

HELLENIC REPUBLIC
MINISTRY OF ECONOMY AND FINANCE

THE 2003 UPDATE OF THE HELLENIC
STABILITY AND GROWTH PROGRAMME:
2003-2006

- *The update of Greece's Stability and Growth Programme is submitted to the European Commission in accordance to the Article 4 of the European Council Regulation 1466/97.*
- *The programme can be found at the web site of the Greek Ministry of Economy and Finance:
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1. Introduction

In 2003 the Greek economy continued to perform quite strongly, and the prospects for growth in the coming years are quite encouraging. The GDP growth rate for 2003 is estimated to be 4 per cent, and that for 2004 around 4.2 per cent. The Private consumption remained buoyant and Investment spending remained linked to the financial flows from the E.U Structural Funds, the accelerating preparations for the Olympics, along with strong private investment. The external sector deficit remained high as exports of tourist services stagnated due to weak foreign demand and geopolitical uncertainties. Inflation continued to be higher than the E.U average, while the unemployment rate fell to 8.9 per cent in the second quarter of 2003 from 9.6 per cent a year ago.

On the fiscal front there was a small deviation from the target for the general government deficit target due mainly to the speeding up of the expenditures for the Olympic games but also to increased expenditures for the compensation of households and firms for the damages they suffered from unusual natural disasters that took place in the first half of 2003. Debt continued to deescalate and is expected to be, at the end of the year, at about 101.7 per cent of GDP.

The present update of the Greek Stability and Growth Program takes place in a period with good prospects for recovery in the world and the European economy. Despite the recent favourable developments in the external environment, the GDP growth projections for the years 2004-2006 are based on cautious assumptions about the domestic components of the economic activity. The Olympic Games that will take place in Athens in 2004 are expected to have significant externality effects on the economy and particularly on the tourist sector for the coming years. Moreover, as many projects that are co-financed by the E.U 3rd Community Support Framework become more mature, we expect higher flows of funds from the E.U that will help to maintain a high level of activity mainly in the construction sector. These factors in combination with the projected strong private consumption and investment can sustain a high level of economic activity over the next few years.

Furthermore, the measures that have been taken recently by the government or have been introduced to the Parliament for approval, touch upon a broad spectrum of areas, like the further simplification of the tax system, the new system of controlling

public expenditures, the continuation of the privatisation of state owned assets, and reforms in the area of public administration. These measures are expected to have a positive impact on the performance of both the private and the public sector and to enhance the productive potential of the Greek economy.

In the following sections we present first the economic developments in 2002 and 2003 and the deviations that have occurred from the targets set in the previous update. In the third part we present the projections for the main economic aggregate for the years 2004-2006, as well as the underlying framework for economic policy. In the fourth part we compare the 2002 Stability and Growth Program with the present one. In the fifth part we present an alternative of economic growth with GDP growth rates well below the baseline scenario. In the sixth section we briefly outline the main structural reform measures that have been initiated by the government and are expected to have an impact on the budgets during the program's period. Finally in the last section we present the main policy commitments of the Greek government for the next three years.

Recent developments and prospects of the Greek Economy

Table 1 presents, in a compound form, the main macroeconomic aggregates and projections of the 2003 updated Stability and Growth Program (SGP) of the Greek economy, for the period 2001-2006, as well as the assumptions used for the external environment..

Table 1. Growth and Associated Factors

	2001	2002	2003	2004	2005	2006
SELECTED ECONOMIC INDICATORS						
GDP GROWTH AT CONSTANT PRICES	4.0%	3.8%	4.0%	4.2%	4.0%	3.8%
GDP LEVEL AT CURRENT MARKET PRICES (bn euro)	131.0	141.3	152.2	163.9	175.9	188.1
GDP DEFLATOR CHANGE	3.5%	4.0%	3.5%	3.4%	3.2%	3.0%
PRIVATE CONSUMPTION DEFLATOR CHANGE	3.3%	3.6%	3.5%	3.0%	2.8%	2.6%
EMPLOYMENT GROWTH	-0.3%	0.1%	1.5%	1.7%	1.3%	1.1%
LABOUR PRODUCTIVITY GROWTH	4.4%	3.7%	2.5%	2.5%	2.7%	2.7%
UNIT LABOUR COSTS	1.1%	4.6%	3.5%	3.9%	2.3%	2.0%
GENERAL GOVERNMENT BALANCE, % OF GDP	-1.5%	-1.2%	-1.4%	-1.2%	-0.5%	0.0%
GENERAL GOVERNMENT DEBT, % OF GDP	106.9%	104.7%	101.7%	98.5%	94.6%	90.5%
SOURCES OF GROWTH: PERCENTAGE CHANGES AT CONSTANT PRICES						
1. PRIVATE CONSUMPTION EXPENDITURE	2.9%	2.8%	3.1%	3.2%	3.3%	3.2%
2. GOVERNMENT CONSUMPTION EXPENDITURE	-1.0%	5.1%	0.5%	1.0%	0.5%	0.5%
3. GROSS FIXED CAPITAL FORMATION	6.5%	5.7%	9.7%	7.0%	5.7%	5.5%
4. CHANGES IN INVENTORIES (% GDP)	0.0%	0.1%	0.0%	0.0%	0.0%	0.0%
5. EXPORTS OF GOODS AND SERVICES	-1.1%	-7.7%	1.9%	6.7%	5.6%	5.3%
6. IMPORTS OF GOODS AND SERVICES	-3.4%	-4.7%	3.0%	4.7%	3.8%	3.7%
CONTRIBUTION TO GDP GROWTH						
7. DOMESTIC DEMAND (excluding inventories)	3.5%	4.0%	4.6%	4.2%	3.8%	3.7%
8. CHANGES IN INVENTORIES	-0.4%	0.1%	-0.2%	0.0%	0.0%	0.0%
9. EXTERNAL BALANCE OF GOODS AND SERVICES	0.9%	-0.4%	-0.5%	0.1%	0.1%	0.1%
BASIC ASSUMPTIONS ON THE EXTERNAL ECONOMIC ENVIRONMENT						
	2001	2002	2003	2004	2005	2006
SHORT-TERM INTEREST RATE	4.3%	3.3%	2.3%	2.3%	3.2%	3.3%
LONG-TERM INTEREST RATE	5.0%	4.9%	4.1%	4.4%	4.8%	5.0%
EURO / USD EXCHANGE RATE	0.90	0.95	1.13	1.16	1.15	1.15
WORLD GDP GROWTH, excl. EU	2.4%	3.2%	4.0%	4.6%	4.6%	4.5%
EU-15 GDP GROWTH	1.7%	1.1%	0.8%	2.0%	2.4%	2.3%
WORLD IMPORT VOLUMES, excl. EU	0.0%	3.2%	6.3%	8.3%	8.6%	8.5%
OIL PRICES (USD/ barrel)	25.0	25.0	28.3	25.6	24.1	24.0

