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GREECE: MACRO FISCAL ASSESSMENT
AN ANALYSIS OF THE JANUARY 2009 UPDATE OF THE STABILITY
PROGRAMME

The Stability and Growth Pact requires each EU Member State to present an annual update of its medium-term budgetary programme, called “stability programme” for countries that have adopted the euro as their currency and “convergence programme” for those that have not.

The attached technical analysis of the programme, prepared by the staff of, and under the responsibility of, the Directorate-General for Economic and Financial Affairs (DG ECFIN) of the European Commission, was finalised on 18 February 2009. Comments should be sent to Georgios Moschovis (george.moschovis@ec.europa.eu). The main aim of the analysis is to assess the realism of the budgetary strategy presented in the programme as well as its compliance with the requirements of the Stability and Growth Pact. However, the analysis also looks at the overall macro-economic performance of the country and highlights relevant policy challenges.

The analysis takes into account (i) the Commission services’ January 2009 interim forecast, (ii) the code of conduct (“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) and (iii) the commonly agreed methodology for the estimation of potential output and cyclically-adjusted balances. Technical issues are explained in an accompanying methodological paper prepared by DG ECFIN.

Based on this technical analysis, the European Commission adopted a recommendation for a Council opinion on the programme on 18 February 2009. The ECOFIN Council is expected to adopt its opinion on the programme on 10 March 2009.

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All these documents, as well as the provisions of the Stability and Growth Pact, can be found on the following website:

http://ec.europa.eu/economy_finance/about/activities/sgp/main_en.htm

1. INTRODUCTION

This document assesses the January 2009 update of the Greece's stability programme. It takes into account all currently available information, notably the Commission services' January 2009 Interim Forecast and the 2009 budget law adopted by Parliament on 21st December 2008. The programme which was submitted on 30 January 2009, covers the period 2008-2011 and builds on the 2009 budget law. The late submission of the programme was due to the recent reshuffle of the Greek government leading to the change of the Minister of Economy and Finance. The programme was approved by the government on 30 January 2009. An addendum to the programme, providing clarifications on changes on the budgeted tax enhancing measures and the planned budgetary process reform, was submitted on 6 February 2009. The addendum does not introduce any change in the fiscal strategy outlined in the programme, while both the macroeconomic scenario and the budgetary projections remained unchanged. Therefore the latter have not been updated relative to the stability programme.

2. MAIN CHALLENGES IN THE ECONOMIC DOWNTURN AND THE POLICY RESPONSE

With growth of 4% on average, the Greek economy has been enjoying buoyant demand-driven activity during the last decade. The cyclical position of the Greek economy has also been improving since the early 2000s, with real GDP growing above potential. Domestic demand has been the most important contributor to GDP growth. Dynamic private consumption, supplemented by public consumption and investment until 2004, when the Olympic Games were held, as well as by private investment (especially dwellings), were funded by the surge in credit growth from the late 1990s. The fall in risk premia was triggered by the European integration and domestic financial liberalisation, while relatively high inflation implied that real interest rates were very low. Moreover, relatively high job creation (1% per year on average), was accompanied by strong productivity growth.

During the same period, although inflation rate was reduced from above 5% in late-1990's to around 3% in 2007, the differential with the euro area remained high at an annual average level of around 1¼ percentage points. This is not only the result of the so-called Balassa-Samuelson effect, associated with catching-up economies, but also of structural factors linked to the malfunctioning of domestic markets¹ (especially in the sheltered sectors of the economy, such as the services sector). Nominal wage growth has been outpacing productivity gains, pushing up unit labour costs and eroding the competitiveness of the Greek economy with respect to the rest of the euro area. The combination of high economic growth, persistent fiscal imbalances and deteriorating competitiveness in the last decade has worsened the external balance of the Greek economy, with the external deficit gradually rising to well above 10% of GDP and exceeding 12% of GDP in 2007, from a close-to-balance position in the mid-1990s.

¹ ECB (2005).

Against this background, the economy decelerated in 2008 and, in the light of the ongoing global financial crisis, is expected to slow down strongly in 2009. Albeit remaining in positive territory for the year as a whole, economic growth will be sluggish and exclusively driven by domestic demand. In a context of uncertainty in global markets, tightening credit conditions should put a brake on private consumption growth, while investment should contract further. Some signs of a weak recovery are foreseen in 2010. The strong slowdown translates also into deteriorating labour market conditions, where, after having stood at an average 8% in 2007, the unemployment rate is expected to exceed 9% in 2009.

In spite of the high growth rates in the recent past, the general government deficit remained on average well above 3% of GDP over the whole period (with a maximum of 7½% of GDP in 2004), in spite of the significant fiscal adjustment in 2005 that cut the budget deficit to 2¾% in 2006² and reduced the structural balance, (i.e. the cyclically-adjusted-balance net of one-offs and other temporary measures) by 3½ percentage points of GDP. In 2007 however, the fiscal stance eased mainly on account of current primary expenditure slippages and, in spite of still good economic times, the general government deficit exceeded 3% of GDP, while the structural balance deteriorated by a ¼ percentage point of GDP. Together with large debt-increasing below-the-line operations, high deficits contributed to the accumulation of public debt, which at almost 94% of GDP in 2008 is the second highest in the EU.

Reflecting to some extent the economic downturn, the Greek public finances are expected to deteriorate further in the medium term. After staying above 3% of GDP also in 2008 due to fiscal slippages, the Commission services' January 2009 interim forecast projects the deficit to reach 3¾% of GDP in 2009 and exceed 4% of GDP in 2010, assuming the discontinuation of revenue enhancing one-off measures adopted for 2009. Moreover, public finances are potentially burdened by the comprehensive banking sector support package, notified by the Greek government on 14 November 2008. The implicit liabilities of this support package might put further pressure on debt developments in the coming years, which is already projected to increase to 98½% of GDP by 2010.

