogation decision was based on the data available at that time, implying the reduction of the general government deficit from 7.9 % of GDP in 2004 to 2.6 % of GDP in 2006. However, according to data notified by the Greek authorities in October 2008[5] and validated by Eurostat[6], the general government deficit in 2006 was revised upwards to 2.8% of GDP.

11. The general government deficit in Greece reached 3.5% of GDP in 2007, thus exceeding the 3% of GDP reference value. The Commission report under Article 104(3) considered that the deficit was close to the 3% of GDP reference value but that the excess over the reference value can not be qualified as exceptional within the meaning of the Treaty and the Stability and Growth Pact. In particular, the deficit did not result from an unusual event or a severe economic downturn. Real GDP growth reached 4% in 2007, before decelerating to 3% in 2008, posting positive output gaps of 3% and 2¾% of potential GDP, respectively. This output gap profile reflects that Greece has been enjoying good economic times in 2007 and 2008. Furthermore, the excess over the reference value can not be considered temporary. According to the Commission services' January 2009 interim forecast, the general government deficit net of one-offs is estimated at 3.6% of GDP in 2008 (or 3.4% of GDP including one-offs). However, a worse-than-projected budgetary outturn in 2008 cannot be excluded, on the basis of the most recent information on the execution of the 2008 Budget Law. For 2009, the Commission services' January 2009 interim forecast projects the general government deficit net of one-offs at 4.4% of GDP (3.7% including one-off revenue) on the basis of a prudent assessment of the 2009 Budget Law approved by Parliament on 21 December. Nevertheless, a worse-than-projected budgetary outturn in 2008 should entail, *ceteris paribus*, a more pronounced negative base effect in 2009. Based on the customary unchanged policy assumption and assuming the discontinuation of one-off measures, the 2010 deficit is projected at 4.2% of GDP. Therefore, the deficit criterion in the Treaty is not fulfilled.

12. General government gross debt stood at 94.8% of GDP in 2007 and 94.6% of GDP in 2008, well above the 60% of GDP Treaty reference value. According to the Commission services' January 2009 interim forecast, the general government debt

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5 According to Council Regulation (EC) No 3605/93, Member States have to report to the Commission, twice a year, their planned and actual government deficit and debt levels. The most recent notification of Greece can be found at: http://epp.eurostat.ec.europa.eu/portal/page?_pageid=2373,58110711&_dad=portal&_schema=portal.

6 News Release 147/2008 of 22 October 2008 on the provision of data for the excessive deficit procedure.

ratio is projected to increase further to 96¼% in 2009 and 98½% of GDP by 2010. Therefore, the debt criterion in the Treaty is not fulfilled.

13. In line with the provisions in the Treaty and the Stability and Growth Pact, the Commission also analysed in its report "relevant factors". According to the Stability and Growth Pact, these can only be taken into account in the steps leading to the decision on the existence of an excessive deficit if the deficit satisfies the double condition of closeness and temporariness. In the case of Greece, the double condition is not met. Considered on their own merit, the relevant factors in the current case on balance do not seem favourable.

14. The opinion of the Economic and Financial Committee in accordance with Article 104(4) of the Treaty is consistent with the assessment in the Commission report under Article 104(3).

CONCLUSION

15. The monitoring of the budgetary situation in Greece and, in particular, the examination of the compliance with the criteria laid down in Article 104(2) has led the Commission to prepare a report in accordance with Article 104(3) of the Treaty. The Commission, having taken into account its report and the opinion of the Economic and Financial Committee, is of the opinion that an excessive deficit exists in Greece.