2.1.1 The Greek Economy in 2002

In 2002, despite the slowdown in the world economy, GDP grew by 3.8 per cent, well above the EU average, with investment and private consumption being the main factors contributing to the economic activity. The contribution of total domestic demand to the GDP change was 4.1 percentage points, while the external balance of goods and services had a negative contribution of 0.4 per cent. Due to the unfavourable external environment, exports of goods and services decreased by 7.7 per cent in real terms, while imports decreased by 4.7 per cent, mainly due to the nominal decrease of the tourist sector payments by 46.1 per cent. Real private consumption increased by 2.8 per cent mainly because of an increase in the households' disposable income, while total investment increased at a strong pace, 5.7 per cent, though slightly less than in 2001. The fall in interest rates on housing loans and the rapid expansion of housing credit, the preparations for the 2004 Olympic games and the Community Structural Funds were the main contributors to this increase.

Table 2: Selected Economic Indicators 2002-2003

	2002		2003	
	<i>SGP2002</i>	<i>SGP2003</i>	<i>SGP2002</i>	<i>SGP2003</i>
1. GDP GROWTH	3.8%	3.8%	3.8%	4.0%
2. GROSS FIXED CAPITAL FORMATION	7.7%	5.7%	9.5%	9.7%
3. REAL UNIT LABOUR COST	-0.4%	0.1%	-1.2%	-0.1%
4. PRIVATE CONSUMPTION DEFLATOR	3.1%	3.6%	2.7%	3.5%
5. GENERAL GOVERNMENT BALANCE (% GDP)	-1.1%	-1.2%	-0.9%	-1.4%
6. GENERAL GOVERNMENT DEBT (% GDP)	105.3%	104.7%	100.2%	101.7%
7. UNEMPLOYMENT RATE	10.0%	10.0%	9.1%	9.0%

Labour market developments were slightly positive in 2002. Although the number of employees decreased rather significantly (1.2 per cent), total employment increased only slightly by 0.1 per cent, after a three-year period of decrease. The number of unemployed decreased by 21,100 persons and thus the unemployment rate fell to 10 per cent of the labour force, from 10.4 per cent in 2001.

Inflation in 2002 remained above the European average. The average Harmonized Index of Consumer Prices (HICP) was 3.9 per cent, 1.7 percentage points higher than the Euro area average. This higher rate can be attributed to the stronger growth performance of the Greek economy, (The well-known Balassa-Samuelson effect) but also to some extraordinary factors, such as the bad weather conditions at the beginning of the year and to the change-over to the Euro.

The general government deficit, on a national accounts basis, fell to 1.2 per cent of GDP from 1.5 per cent in 2001. Moreover, the consolidated general government debt was reduced by 2.2 percentage points, from 106.9 per cent of GDP in 2001 to 104.7 per cent in 2002.

2.1.2 The Greek Economy in 2003

It is now generally agreed that in 2003 GDP grew by 4.0 per cent in real terms, 0.2 percentage points more than it was projected in the 2002 SGP. Quarterly national accounts data show, for the first semester of 2003, an increase of GDP by 4.4 per cent, against 4.2 per cent in the same period of 2002. All available data suggest that investment and private consumption remain the main factors contributing to the strong economic activity. According to the quarterly national accounts data for the first semester of 2003, real total consumption expenditure increased by 3.9 per cent and gross fixed capital formation by 8.0 per cent. Other short-term indicators, which can be considered as proxies for the economic activity, support the view for a robust growth. More specifically, the volume of retail sales, in the period of January-June, increased by 5 per cent and credit to households, during the same period, continued to increase rapidly, (28,6 per cent in July). Finally, private building activity, in the first 5-month period increased significantly by 10.6 per cent. Based on the above conjectural indicators, it can be safely projected that, for the year as a whole, private consumption growth will be 3.1 per cent and investment growth 9.7 per cent.

As far as the external balance is concerned, it is estimated that exports of goods and services will increase in real terms by 1.9 per cent and imports by 3.0 %. Thus, the contribution of the external sector to the GDP growth will be negative by 0.5 percentage points. Balance of Payments (BOP) data, published by the Bank of

Greece, show that in the first nine months of 2003, exports and imports of goods, at current prices, increased by 5.9 and 2.2 per cent respectively. For the whole year, the current external balance as a percent of GDP, on a national accounts basis, is estimated to be less than 6 per cent. It is true that in the last few years, there was an increase of the Greek external deficit as a percent of GDP, due mainly to the high growth rates of the economy.