The Greek government has not adopted a short-term stimulus package in response to the economic slowdown which, in view of the large economic imbalances, would be in line with the EERP. This was also confirmed by the addendum. The programme foresees a number of structural measures without direct budgetary impact, such as those aimed at sustaining employment, and in particular youth and women employment, enhancing business investment via private-public partnerships, boosting lending to SMEs and improving EU funds absorption. It envisages also a number of temporary sectoral specific measures, in particular in the tourism sector, in order to support the industry in view of the coming tourism season. The update also includes a series of structural reform measures, which are part of the longer-term strategy for improving the quality and sustainability of public finances, such as the reform in the public expenditure management and control and the implementation of the recently adopted pension reform. These measures are related to the medium-term reform agenda and the country-specific

² Council Decision 2007/465/EC 7 June 2007 abrogating Decision 2004/917/EC on the existence of an excessive deficit in Greece.

recommendations proposed by the Commission on 28 January 2009 under the Lisbon Strategy for Growth and Jobs.

At this juncture, Greece faces the challenge to address timely and effectively the widening structural imbalances of the economy and to reverse the upward trend of public debt. Strengthening the fiscal consolidation path, based on permanent measures to control current primary expenditure including public wages, would be one precondition to achieve sound and sustainable public finances in Greece. Moreover, further actions are necessary to support policies to improve the quality of public finances. The structural nature of the factors underlying competitiveness losses and the widening external imbalances urgently requires the implementation of bold structural reforms. In the long term, the level of debt coupled with the projected increase in age-related spending, will also affect negatively the long term sustainability of public finances, which remains at high risk.

3. MACROECONOMIC SCENARIO

The programme projects real GDP growth to slow from 3% in 2008 to 1.1% in 2009 and recover mildly afterwards, reaching 2.3% in 2011. The downturn in 2009 would be mainly triggered by weakening domestic demand and lower export growth, whereas the mild recovery from 2010 onwards would be driven by stronger domestic demand and a slight pick-up in exports.

The programme foresees domestic demand to decelerate strongly in 2009, though still remaining the main driver of growth, underpinned by relatively resilient private consumption, supported by strong real wages growth and prices moderation. In contrast, private investment is foreseen to contract in 2009, after high growth rates recorded in the recent past. Public investment in turn, fuelled mainly by the acceleration of projects under the 3rd Community Support Framework and the implementation of planned PPPs (public-private partnerships), is expected to keep last year's dynamism. The deteriorating economic outlook in Greece's main trading partners will have an impact on merchandise exports, which are foreseen to decelerate strongly in 2009. Transportation and tourism services, which have exhibited considerable resilience in 2008, are also expected to suffer from the repercussions of the crisis. With imports following the trends of slowing domestic demand, the external sector's contribution to growth is projected to be broadly neutral over the programme period.

According to the programme, the economic slowdown in 2009 would imply temporarily slower employment growth, whereas unemployment is set to remain broadly unchanged, on the back of policy initiatives and structural reforms in the labour market. Inflationary pressures are projected to ease smoothly in 2009 and 2010.

The programme's growth projections are more favourable than the Commission services' January 2009 interim forecast. The Commission services' forecast expects a deeper and more protracted economic downturn, with real GDP growing below potential in 2010. In addition, according to the Commission services' forecast, labour market developments are less favourable, so that the outlook for private consumption growth is more subdued than envisaged in the programme. Together with a more moderate expansion of world trade, the Commission services also project a slower recovery of investment.

Given the accelerating decline in economic activity in a growing number of Greece's trading partners and the weakening international trade prospects, the current global downturn may turn out more severe and drawn-out than foreseen in the update. This would entail considerable downside risks to the macroeconomic scenario of the programme, reflecting mainly the performance of the shipping and tourism sector's vulnerability.

Finally, the programme's projections for inflation appear to be realistic, while the evolution of the external imbalances in the medium term is somewhat favourable.

Table I: Comparison of macroeconomic developments and forecasts

| | 2008 | | 2009 | | 2010 | | 2011 |
|--|-------|-------|-------|-------|-------|-------|-------|
| | COM | SP | COM | SP | COM | SP | SP |
| Real GDP (% change) | 2.9 | 3.0 | 0.2 | 1.1 | 0.7 | 1.6 | 2.3 |
| Private consumption (% change) | 2.4 | 2.3 | 0.7 | 1.9 | 0.7 | 2.0 | 2.1 |
| Gross fixed capital formation (% change) | -0.5 | -8.9 | -2.8 | -0.5 | -0.1 | 3.0 | 3.5 |
| Exports of goods and services (% change) | 3.7 | 3.9 | -1.5 | 1.5 | 0.8 | 2.5 | 3.3 |
| Imports of goods and services (% change) | -0.2 | 0.4 | -0.9 | -1.8 | 1.1 | 2.2 | 2.6 |
| <i>Contributions to real GDP growth:</i> | | | | | | | |
| - Final domestic demand | 2.1 | 0.3 | 0.3 | 1.8 | 0.9 | 2.2 | 2.4 |
| - Change in inventories | -0.1 | 1.9 | 0.0 | -1.7 | 0.0 | -0.5 | 0.0 |
| - Net exports | 1.0 | 0.8 | 0.0 | 1.0 | -0.2 | -0.2 | -0.1 |
| Output gap ¹ | 2.8 | 1.9 | 0.5 | 0.3 | -1.2 | -0.8 | -1.0 |
| Employment (% change) | 0.8 | 1.1 | -0.1 | 0.2 | 0.2 | 0.6 | 0.7 |
| Unemployment rate (%) | 8.3 | 7.5 | 9.0 | 8.0 | 9.4 | 8.0 | 7.9 |
| Labour productivity (% change) | 2.1 | 1.9 | 0.3 | 0.9 | 0.5 | 1.0 | 1.6 |
| HICP inflation (%) | 4.3 | 4.3 | 2.5 | 2.6 | 2.7 | 2.5 | 2.4 |
| GDP deflator (% change) | 4.2 | 4.3 | 3.1 | 2.7 | 2.7 | 2.6 | 2.5 |
| Comp. of employees (per head, % change) | 7.6 | 7.6 | 6.7 | 6.1 | 6.3 | 3.4 | 3.5 |
| Net lending/borrowing vis-à-vis the rest of the world (% of GDP) | -11.7 | -12.8 | -11.2 | -11.4 | -11.6 | -10.8 | -10.0 |
| <u>Note:</u> | | | | | | | |
| ¹ In percent of potential GDP, with potential GDP growth according to the programme as recalculated by Commission services. | | | | | | | |
| <u>Source:</u> | | | | | | | |
| Commission services' January 2009 interim forecasts (COM); Stability programme (SP) | | | | | | | |

4. BUDGETARY STRATEGY

4.1. Budgetary implementation in 2008

According to data notified by the Greek authorities in October 2008³ and validated by Eurostat⁴, the general government deficit reached 3.5% of GDP in 2007, thus exceeding the 3% of GDP reference value. More specifically, Greece notified a general government deficit of 3.5% of GDP in 2007, revised upwards from 2.7% of GDP. This upward revision created a base-effect, carrying over the worse starting point in 2008. Thus, the budgetary figures presented in the December 2007 update concerning the general government deficit in 2007 and the budgetary target for 2008, are not directly comparable with the current year's update.

For 2008, the general government deficit is estimated at 3.7% of GDP in the update (including 0.4% of GDP deficit-decreasing one-off measures), which is ¼ of a percentage point higher than the projection in the Commission services' January 2009 interim forecast. This compares with a target of 1.6% of GDP set in the previous update. The deviation of 2 percentage points reflects both revenue shortfalls and expenditure overruns. On the one hand, revenue is estimated at about 1 percentage point of GDP lower than budgeted, stemming from the lower-than-expected yield of the revenue-enhancing measures implemented in 2008. On the other hand, expenditure overruns amount to around another 1 percentage point of GDP, reflecting mainly primary current expenditure slippages and, in particular, higher-than-expected public consumption and wages.

The impact of the global financial crisis on the 2008 budget balance has been limited, as the Greek government has neither implemented any fiscal stimulus in 2008, nor any financial sector rescue operations, as have not been needed.

4.2. Near-term budgetary strategy

According to the update, the deficit target for 2009 is set at 3.7% of GDP (including ½% of GDP one-offs), revised upwards by 1¾% percentage points of GDP, compared with the target set in the 2009 budget law, which was approved by the Parliament on 21 December 2008. Thus, the general government deficit is projected to remain broadly unchanged in 2009, compared with the outturn of 2008. The new budgetary target takes into account the more recent information on budgetary implementation in 2008, which ceteris paribus should lead to a more pronounced worsening of the general government deficit in 2009. It also reflects a more prudent projection for total revenue, which is revised downwards by 1 percentage point of GDP, compared with the 2009 budget target.

³ 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.

⁴ News Release 147/2008 of 22 October 2008 on the provision of data for the excessive deficit procedure.

More specifically, the revised revenue target estimates direct taxes to be less than the initial target by 0.2 percentage points of GDP, mainly due to lower corporate profitability in 2008, 0.6 percentage points of GDP less indirect taxes than initially targeted, due to strong deceleration in consumption and an increase in VAT tax refunds by 0.2 percentage points of GDP.

The revenue ratio is still projected to grow by almost 1 percentage point of GDP in 2009 compared with the 2008 outturn, on the back of the tax revenue-enhancing package adopted in September 2008 and included in the 2009 budget law. Part of this package however, was modified by the Greek authorities in the addendum received on 6 February. More specifically, the Greek government will abolish the tax bracket for self-employed introduced in September 2008 and the tax-free threshold for income up to € 10,500 is restored. In order to compensate for the corresponding loss in revenue (which according to the addendum is estimated at 0.2% of GDP), the excise tax on cigarettes and alcoholic beverages will be increased. According to the addendum, the budgetary impact of these changes will be broadly neutral. Changes are also introduced in the unified property tax scheme adopted in 2008, in order to facilitate its implementation and render it simpler and fair (calculated in function of the legal value of dwellings, instead of the surface). According to the addendum, the budgetary impact of these changes will be neutral.

According to the programme and the addendum, almost half of the overall increase in total revenues projected in 2009 ($\frac{1}{2}\%$ out of 1% of GDP) consists of temporary measures (tax settlement, including the collection of delinquent obligations to the state). In particular, the revenue-to-GDP ratio is expected to increase to 41% of GDP compared with 40% in 2008, supported by an increase in the advance payment rate for enterprises from 65% to 80%, the introduction of a new tax on dividends and capital gains from selling stocks, the imposition of a new tax on stock options and an increase in excise duties on tobacco and alcohol. As a result, taxes on production and imports are projected to rise by $\frac{1}{2}$ percentage points of GDP, while current taxes on income and wealth are also expected to record an increase of $1\frac{1}{2}$ percentage points of GDP. Part of the overall increase in tax revenues will be offset by a fall in other revenues of almost 1 percentage point of GDP, for which the programme does not provide any information.

Table II. Main budgetary measures for 2009

| Revenue measures ¹ | Expenditure measures ² |
|---|--|
| Measures in response to the downturn | |
| | <ul style="list-style-type: none"> • Ad hoc Social Cohesion benefits to low income pensioners and registered unemployed. • Ad hoc housing benefit to registered unemployed on mortgage (housing loan taken before 2009) • Twofold increase in the Easter bonus for registered unemployed <p>All above mentioned measures are financed through the National Fund for Social Cohesion (0.2% of GDP)</p> |
| Other measures | |
| <ul style="list-style-type: none"> • Increase in the excise duties of tobacco and alcohol (0.15% of GDP) • Increase in the advance payment rate for enterprises to 80% from 65% (0.15% of GDP). • The introduction of a tax rate of 10% on dividends; the same rate holds for capital gains from selling stocks (<0.1% of GDP). • The introduction of a new tax on stock options, in line with rules pertaining to wage income (<0.1% GDP). • Tax settlement (0.5% of GDP) | |
| <p>Note: 1 Estimated impact on general government revenue 2 Estimated impact on general government expenditure Source: Commission services and 2009 Budget Law</p> | |

Total expenditure is projected in the programme to increase by 1 percentage points of GDP in 2009, implying an upward revision of 0.4% of GDP, compared with the 2009 budget target. More specifically, the expenditure-to-GDP ratio is projected to rise to 44.7% of GDP, compared with 43.7% of GDP in 2008. Public wages and social transfers are set to rise by $\frac{3}{4}$ and $\frac{1}{2}$ of a percentage point of GDP respectively, partly due to the adoption of a social welfare package, which had already been included in the budget, consisted mainly of allowances to the old-age pensioners and unemployed. Interest expenditure is also projected to increase by some $\frac{1}{2}$ of a percentage point of GDP, stemming from the rising debt servicing costs, also reflected by the rising spreads of government bond yields. Capital and other expenditure in turn, are projected to decline by $\frac{1}{4}$ and $\frac{1}{2}$ of percentage point of GDP respectively.