With regard to labour market developments in 2003, we observe that, in the first semester, according to the Labour Force Survey, total employment increased by 2.1 per cent, the number of employees also rose by 0.4 per cent and the unemployment rate fell to 9.4 per cent from 10.3 per cent in the corresponding period of 2002. For the year as a whole, the unemployment rate is estimated to be at about 9.0 per cent, from 10.0 per cent in 2002. This improvement can be attributed not only to the high GDP growth rate but also to the large-scale restructuring that has been taking place in the Greek economy over the last few years..

According to the latest available data, the average HICP inflation was in August 3.6 per cent, 1.5 percentage points higher than the Euro area average. In 2003, inflation shows a deceleration trend. The HICP increased by 3.8 per cent in the first quarter, by 3.5 per cent in the second and it is estimated to increase by 3.4 per cent in the third quarter of the year. For the whole year, the average HICP inflation is estimated to be around 3.5 per cent, from 3.9 per cent in 2002. An important factor that influences inflation, the unit labour cost, is estimated to increase by 3.5 per cent in 2003, from 4.6 per cent in 2002, while the output gap remains positive.

In the area of public finances, the general government deficit is estimated to be 1.4 per cent and the general government debt 101.7 per cent of GDP. The estimated deficit outturn is 0.5 percentage point higher than it was projected in the 2002 SGP. This deviation from the budget target can be explained by overruns in ordinary budget expenditures, which were due to the speeding up of the expenditures for the 2004 Olympic Games, and also to some extra expenditure for the compensation of the households and firms that suffered important damages caused by the bad weather.

Tables 3 and 4 present the data of the government budget as it was submitted to the Parliament last year and estimates for outturn in 2003 as included in the draft budget of 2004.

Table 3: Central Government Revenues and Expenditures (million Euro)

Million euro	2003 BUDGET		DIFFERENCE (1)-(2)
	BUDGET (1)	ESTIMATE (2)	
1. REVENUES	43000	42205	+795
(a) ORDINARY (NET REVENUE)	38900	39000	-100
<i>of which</i>			
i. DIRECT TAXES	15510	15457	+53
ii. INDIRECT TAXES	22035	22608	-573
(b) PUBLIC INVESTMENT PROGRAM	4100	3205	+895
2. EXPENDITURES	48303	48410	-107
(a) ORDINARY BUDGET	39385	39810	-425
<i>of which</i>			
i. COMPENSATION OF EMPLOYEES	15130	15236	-106
ii. OTHER EXPENDITURE	14855	15224	-369
iii. INTEREST PAYMENTS	9400	9350	+50
(b) PUBLIC INVESTMENT PROGRAM	8918	8600	+318
3. CENTRAL GOVERN. BALANCE (1-2+3)	-5303	-6205	+902
4. PUBLIC ENTITIES SURPLUS AND ESA ADJUSTMENT	3935	4015	-80
5. GENERAL GOVERNMENT BALANCE (3+4), % OF GDP	-1368	-2190	+822

Source: Greek Government Budget

Table 4: Contributions to Debt Developments (million Euro)

	2003 BUDGET		DIFFERENCE (1)-(2)
	BUDGET (1)	ESTIMATE (2)	
1. NET BORROWING REQUIREMENTS	5303	6205	-902
2. BURDEN FROM FOREIGN EXCHANGE	-220	-290	+70
3. DEBT ASSUMPTIONS	1980	4347	-2367
4. MILITARY BORROWING	1139	2060	-921
5. PRIVATISATION PROCEEDS (DEKA)	2990	3000	-10
6. INCREASE IN DEBT (1+2+3+4-5)	5212	9322	-4110
7. CENTRAL GOVERNMENT DEBT	171054	175439	-4385
8. INTERGOVERNMENTAL DEBT	20624	20624	0
9. GENERAL GOVERNMENT DEBT (7-8)	150430	154815	-4385

2.2 Basic Growth Scenario 2004-2006

The medium-term prospects of the Greek economy are quite encouraging. According to available data, announced policies, and the forecasts for the future economic activity in Europe and the World economy, it is projected that for the period of the Greek Stability and Growth Program, the domestic economic activity will remain quite robust, the inflation rate will decelerate and the fiscal position will be compatible with the requirements of Stability and Growth Pact.

For the external sector, we assume that markets will develop according to the projections of the Commission and other international organisations. The recently presented forecasts suggest an improvement in the external environment, with rates of growth for the total World GDP around 4.6 per cent and 2.2 per cent for the EU-15 GDP. It is also assumed that the price of oil will be, on average, around 24.5 USD per barrel. For the Euro parity to the USD, a small appreciation is assumed

Our baseline scenario for the period 2004-2006 is presented in Table 5, while detailed figures are given in the Annex.

Table 5: Selected Economic Indicators 2004-2006

	2004		2005		2006	
	<i>SGP2002</i>	<i>SGP2003</i>	<i>SGP2002</i>	<i>SGP2003</i>	<i>SGP2002</i>	<i>SGP2003</i>
1. GDP GROWTH	4.0%	4.2%	3.7%	4.0%	3.6%	3.8%
2. GROSS FIXED CAPITAL FORMATION	7.0%	7.0%	6.1%	5.7%	5.1%	5.5%
3. REAL UNIT LABOUR COST	-0.7%	+0.2%	-0.7%	-1.0%	-0.7%	-1.0%
4. PRIVATE CONSUMPTION DEFLATOR	2.8%	3.0%	2.6%	2.8%	2.6%	2.6%
5. GENERAL GOVERNMENT BALANCE (% GDP)	-0.4%	-1.2%	0.2%	-0.5%	0.6%	0.0%
6. GENERAL GOVERNMENT DEBT (% GDP)	96.1%	98.5%	92.1%	94.6%	87.9%	90.5%
7. UNEMPLOYMENT RATE	8.4%	8.0%	7.7%	7.4%	7.1%	7.0%

For the period 2004-2006, a robust sustainable growth rate is projected. Based on a buoyant domestic demand, the large inflows of funds from the EU's 3rd Community Support Framework and the infrastructure under construction for the preparations for the 2004 Olympic Games, GDP is projected to increase by an annual average rate of 4.0 . Fixed capital formation is expected to increase by 7.0 per cent in 2004 and by an average rate of 5.6 per cent for the years 2005 and 2006, while business investment is projected to grow by 7.9 per cent annually. In 2006, the share of investments as a percentage of GDP will be at about 26 per cent.