To ensure meeting the revised targets, the update envisages a number of measures, on top of those included in the 2009 budget law, aiming at constraining primary expenditure and rationalizing the public expenditure management. More specifically, the programme envisages a prudent public wages policy, limited number of new hiring in the public sector and better public wages management, through the establishment of a central wage payments authority. Moreover, a revision of the public sector's high-level officials' remuneration scheme is planned, with the imposition of a ceiling at the level of the

Ministry Secretary General's salary. In addition, a temporary 10% cut will be imposed on expenditure for fixed-term employment in the public sector, only in 2009. These measures will be coupled by another 10% cut in the elastic expenditures of the public sector, with particular emphasis in travel and public relations expenses, overtime remuneration etc.

However, although the addendum confirms these measures and provides some clarifications, it states that savings from these measures have not been included in the fiscal projections of the programme and will be used as buffers, to ensure that the budgetary targets are achieved, against potential adverse economic developments. Moreover, it does not provide any information on the implementation framework and a timeframe of adoption, since most of these measures should be legislated and passed a parliamentary process.

Table III: Composition of the budgetary adjustment

| (% of GDP) | 2007 | 2008 | | 2009 | | 2010 | | 2011 | Change: 2008-2011 |
|---|-------------|-------------|-------------|-------------|-------------|------------------|-------------|-------------|----------------------|
| | COM | COM | SP | COM | SP | COM ¹ | SP | SP | SP |
| Revenue | 40.0 | 39.9 | 40.0 | 40.8 | 41.0 | 40.0 | 41.1 | 41.2 | 1.2 |
| <i>of which:</i> | | | | | | | | | |
| - Taxes on production and imports | 12.1 | 12.0 | 11.9 | 12.3 | 12.3 | 12.3 | 12.4 | 12.4 | 0.5 |
| - Current taxes on income, wealth, etc. | 7.9 | 7.9 | 7.8 | 8.7 | 9.3 | 8.2 | 9.0 | 9.0 | 1.2 |
| - Social contributions | 13.9 | 14.2 | 14.2 | 14.6 | 14.2 | 14.8 | 14.2 | 14.2 | 0.0 |
| - Other (residual) | 6.0 | 5.8 | 6.1 | 5.2 | 5.2 | 4.8 | 5.5 | 5.6 | -0.5 |
| Expenditure | 43.4 | 43.4 | 43.7 | 44.5 | 44.7 | 44.2 | 44.3 | 43.8 | 0.1 |
| <i>of which:</i> | | | | | | | | | |
| - Primary expenditure | 39.4 | 39.4 | 39.7 | 40.3 | 40.2 | 40.0 | 39.9 | 39.5 | -0.2 |
| <i>of which:</i> | | | | | | | | | |
| Compensation of employees | 11.0 | 11.3 | 11.3 | 11.7 | 12.0 | 11.7 | 11.9 | 11.7 | 0.4 |
| Intermediate consumption | 5.2 | 4.9 | 5.0 | 4.6 | 5.0 | 4.6 | 4.9 | 4.9 | -0.1 |
| Social payments | 17.2 | 17.9 | 18.0 | 18.8 | 18.6 | 18.7 | 18.6 | 18.6 | 0.6 |
| Subsidies | 0.1 | 0.1 | 0.1 | 0.1 | 0.1 | 0.1 | 0.1 | 0.1 | 0.0 |
| Gross fixed capital formation | 3.0 | 3.0 | 3.0 | 2.6 | 2.7 | 2.6 | 2.7 | 2.7 | -0.3 |
| Other (residual) | 2.9 | 2.2 | 2.3 | 2.4 | 1.8 | 2.4 | 1.9 | 1.7 | -0.6 |
| - Interest expenditure | 4.1 | 4.0 | 4.0 | 4.2 | 4.5 | 4.1 | 4.4 | 4.3 | 0.3 |
| General government balance (GGB) | -3.5 | -3.4 | -3.7 | -3.7 | -3.7 | -4.2 | -3.2 | -2.6 | 1.1 |
| Primary balance | 0.6 | 0.6 | 0.3 | 0.6 | 0.8 | 0.0 | 1.2 | 1.7 | 1.4 |
| One-off and other temporary measures | -0.2 | 0.4 | 0.4 | 0.8 | 0.5 | 0.0 | 0.0 | 0.0 | -0.4 |
| GGB excl. one-offs | -3.3 | -3.8 | -4.1 | -4.4 | -4.2 | -4.2 | -3.2 | -2.6 | 1.5 |
| Output gap ² | 3.0 | 2.8 | 1.9 | 0.5 | 0.3 | -1.2 | -0.8 | -1.0 | -2.9 |
| Cyclically-adjusted balance ² | -4.8 | -4.7 | -4.5 | -3.9 | -3.8 | -3.7 | -2.8 | -2.2 | 2.4 |
| Structural balance³ | -4.6 | -5.0 | -4.5 | -4.7 | -4.3 | -3.7 | -2.8 | -2.2 | 2.4 |
| <i>Change in structural balance</i> | | -0.5 | 0.1 | 0.4 | 0.2 | 1.0 | 1.5 | 0.7 | |
| Structural primary balance ³ | -0.5 | -1.0 | -0.5 | -0.4 | 0.2 | 0.5 | 1.6 | 2.1 | 2.7 |
| <i>Change in structural primary balance</i> | | -0.5 | 0.0 | 0.6 | 0.7 | 0.9 | 1.4 | 0.6 | |
| Notes: | | | | | | | | | |
| ¹ On a no-policy-change basis. | | | | | | | | | |
| ² Output gap (in % of potential GDP) and cyclically-adjusted balance according to the programme as recalculated by Commission services on the basis of the information in the programme. | | | | | | | | | |
| ³ Structural (primary) balance = cyclically-adjusted (primary) balance excluding one-off and other temporary measures. | | | | | | | | | |
| Source: | | | | | | | | | |
| Stability programme (SP); Commission services' January 2009 interim forecasts (COM); Commission services' calculations | | | | | | | | | |

4.3. Medium-term budgetary strategy

The budgetary strategy outlined in the programme and confirmed in the addendum, aims at reducing the structural deficit from 4.5% of GDP in 2008 to 4.3% in 2009 and 2.2% by 2011, while the medium term objective (MTO) of a balanced budget in structural terms (i.e. in cyclically-adjusted terms net of one-off and other temporary measures) is not projected to be attained within the programme horizon. After targeting 3.7% of GDP in 2009, the headline deficit will decline over the programme period to 3.2% of GDP in 2010 and 2.6% by 2011. Similarly, the primary balance will reach a surplus of 1.7% of GDP by 2011, which compares with 0.8% in 2009. In structural terms, this would amount to an improvement of $\frac{3}{4}$ percentage points of GDP on average. Budgetary consolidation is mainly based on an ambitious expenditure retrenchment, which is however, not backed with concrete measures.

According to the programme, fiscal policy is geared towards restoring investor confidence and addressing the existing macroeconomic imbalances. The Greek government has not adopted a short-term stimulus package in response to the economic slowdown which, in view of the large economic imbalances, would be in line with the EERP. Apart from the strong commitment and the clear indication of the Greek government's intentions, the medium-term budgetary strategy outlined in the programme is not supported by measures or any sufficient information on specific policies. Taken as such however, it points to a mainly expenditure-based consolidation, as the expenditure-to-GDP ratio would be reduced by 1 percentage points of GDP by 2011, whereas the revenue-to-GDP ratio would rise by only $\frac{1}{4}$ of a percentage point of GDP. Nevertheless, the envisaged back-loaded cuts in some expenditure categories appear very ambitious.

The new programme does not revise the medium term objective (MTO) of a balanced budget in structural terms (i.e. in cyclically-adjusted terms net of one-off and other temporary measures). The programme however, does not specify the target year for attaining the MTO.

4.4. Risks to the budgetary targets

The budgetary outcomes are subject to significant downside risks. In particular, the underlying macroeconomic scenario is based on favourable growth assumptions. Risks are also linked to possible slippages in the implementation of the revised 2009 budgetary target, especially when taking into account track record of recurrent expenditure overruns and revenue shortfalls.

Total revenue in 2009 is projected to increase by 1 percentage point of GDP. However, this may not be a plausible development, in the light of a weaker economic environment and strongly decelerating economic activity. In addition, the delays in implementing the revenue enhancing measures included in the 2009 budget and the reliance to a significant extent, on the results from the fight against tax evasion, which is only partly supported by reforms in tax administration, pose further downside risks to achieving the target.

Total expenditure in turn, is foreseen to rise by 1 percentage point in 2009, although the Greek government has not adopted a short-term stimulus package. The main risk associated to this projection is the lack of sufficient institutional anchor for all levels of the budgetary authorities to pursue expenditure discipline and ensure fiscal prudence.

From 2010 onwards, significant risks stem from the lack of information on the measures to support the envisaged consolidation, particularly on the expenditure side and the marked reliance on expenditure restraint, for instance in the area of current primary spending. Moreover, the economic outlook appears to be somewhat favourable with a slightly more marked recovery in 2010, than projected by the Commission Services' forecast. Finally, there are risks related to the debt servicing expenditures, as the spread between Greek and German government bond yields, has been constantly on the increase since autumn 2008, exceeding already the historical levels since the euro-adoption by Greece.

Overall, there are considerable downside risks due to the structural weaknesses of the overall Greek budgetary system. Revenue outcome could be worse than targeted, while the consolidation strategy outlined in the programme after 2009 is not sufficiently backed by measures.

5. DEBT DEVELOPMENTS AND LONG-TERM SUSTAINABILITY

5.1. Debt developments

Government gross debt, estimated at 94.6% of GDP in 2008, is projected in the programme to exceed 96% of GDP in 2009 and 2010, before returning to 94¾% in 2011, thus still remaining well above the 60% of GDP reference value. According to the update, the combined effect of still positive primary balance and relatively resilient nominal GDP growth would be the main driving forces behind the projected path of debt-reduction after 2009.

The programme's target for the debt-to-GDP ratio in 2009 is more favourable than the Commission services' January 2009 interim forecast. In parallel, while the SFA (stock-flow adjustment) are still high, the programme does not give information on their composition. Experience shows that debt targets have been persistently missed in successive programmes, not only because of deficit slippages, but also due to the underestimation of SFA. In the case of Greece in particular, large SFA in the past, have been an indication of upward deficit revisions ex-post.

According to the programme, the further decline in the debt ratio in 2010 and 2011 would be mainly driven by the targeted primary deficits, whereas stock-flow adjustments would shrink. However, a positive snow-ball effect due to a weakening growth effect and to a lesser extent, due to increasing interest expenditure, mirrored also by the rising spread between Greek and German government bond yields and the implied re-pricing of risks, puts further pressure on the debt burden and decelerates the speed of decline in both years.

Risks associated with the projected evolution of the debt-to-GDP ratio also appear to be on the upside, stemming from the risks attached to the deficit projections. These risks

may be compounded by uncertainty about the stock-flow adjustment. In addition, possible debt increasing financial transactions within the framework of the financial sector support package may put further upward pressure to the debt-to-GDP ratio, in particular the securities scheme share of the package (see box). However, with no reference to this financial package, the programme does not take into account its potential impact on the debt developments.

In view of the risk assessment, debt would increase and remain well above the reference value of 60% throughout the update horizon and cannot be considered as sufficiently diminishing.