With regard to the other components of GDP, private consumption in the 2004-2006 period is projected to remain strong and increase by slightly more than 3 per cent every year, while the contribution of the external sector to GDP growth is expected to be slightly positive, due to the projected increased rates of exports of goods and services. This is due not only to the increased economic activity abroad, but also to the beneficial effects that the Olympic Games are expected to have, particularly on the tourist sector.

As a result of the high growth rates and the labour market reforms, employment, for the years 2003-2006, is projected to increase and unemployment to fall. The unemployment rate is expected to fall from an estimated 9.0 per cent in 2003 to at about 7.0 per cent in 2006.

Fiscal policy in the same period will continue to be prudent, aiming at increasing the general government primary surplus and at lowering the debt/GDP ratio. For the years 2004 and 2005, the general government balance is projected to remain negative but declining over the period, from -1.4 per cent of GDP in 2003, to -1.2 per cent in 2004 and -0.5 per cent in 2005. In 2006 it is projected a small surplus of 46 million euro. These targets satisfy the medium term objective of the Stability and Growth Pact, for the general government budget to be close to balance or in surplus. Primary surplus is estimated to range between 4.7 per cent and 5.3 per cent of GDP and it will be progressively increasing. These primary surpluses, along with the privatisation proceeds, secure a decline in the general government debt/GDP ratio, from 101.7 percent of GDP in 2003, to 90.5 percent in 2006.

For the years 2004-2006, inflation is projected to decline gradually towards the medium-term target of price stability. The private consumption deflator is projected to fall from 3.5 per cent in 2003 to 2.6 per cent in 2006. However, inflation in Greece will remain slightly above the European average, influenced by the high growth rates and the positive output gaps. It is worth mentioning that one of the factors influencing inflation, the nominal unit labour cost is projected to decelerate from 3.9 per cent in 2004 to 2.0 per cent in 2006. Labour productivity is also expected to continue rising by, more than 2.5 per cent annually, while nominal compensation of employees per head is projected to increase by an annual average rate of 5.4 per cent.

3. Economic Policies for 2004 - 2006

Economic policy in the medium term is oriented towards sustaining macroeconomic stability and pursuing real convergence with the EU average per capita income. Real convergence can be gradually achieved only through persistently higher (above EU averages) growth rates. However, sustainable high growth rates cannot be achieved only through macroeconomic policies. Structural reforms are a prerequisite for enhancing the productive potential of the economy and for making the economy more resilient to adverse shocks. Economic policies are therefore oriented towards these two goals.

Fiscal policies will continue to be geared towards reaching a close to balance budget position by 2006, reducing public debt to around 90 % of GDP. To this end a number of new measures have been initiated. Some of these measures are the following:

- A new draft law has been submitted to the Parliament for the simplification of the tax system, with main emphasis on the tax auditing procedures.
- A draft law, which enhances transparency and improves auditing and evaluation procedures for all categories of public expenditure, has been submitted to the Parliament.
- The government has announced that there will be a gradual reduction of the highest marginal tax rate, for personal income tax, by one percentage point every year, until it reaches 35 %.
- Also for the corporate income tax rate there will be a similar gradual reduction by one percentage point every year until it reaches 30 %.
- In early September, the Government announced also a series of measures, the so called “social package”, according to which there will be in 2004 increases to low pensioners and some other social groups higher than those contained in the last years update of the SGP.

In the coming years Greece will continue the efforts to make the best use of the resources of the 3rd Community Support Framework by completing the investment in the basic infrastructures, which will enhance significantly the productivity of the

private and public sector, but also by investing in education and training of the labour force..

Furthermore a number of measures of structural nature, mentioned in the section for structural reforms below, will improve the functioning of markets, the competitiveness of Greek firms, and will thus enhance the productive capacity of the Greek economy.

3.1 Fiscal Policy and Prospects for 2004-2006

Fiscal developments in 2002-2003 were characterized by some slippages in the general government deficit, which were mainly caused by overruns in expenditures, due to the speeding up of some projects for the 2004 Olympic games, and also to some expenditures for the compensation of the households and firms to cover damages caused by the bad weather..

As stated earlier, fiscal policy for the coming years, will continue to aim at bringing down to balance the general government deficit and to reduce the debt/GDP ratio. Despite some slippage in 2003 and 2004 from the targets set in the last year's update of the Greek SGP, from 2005 it will be easier to reduce public expenditures since the government budget will not bear anymore the costs of the Olympic Games. Moreover, the task of controlling more efficiently public expenditures will be facilitated by the implementation of the « Code of Fiscal Stability », which is part of a broader draft law, now before the Parliament, and is expected to be approved early next year.. According to the Code central government, local authorities and public sector entities can borrow only for investment and not for other expenditures.

On the revenue side of the budget, we expect that the last year's tax reform and the new measures for better tax auditing and further simplification of the tax system will enhance the efficiency of tax administration contributing thus to the maintenance of a high level of tax receipts.

With high GDP growth rates and improvements in the efficiency of both the revenue and the expenditure side of the budget, our target for the general government deficit could be attained without much difficulty.

The debt/GDP ratio remained above 100% at the end of 2003, a rate which is one of the highest in the European Union. It is true that the debt/GDP ratio, despite

the high primary surpluses in the last few years, has not been reduced correspondingly, due to the high stock flow adjustments. However, after the clearance of some issues related to the capital transfers to public corporations, the stock-flow adjustment items have been reduced significantly, and the reduction in the debt is much more in line with primary surpluses and the privatisation proceeds.