Box: Support package for Greek credit institutions

On 14 November 2008, the Greek authorities notified to the European Commission a package of measures designed to stabilise the financial markets. The package consists of:

- A recapitalisation scheme, making available new capital to credit institutions in exchange of preferential shares, to allow them to strengthen their capital base against potential losses. The State will purchase preference shares which are considered as non core tier 1 capital and will be remunerated with 10 % interest.
- A guarantee scheme, covering against remuneration new debt with a maturity between three months and three years, issued during maximum six months after 19 November 2008. Subordinated debt and interbank deposits are excluded from the scheme. The remuneration is aligned with the ECB recommendations.
- A securities scheme, providing against remuneration government bonds to eligible credit institutions to enhance their access to liquidity in particular with the ECB. The bonds are borrowed by the credit institutions against collateral, which has been subject to significant haircuts and against a fee similar to that of the guarantee.

The scheme provides for non-discriminatory access, as it is open to all credit institutions licensed in Greece. It is limited in time and scope, with entry windows of maximum six months and budget caps. It requires beneficiaries to pay a market-oriented remuneration. The measures target only financially sound companies; the provision of guarantees and capital and bond allocations are based on solvency and capital ratio requirements.

Table IV: Debt dynamics

| (% of GDP) | average 2002-06 | 2007 | 2008 | | 2009 | | 2010 | | 2011 |
|-------------------------------------|--------------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|
| | | | COM | SP | COM | SP | COM | SP | SP |
| Gross debt ratio¹ | 98.5 | 94.8 | 94.0 | 94.6 | 96.2 | 96.3 | 98.4 | 96.1 | 94.7 |
| Change in the ratio | -1.4 | -1.0 | -0.9 | -0.2 | 2.2 | 1.7 | 2.3 | -0.2 | -1.4 |
| <i>Contributions²:</i> | | | | | | | | | |
| 1. Primary balance | 0.4 | -0.6 | -0.6 | -0.3 | -0.6 | -0.8 | 0.0 | -1.2 | -1.7 |
| 2. “Snow-ball” effect | -2.3 | -2.1 | -2.3 | -2.4 | 1.2 | 1.1 | 1.0 | 0.6 | -0.1 |
| <i>Of which:</i> | | | | | | | | | |
| Interest expenditure | 4.8 | 4.1 | 4.0 | 4.0 | 4.2 | 4.5 | 4.1 | 4.4 | 4.3 |
| Growth effect | -3.9 | -3.6 | -2.6 | -2.6 | -0.2 | -1.0 | -0.6 | -1.5 | -2.1 |
| Inflation effect | -3.1 | -2.6 | -3.7 | -3.8 | -2.8 | -2.4 | -2.5 | -2.4 | -2.3 |
| 3. Stock-flow adjustment | 0.6 | 1.8 | 2.1 | 2.6 | 1.6 | 1.5 | 1.2 | 0.5 | 0.5 |
| <i>Of which:</i> | | | | | | | | | |
| Cash/accruals diff. | 0.5 | 1.3 | | n.a. | | n.a. | | n.a. | n.a. |
| Acc. financial assets | 0.0 | 0.5 | | n.a. | | n.a. | | n.a. | n.a. |
| <i>Privatisation</i> | -0.8 | -0.7 | | n.a. | | n.a. | | n.a. | n.a. |
| Val. effect & residual | 0.0 | 0.0 | | n.a. | | n.a. | | n.a. | n.a. |

Notes:
¹End of period.
²The snow-ball effect captures the impact of interest expenditure on accumulated debt, as well as the impact of real GDP growth and inflation on the debt ratio (through the denominator). The stock-flow adjustment includes differences in cash and accrual accounting, accumulation of financial assets and valuation and other residual effects.

Source:
Stability programme (SP); Commission services’ January 2009 interim forecasts (COM); Commission services’ calculations

5.2. Long-term debt projections and the sustainability of public finances

This section presents sustainability indicators based on the long-term age-related government spending as projected by the Member States and the EPC in 2006 according to an agreed methodology. The projected increase in age-related spending in Greece is not comparable with the other Member States, since projections for pension expenditure and on long-term care expenditure were not available in the Ageing Report.⁵

Table 4 in the Annex shows that the projected increase in age-related spending, excluding pensions, is rising by 1.5% of GDP between 2010 and 2050. The programme mentions the current process of updating of the common EPC projections, this time including pension and long-term care projections. The updated projections are not finally validated by the EPC, but indicate that the increase in pension expenditure in Greece will be significantly above the EU average.

⁵ Economic Policy Committee and the European Commission (2006), 'The impact of aging on public expenditure: projections for the EU-25 Member States on pensions, health care, long-term care, education and unemployment transfers (2004-50)', *European Economy – Special Report No. 1/2006*. European Commission (2006), 'The long-term sustainability of public finances in the European Union', *European Economy No. 4/2006*. European Commission (2008), *Public finances in EMU – 2008*, *European Economy No. 4/2008*.

Sustainability indicators for two scenarios are presented in Table 5 in the Annex. Since the increase in the cost of ageing is severely underestimated, it is useful to look at the sub-indicator "initial budgetary position" (IBP) only. Excluding the increase of age-related expenditure and assuming that the structural primary balance remained at its 2008 level, the IBP-component of the sustainability gap (S2)⁶ would amount to 2.9% of GDP; almost 2½ percentage points more than in last year's assessment, which is due to a lower estimated structural primary balance in the starting year. The starting budgetary position is not sufficient to stabilize the debt ratio over the long-term and entails a risk of unsustainable public finances even before considering the long-term budgetary impact of ageing.

In contrast to the "2008 scenario", which reflects the weakening of the budgetary position in response to the current economic crisis, the "programme scenario", which is based on the end-of-programme structural primary balance, shows a smaller gap based on the IBP. If the budgetary consolidation planned in the programme was achieved, risks to long-term sustainability of public finances would be slightly mitigated, though the increase in the cost of ageing will remain substantial.

For an overall assessment of the sustainability of public finances, other relevant factors are taken into account, as shown in Table 6 in the Annex. This concerns in particular the current debt ratio, which exceeds the Treaty reference value by far.