One other aspect that is worth mentioning is the significant improvement in the area of the public debt management. with the creation of the Public Debt Management Office (PDMA). The maturity structure of the Greek Public debt is now much smoother than a few years ago and the PDMA has achieved considerable savings by being very active in the markets. It is also important to note that the spreads of the Greek state bonds have narrowed significantly over the last few years.

On the basis of the 2004 draft budget that was submitted to the Parliament on the 18th of October, the prospects could be summarised as follows. At the level of general government, total revenues are projected to remain almost stable as a percent of GDP (43.7 per cent in 2003, 43.5 percent in 2006), while total expenditure is expected to decline from 45.2 percent to 43.5 percent in 2006. (see table 6)

For the current year the estimated balance of the general government will be a deficit of the order of 1.4 percent of GDP. For the coming years, the deficit will be declining and it is expected to be zero by the year 2006. At the same time the general government primary balance will increase gradually from 4.7 percent in 2004 to 5.3 percent of GDP in 2006. It should be mentioned that public expenditures in 2003 and 2004 are higher by almost 1 percent of GDP, due to the extra expenditure needed for the preparation of the Olympic Games, and which means that these expenditures will not be recurring in the years after 2004. Moreover, the expenditures for 2004 will be also higher than those included in the 2002 update by an amount of the order of 1/2 percentage point of GDP, due to the extra increases that will be given in 2004 to low pensioners, to some other vulnerable social groups, lone mothers, etc.

In the same period, the general government consolidated public debt will decline, and it is projected to be around 90 percent of GDP in 2006. The medium to long term target for public debt remains as before, namely to reduce the ratio of public debt to GDP, to 60 percent. (see table 7)

Table 6: General Government Budgetary Developments (on a national accounts basis)

% of GDP	2003	2004	2005	2006
GENERAL GOVERNMENT				
5. TOTAL REVENUE	43.7%	43.7%	43.7%	43.5%
6. TOTAL EXPENDITURE	45.2%	45.0%	44.2%	43.5%
7. GENERAL GOVERNMENT BALANCE	-1.4%	-1.2%	-0.5%	0.0%
8. INTEREST	6.1%	5.9%	5.6%	5.2%
9. GEN. GOVN. PRIMARY SURPLUS (8-7)	4.7%	4.7%	5.1%	5.3%
COMPONENTS OF REVENUES /EXPENDITURES				
10. TAXES	23.5%	23.3%	23.2%	22.9%
11. SOCIAL CONTRIBUTIONS	14.0%	14.0%	14.0%	14.0%
12. OTHER CURRENT RESOURCES	3.5%	3.2%	3.0%	2.9%
13. TOTAL CURRENT REVENUE	41.0%	40.5%	40.1%	39.8%
14. GOVERNMENT FINAL CONSUMPTION EXPENDITURE	15.1%	14.9%	14.7%	14.4%
15. SOCIAL TRANSFERS OTHER THAN IN KIND	16.5 %	16.7%	16.8%	16.8%
16. SUBSIDIES	0.2%	0.1%	0.1%	0.1%
17. INTEREST PAYMENTS	6.1%	5.9%	5.6%	5.2%
18. OTHER CURRENT EXPENDITURE	1.2%	1.2%	1.2%	1.1%
19. GROSS FIXED CAPITAL FORMATION	4.2%	4.2%	4.2%	4.2%
20. TOTAL EXPENDITURE	45.2%	45.0%	44.2%	43.5%

Table 7: General Government Debt Developments

% of GDP	2003	2004	2005	2006
GEN. GOVN CONSOLIDATED GROSS DEBT	101.7%	98.5%	94.6%	90.5%
CHANGE	-3.0%	-3.2%	-3.9%	-4.1%
CONTRIBUTION TO CHANGES IN GENERAL GOVERNMENT CONSOLIDATED GROSS DEBT				
PRIMARY SURPLUS	4.7%	4.7%	5.1%	5.3%
INTEREST	6.1%	5.9%	5.6%	5.2%
NOMINAL GDP	7.6%	7.7%	7.3%	6.9%
OTHER FACTORS AFFECTING THE GENERAL GOVERNMENT CONSOLIDATED DEBT				
ADJUSTMENT FACTORS & PRIVATISATION PROCEEDS	3.0%	2.9%	2.3%	2.1%
IMPLICIT INTEREST RATE (General Government)	6.3%	6.3%	6.0%	5.9%

Given that nominal balances may not accurately reflect the effort for fiscal consolidation, the cyclically adjusted balance is increasingly used as an indicator for fiscal policy. However, it is worth emphasizing that the estimation of cyclically

adjusted balance is subject to much controversy, mainly associated with measurement issues of the output gap and the sensitivity of public finances to the growth of GDP.

By employing the production function approach, we have estimated that in 2003, Greece achieved a cyclically-adjusted primary balance of 4.1% of GDP. However, the cyclically adjusted balance for 2003 is estimated to be 2.0%. In the years ahead, it gradually falls and reaches the level of -0.5% in 2006.

Table 8. Cyclical Adjusted Budget Balance⁽¹⁾

% GDP	2003	2004	2005	2006
1. GDP growth at constant prices	4.0%	4.2%	4.0%	3.8 %
2. Net borrowing	-1.4%	-1.2%	-0.5%	0.0%
3. Interest payments	6.1%	5.9%	5.6%	5.2%
4. Potential GDP growth	3.3%	3.4%	3.4%	3.4%
5. Output gap	1.4%	1.6%	1.4%	1.2%
6. Cyclical budgetary component	0.7%	0.7%	0.6%	0.5%
7. Cyclically-adjusted balance	-2.0%	-1.8%	-1.1%	-0.5%
8. Cyclically-adjusted primary balance	4.1%	4.1%	4.5%	4.6%

(1) Percentages of GDP, the data are based on estimations of the Ministry of Economy and Finance. The estimated output gap used in the above Table differs from that published in the autumn of 2003 by the European Commission. The reason behind this is the difference in the GDP growth and potential growth.

4. Comparison of the 2003 SGP with the 2002 SGP

In this section, we attempt to briefly present and explain the deviations between the present and the 2002 update of the SGP.

Table 9: Divergence from the 2002SGP

% of GDP	2003	2004	2005	2006
REAL GDP GROWTH				
SGP 2002	3.8%	4.0%	3.7%	3.6%
SGP 2003	4.0%	4.2%	4.0%	3.8%
DIFFERENCE	0.2	0.2	0.3	0.2
GENERAL GOVERNMENT BALANCE				
SGP 2002	-0.9%	-0.4%	0.2%	0.6%
SGP 2003	-1.4%	-1.2%	-0.5%	0.0%
DIFFERENCE	-0.5	-0.8	-0.7	-0.6
GENERAL GOVERNMENT GROSS DEBT				
SGP 2002	100.2	96.1	92.1	87.9
SGP 2003	101.7	98.5	94.6	90.5
DIFFERENCE	1.5	2.4	2.5	2.6

1. Real GDP Growth

According to the most recent data and conjectural indicators, the GDP growth in 2003, is estimated to be 4.0 per cent, higher by 0.2 percentage points than initially projected. Public consumption is the main demand component contributing to this increase. The GDP growth projections for 2004-2006, included in the present SGP update, are also higher than those of 2002 SGP by 0.2 – 0.3 percentage points. This revision is due to higher (projected) public expenditures and an expected stronger private consumption, partly due to the impact of the announced social package and also due to a higher positive contribution of the external balance of goods and services as compared with the 2002 SGP. The latter is explained by the fact that the growth prospects for Europe and the World economy are now much more solid than they were in the same period last year, when the 2002 update of the Greek SGP took place.

**Table 10: Factors Influencing GDP Growth
(Differences between SGP 2003 and SGP 2002 in growth rates)**

		2003	2004	2005	2006
GDP	SGP 2002	3.8%	4.0%	3.7%	3.6%
	SGP 2003	4.0%	4.2%	4.0%	3.8%
	DIFFERENCE	0.2	0.2	0.3	0.2
1. PRIVATE CONSUMPTION	SGP 2002	3.1%	3.2%	3.2%	3.0%
	SGP 2003	3.1%	3.2%	3.3%	3.2%
	DIFFERENCE	0.0	0.0	0.1	0.2
2. PUBLIC CONSUMPTION	SGP 2002	-1.5%	0.0%	0.0%	0.0%
	SGP 2003	0.5%	1.0%	0.5%	0.5%
	DIFFERENCE	2.0	1.0	0.5	0.5
3. GROSS FIXED CAPITAL FORMATION	SGP 2002	9.5%	7.0%	6.1%	5.1%
	SGP 2003	9.7%	7.0%	5.7%	5.5%
	DIFFERENCE	0.2	0.0	-0.4	0.4
4. FINAL DOMESTIC DEMAND	SGP 2002	4.0%	3.7%	3.6%	3.2%
	SGP 2003	4.2%	3.8%	3.6%	3.5%
	DIFFERENCE	0.2	0.1	0.0	0.3
5. EXPORTS OF GOODS AND SERVICES	SGP 2002	4.6%	7.6%	6.3%	6.3%
	SGP 2003	1.9%	6.7%	5.6%	5.3%
	DIFFERENCE	-2.7	-0.9	-0.7	1.0
6. IMPORTS OF GOODS AND SERVICES	SGP 2002	4.9%	5.8%	5.2%	4.4%
	SGP 2003	3.0%	4.7%	3.8%	3.7%
	DIFFERENCE	-1.9	-1.1	-1.4	-0.7
7. EXTERNAL BALANCE, (contribution to GDP change)	SGP 2002	-0.45	-0.01	-0.12	0.15
	SGP 2003	-0.49	0.07	0.09	0.10
	DIFFERENCE	-0.04	0.08	0.21	-0.05

2. General Government Balance

In the 2002 SGP, the target for the general government balance in 2003 was a deficit of 0.9 percent of GDP. Now the estimated outturn is 1.4 per cent of GDP. The 0.5 percentage point higher deficit, as explained earlier, is mainly due to overruns of the ordinary state budget expenditures. For the 2004-2005 period, we now project a higher general government deficit as compared to the previous update of the SGP. For 2004, the impact on the budget of the social package along with the higher increases in the wages of civil servants is estimated to be around 0.6 per cent of GDP. More specifically, it is estimated that there will be a higher nominal increase of Social Transfers (9.5 per cent against 7 per cent in the 2002 SPG) and also a higher wage bill increase for the General Government (7.9 per cent against 6 per cent). Finally, the budget for the Olympic Games will be higher than projected in the previous SGP by 0.2 percentage points of GDP. Consequently, the estimated deficit for 2005 is higher

**Table 11: Factors Influencing General Government Balance and Debt
(Differences between SGP 2003 and SGP 2002 in growth rates)**