The long-term budgetary impact of ageing is likely to be well above the EU average, as indicated by the long-term projections of pension expenditure, which are under preparation according to the commonly agreed method. The budgetary position in 2008 as estimated in the programme, which is worse than the starting position of the previous programme, would compound the long-term budgetary impact of an ageing population. Moreover, the current level of gross debt is well above the Treaty reference value. Reducing it requires achieving high primary surpluses for a long period of time. Achieving higher primary surpluses over the medium term, as already foreseen in the programme, and reforming the pension system aiming at containing the likely significant increase in age-related expenditures would contribute to reducing the high risks to the long-term sustainability of public finances.

6. INSTITUTIONAL FEATURE OF PUBLIC FINANCES

The medium-term budgetary framework in Greece remains weak, characterised by a poor track record. Fiscal developments reflect insufficient control of public expenditure, while revenue projections have proven to be systematically overoptimistic. Moreover, structural and endemic problems related to the recording of Greek government accounts in the

⁶ The S2 indicator is defined as the change in the current level of the structural primary balance required to make sure that the discounted value of future structural primary balances (including the path of property income) covers the current level of debt.

recent past, have also been detrimental for timely and effective revenue and expenditure control.

The programme envisages the continuation of the ongoing budgetary reform and further progress with the implementation of programme budgeting, with a view to improving the public expenditure monitoring and management, increasing transparency and introducing a multi-year planning perspective in the budgetary process. In particular, the Executive Summary of the report “Program Budgeting 2009”, annexed to the addendum, considers programme budgeting as a very important institutional reform, which is planned to be fully implemented by 2012 at the earliest.

Although the on-going reforms touch several aspects of the budget process, the key goal to introduce a new philosophy of public finance management and make the budget a strategic tool for better fiscal governance may not be fully fulfilled, since the scope of the reform is limited (see Annex 1 for the details). The reform only tackles procedural aspects of the budget process, mainly in its preparation phase. Moreover, it is not clear whether any binding expenditure, fiscal rules or ceilings would be introduced in the reformed budgetary system, alongside a timely and regular monitoring mechanism. Expenditure ceilings would facilitate a top-down procedure in the preparation phase of the budget and would allow the medium-term budgetary impact of policy decisions to be fully taken into account. In addition, they would increase the control of the government on public expenditure management, and thus prevent fiscal slippages. However, in the absence of any kind of fiscal ceilings, the risk of fiscal slippages remains.

Despite its limitations, the ongoing reform can improve to some extent the transparency and accountability of public finances. It can also contribute to rationalise public spending and improve the quality and composition of government expenditure, with a positive impact on economic efficiency. But the feasibility of the ongoing and planned measures will depend on the extent to which the existing rigidities in the Greek fiscal system can be successfully overcome.

7. ASSESSMENT

This section assesses the budgetary strategy, taking into account risks, in the light of (i) the criteria for short-term action laid down in the Commission Communication of 26 November 2008 on the European Economic Recovery Plan (EERP) as endorsed by the European Council conclusions on the European Economic Recovery Plan (EERP) on 26 December 2008; (ii) the adequacy of the fiscal stimulus package and the overall fiscal stance (iii) the objectives of the Stability and Growth Pact.

With the general government deficit having remained above the 3% of GDP threshold since 2007, and one of the highest public debts in the EU, Greece has no room for fiscal impulse, so as not to jeopardise further the long-term sustainability of public finances and the competitiveness position of the country. In addition the impact of the ongoing global economic and financial crisis on the Greek economy, mirrored also by the rising spread between Greek and German government bond yields, and the implied re-pricing of risks put further pressure on the debt burden. Therefore, the Greek government has not adopted a short-term stimulus package in response to the economic slowdown which, in view of

the large economic imbalances, would be in line with the EERP. This was also confirmed in the addendum.

Fiscal policy outlined in the update is geared towards restoring investor confidence and addressing the macroeconomic imbalances. On the basis of the change in the (recalculated) structural balance, the overall fiscal stance is broadly neutral in 2009 and restrictive in 2010. However, it falls short to address timely and effectively the widening structural imbalances of the Greek economy and reverse the upward trend of public debt. In addition, the programme does not outline measures clearly showing potential to improve the long-term sustainability of public finances. Finally, it is important to note that Greece's budgetary framework has shown a poor track record, reflecting insufficient control of public expenditure, while revenue projections have proven to be systematically overoptimistic. In parallel, structural and endemic problems related to the recording of Greek government accounts in the recent past, have also been detrimental for timely and effective revenue and expenditure control.

The programme projects the headline deficit to remain above the 3% of GDP reference value throughout its period: the deficit would peak in 2009 and is set to decline gradually thereafter. In addition, the programme does not target the achievement of the MTO by its horizon. For 2010 and beyond, the programme plans for the structural balance to improve by more than 0.5% of GDP per year on average, in line with the Stability and Growth Pact. However, taking into account the balance of risks to the budgetary targets the pace is likely to turn out less pronounced than planned. Succeeding in consolidating public finances over the medium term will also help in curbing the large external deficit.

ANNEX 1. SPECIAL TOPIC: THE BUDGETARY PROCESS AND FISCAL INSTITUTIONS

1. INTRODUCTION

Fiscal developments in Greece over the last decade reflect insufficient control of public expenditure, while revenue projections have proven to be systematically optimistic. Moreover, structural and endemic problems related to the recording of Greek government accounts, have also been detrimental for timely and effective revenue and expenditure control, with systematic slippages in the execution of the Budget Laws having an expansionary impact, at times of above potential growth. This has contributed to feed inflation and lead to a sizeable appreciation of the real effective exchange rate (REER) vis-à-vis the euro area, eroding further the competitive position of the country. In addition, systemic problems related to the statistical governance in Greece, has led to significant statistical revisions of national accounts and public finances data, thus rising serious doubts about the reliability of the Greek statistics.