		2003	2004	2005	2006
1. TOTAL CURRENT RESOURCES	SGP 2002	5.8%	6.2%	6.4%	6.3%
	SGP 2003	5.5%	6.4%	6.3%	6.1%
	DIFFERENCE	-0.3	0.2	-0.1	-0.2
of which					
TAXES ON PRODUCTION AND IMPORTS	SGP 2002	5.8%	7.0%	6.8%	6.7%
	SGP 2003	7.7%	7.7%	7.1%	6.7%
	DIFFERENCE	1.9	0.7	0.3	0.0
TAXES ON INCOME AND WEALTH	SGP 2002	4.9%	5.5%	6.7%	6.5%
	SGP 2003	4.3%	6.0%	5.2%	5.0%
	DIFFERENCE	-0.6	0.5	-1.5	-1.5
SOCIAL CONTRIBUTIONS	SGP 2002	7.3 %	7.3%	7.0%	6.8%
	SGP 2003	7.5%	7.7%	7.3%	7.2%
	DIFFERENCE	0.2	0.4	0.3	0.4
2. TOTAL CURRENT EXPENDITURE	SGP 2002	4.8%	5.6%	5.3%	5.4%
	SGP 2003	6.5%	7.5%	5.6%	5.3%
	DIFFERENCE	0.7	1.9	0.3	-0.1
of which					
GOVERNMENT CONSUMPTION	SGP 2002	2.5%	5.5%	5.0%	4.7%
	SGP 2003	4.5%	6.7%	5.6%	5.0%
	DIFFERENCE	2.0	1.2	0.6	0.3
SOCIAL TRANSFERS THAN IN KIND	SGP 2002	7.7%	7.0%	7.0%	7.0%
	SGP 2003	8.0%	9.5%	7.6%	7.4%
	DIFFERENCE	0.3	2.5	0.6	0.4
INTEREST	SGP 2002	2.2%	1.9%	2.0%	3.3%
	SGP 2003	2.4%	4.3%	1.0%	0.8%
	DIFFERENCE	0.2	2.4	-1.0	-2.5
3. GROSS FIXED CAPITAL FORMATION	SGP 2002	13.0%	9.5%	8.0%	7.0%
	SGP 2003	20.0%	7.0%	8.2%	7.0%
	DIFFERENCE	7.0	-2.5	0.2	0.0
4. CAPITAL TRANSFERS RECEIVED	SGP 2002	4.2%	3.2%	8.0%	9.7%
	SGP 2003	27.6%	29.0%	17.5%	11.7%
	DIFFERENCE	23.4	25.8	9.5	2.0
5. PRIMARY SURPLUS (% GDP)	SGP 2002	4.4%	4.6%	5.0%	5.2%
	SGP 2003	4.7%	4.7%	5.1%	5.3%
	DIFFERENCE	0.3	0.1	0.1	0.1
6. GENERAL GOVERNMENT BALANCE (% GDP)	SGP 2002	-0.9%	-0.4%	0.2%	0.6%
	SGP 2003	-1.4%	-1.2%	-0.5%	0.0%
	DIFFERENCE	2.3	-0.8	-0.8	-0.6
7. GENERAL GOVERNMENT DEBT (% GDP)	SGP 2002	100.2%	96.1%	92.1%	87.9%
	SGP 2003	101.7%	98.5%	94.6%	90.5%
	DIFFERENCE	1.5	2.4	2.5	2.6
8. NOMINAL GDP GROWTH	SGP 2002	7.0%	7.3%	6.8%	6.7%
	SGP 2003	7.6%	7.7%	7.3%	6.9%
	DIFFERENCE	0.6	0.4	0.5	0.2

by 0.5 per cent of GDP, while for 2006 the general government is projected to be in balance. (see table 11)

3. General Government Gross Debt

In the 2003 SGP, the projected general government consolidated gross debt, for the period 2004-2006, is higher than the targets set by the 2002 SGP. These differences are in the area of 2.5 percentage points of GDP for each year, and are due to the projected higher general government deficits.

5. Alternative Growth Scenario

In this section we present a “less optimistic” outlook for the world and European economic activity, and the Greek economy, and compare the projections on the basis of this scenario with the results of the “baseline” scenario. The smaller world GDP assumption influences negatively the Greek exports of goods and services and thus deteriorates the external balance of Greece.

Comparison of the two scenarios is shown in Table 12.

Table 12: Comparison of the Two Alternative Growth Scenarios for the Greek Economy

	Annual Average Rates of Change	Baseline Scenario		Alternative Scenario			
		Annual Average rates of Change	% GDP (except as indicated)		Annual Average rates of Change	% GDP (except as indicated)	
			2003	2006		2006/2003	2003
A. DEMAND AND OUTPUT (CONSTANT PRICES 1995)							
GDP	3.6%	4.0%			3.3%		
PRIVATE CONSUMPTION	2.7%	3.2%			2.9%		
GOVERNMENT CONSUMPTION	1.8%	0.7%			0.7%		
GROSS FIXED CAPITAL FORMATION	8.3%	6.0%			5.0%		
TOTAL DOMESTIC DEMAND	3.7%	3.6%			3.2%		
EXPORTS OF GOODS AND SERVICES	6.4%	5.9%			4.5%		
IMPORTS OF GOODS AND SERVICES	5.9%	4.1%			3.6%		
B. PRICES							
PRIVATE CONSUMPTION DEFLATOR	4.3%	2.8%			2.6%		
GDP DEFLATOR	4.6%	3.2%			3.0%		
MERCHANDISE OF EXPORT PRICES	3.4%	1.9%			1.7%		
MERCHANDISE OF IMPORTS PRICES	3.4%	1.5%			1.5%		
C. PRODUCTIVITY, INCOME AND EMPLOYMENT							
LABOUR PRODUCTIVITY	3.1%	2.6%			2.1%		
REAL COMPENSATION PER EMPLOYEE	3.1%	2.5%			2.2%		
NOMINAL UNIT LABOUR COST	4.3%	2.7%			2.7%		
EMPLOYMENT	0.5%	1.4%			1.2%		
UNEMPLOYED	0.4%	-7.7%			-5.3%		
D. PUBLIC FINANCES							
<i>TOTAL CURRENT RESOURCES OF WHICH</i>			41.0%	39.8%		41.0%	40.2%
DIRECT TAXES	11.3%	5.4%			4.9%		
INDIRECT TAXES	9.1%	7.2%			6.4%		
<i>TOTAL CURRENT EXPENDITURE OF WHICH</i>			39.0%	37.8%		39.0%	38.7%
SOCIAL TRANSFERS OTHER THAN IN KIND	9.6%	8.2%			8.1%		
INTEREST	-1.2%	2.0%			2.3%		
GENERAL GOVERNMENT BALANCE			-1.4%	0.0%		-1.4%	-0.5%
GENERAL GOVERNMENT DEBT			101.7	90.5%		101.7	93.5%
E. CURRENT EXTERNAL TRANSACTIONS							
TRADE BALANCE			-14.5%	-13.6%		-14.5%	-13.9%
CURRENT EXTERNAL BALANCE			-5.8%	-4.2%		-3.8%	-3.4%

The combined effect of the alternative assumptions on economic activity will result to an average annual GDP growth rate, which will be about 0.7 percentage points lower compared to the baseline scenario, while the annual average inflation rate, as measured by the private consumption deflator, is projected to show a small

improvement by 0.2 percentage points, due to a slower, by 0.4 per cent per year, growth of the domestic demand.

Assuming the baseline scenario elasticities of government revenue to GDP, we find that the general government balance improvement will be smaller in the less optimistic scenario and so in 2006, there will be a deficit of 0.5 percent of GDP instead of a balanced position. Hence, the general government consolidated gross debt, as a percentage of GDP, will be higher compared to the baseline scenario by 3.0 percentage points.

6. Budgetary Implications of Structural Reforms

As we have stressed repeatedly the performance of the Greek economy in the coming years will be based not only on strong investment growth but also on a structural reforms program that leads to the strengthening of potential growth. The Greek government is committed to step up reform efforts, aiming at extending and deepening structural reforms in product, capital and labour markets, so as to sustain a strong economic performance, to make the economy more flexible and adjustable to the changing economic conditions, and thus accelerate the process of real convergence with the other EU countries.

In September 2003 the government announced a comprehensive strategy, called the “Convergence Charter”, for accelerating the process of real and social convergence of the Greek economy and society to the average level of its EU partners. The Charter is set within the wider context of the Lisbon Agenda reform program, and aims at boosting productivity and the long-term growth potential of the economy.

In 2003 the government, in addition to the measures already mentioned in the section 3 “Economic Policies for 2004 – 2006” above, introduced new measures, the most important of which are the following:

- Linking unemployment benefits to offering part-time work in social services.
- Expenditures on ALMPs will be doubled as a percent of GDP in the period 2004-2008.
- Tax incentives for investing in training programs
- Tax credits for R&D expenditures
- Part time employment in the Public Sector
- Reduction of the non-wage labor costs
- A number of other measures aimed at enhancing competition in the energy sector, encouraging private investment, facilitating entrepreneurship, promoting regional development, etc.

The budgetary costs of these measures are not very significant and have been taken into account. The area, however, which has already had important effects on government accounts and is expected to influence the reduction of public debt is the

revenues from privatisation. In this area, Greece continued to make significant progress in privatising public enterprises and opening up network industries. Privatisation proceeds in 2002 reached € 2.7 bn, thus topping the list of EU countries (as a ratio to GDP). Approximately the same amount has been raised during the January to October period in 2003. These proceeds (table 13) have been mainly used for the reduction of the general government debt.

Table 13: Privatisation of State-owned Enterprises in 2003

Company	Method of Privatization & % sold	Total amount raised (in m €)
AGNO	Trade sale (99.99%)	12
KAE	Trade sale (40%)	174
Hellenic Petroleum	Trade sale (16.65%)	326
Parnitha Casino (Mont Parnes SA)	Trade sale (49%)	90
Hellenic Industrial Bank	Third installment	70
Football Prognostics Organization (OPAP)	Additional Offering (24.61%)	736
Hellenic Exchanges S.A	Trade sale (33.4%)	89
Piraeus Port Corporation	Initial Public Offering (25%)	55
National Bank of Greece	Trade Sale to institutional investors (11%)	490
Public Power Corporation III	Additional Offering (15.57%)	636
Total		2,678

7. Some Concluding Remarks

In 2003 the Greek economy continued to have a GDP growth rate well above the European average. Unemployment continued to fall, inflation decelerated only slightly, and fiscal consolidation deviated from target by ½ percentage point, mainly because of some slippage on the expenditure side.

The main driving forces of the economic activity were private consumption as well as private and public investment. The contribution of the external sector was slightly negative due mainly to the weak international and particularly European economic activity.

The prospects for the 2004-2006 are quite encouraging since the economic activity is expected to remain buoyant, unemployment is projected to further fall, and inflation is also expected to further decelerate, although it will remain at level higher than the EU average. The recovery of the economic activity in the EU is expected to contribute favourably to the growth prospects of the Greek economy. Fiscal consolidation is projected to speed up after 2004, when the burden of the expenditures for the Olympic Games will be eliminated. The gradual increase of the primary surpluses will contribute to the decline of the public debt as a percentage of GDP. The rapid de-escalation of the public debt is a sine qua non for the Greek economic policy, if the Greek society is to deal effectively with the challenges posed by the ageing of the population.

For the period 2004-2006, the goal of the Greek government is twofold. On the one hand it will seek to maintain an environment of macroeconomic stability and will follow fiscal policies by strictly adhering to the framework set by the Treaty and the Stability and Growth Pact and on the other hand will continue its program of structural reforms, within the spirit of the Lisbon agenda. Further reforms in the product, labour and capital markets will further enhance the productive capacity of the Greek economy and will contribute to the speeding up of the economic and social convergence process.

Appendix

Detailed tables 2002-2006