In this context, the Council, in its opinion of 4 March 2008, invited Greece to pursue the ongoing reforms of tax administration and continue improving the budgetary process by further increasing its transparency, spelling out the medium-term budgetary framework and effectively implementing mechanisms to monitor, control and improve the efficiency of primary expenditure. The Council also noted that such policy actions should be consistent with the April 2007 Eurogroup orientations for fiscal policies provided in the framework of the Lisbon Strategy; specifically, to improve the quality of public finances by reviewing public expenditures and taxation and by modernising public administration, with the intention to enhance productivity and innovation, thereby contributing to economic growth, employment and fiscal sustainability. In line with this recommendation, the Greek government has recently presented a reform agenda of the budget process, with the primary focus addressed at introducing a program based budget.

More specifically, the programme envisages the continuation of the ongoing budgetary reform and further progress with the implementation of programme budgeting, with a view to improving the public expenditure monitoring and management, increasing transparency and introducing a multi-year planning perspective in the budgetary process. The full implementation of the envisaged reform is planned for 2012 at the earliest. The Executive Summary of the report “Program Budgeting 2009”, providing some more technical information is annexed to the addendum to the programme.

2. FISCAL DEVELOPMENTS

Greece submitted its first Stability Programme in December 2000, which set up a medium-term objective (MTO) of a balanced budgetary position in structural terms. However, since then, this objective has become a moving target, with the execution of the successive Budget Laws failing to achieve the budgetary targets. Fiscal outcomes, as presented in the corresponding EDP notifications, deviated from the budgetary targets by around 2 percentage points of GDP on average. As a result, the objectives set in the successive updates of the Stability Programme were regularly revised to take account of

the continuous budgetary slippages. Tables 1&2, show in detail the subsequent revisions of the targets in the successive updates of programme, as well as the differences between budget targets and outcomes of both budgetary data and GDP.

On top of the budgetary slippages, structural and systemic problems related to the recording of Greek government accounts during the period 1997-2005 led to exceptionally large revisions in 2004 of the public finance figures, raising serious doubts about the reliability of Greek statistics. As a result, fiscal outcomes for 2001-2005, as presented in the corresponding EDP notifications, were significantly revised upwards by more than 3 percentage points of GDP on average⁷ (Tables 1&2). The most significant deviation, around 5 percentage points of GDP, was observed in 2004, when the budgetary target was set at 1.2% of GDP while, according to the corresponding EDP notification, the outturn was 6.1% of GDP. In its Opinion of 17th February 2005⁸, the Council invited Greece to put an end to the excessive deficit situation by 2006 at the latest. The 2006 Budget Law was the first budget to achieve its deficit budgetary objective of a general government deficit of 2.6% of GDP, although on the back of one-off measures amounting to 0.6%, thus leading to the abrogation of the EDP (Excessive Deficit Procedure) against Greece. However, further statistical revisions in October 2008 revealed problems in the accounting of EU funds that led to an upward revision of the government deficit for 2007 by ¼ percentage points, thus pushing the deficit again beyond the threshold of 3%. This new revision confirms the existence of still ongoing structural challenges, both in the preparation of the Greek budget and in its execution.

As shown in Table 1, the differences between fiscal targets and outcomes are also due to the revisions of the GDP series. The National Statistical Service of Greece (NSSG) carried out an in-depth revision of the Greek national accounts in 2006⁹, which was amended by Eurostat in 2007, leading to a significant upward revision of the GDP by 9.6% for the base year 2000¹⁰. Consequently, the deficit-to-GDP ratios for the years 2000 to 2006 were artificially reduced by around ½ percentage points of GDP, as a result of a denominator effect.

Debt targets were frequently missed (see Table 2), although in some years they were also over-achieved. This was the result of a combination of factors with opposite impact on the debt. On the one hand, debt outcomes were negatively affected by the accumulation of fiscal slippages. On the other hand, the 2004 statistical revisions both of GDP series and budgetary data led to reduction of the debt-to-GDP ratio. Specifically, the revision of budgetary data led to the identification of significant financial operations that were wrongly recorded as deficit-neutral, while they should have been recorded instead, as above-the-line operations with a deficit-increasing impact.

⁷ For details, see box 7 of the Commission services' technical assessment of the Stability Programme of Greece (2006-2009), http://ec.europa.eu/economy_finance/publications/publication4954_en.pdf.

⁸ Council Decision 2005/334/EC2

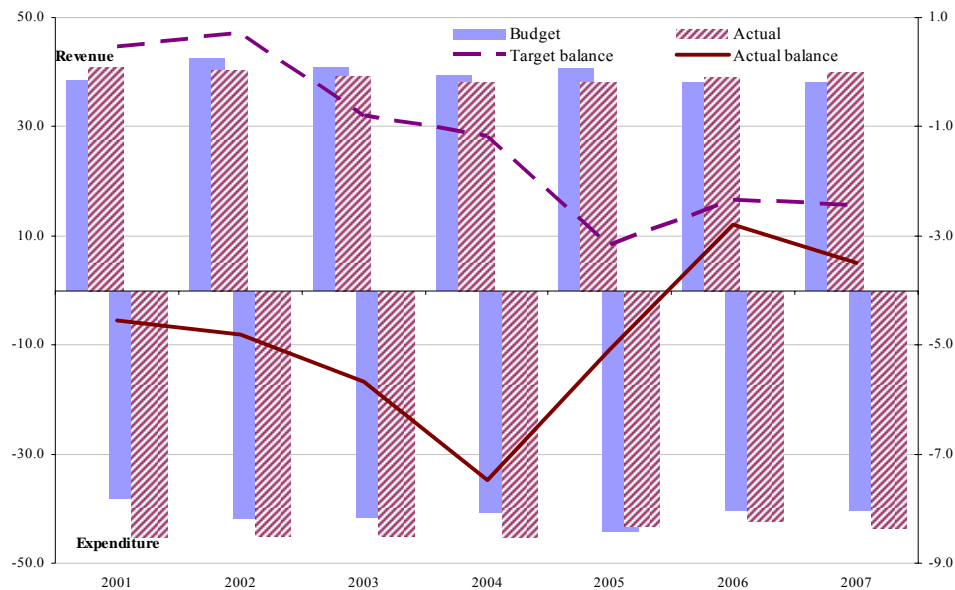
⁹ For more details on the statistical revisions of the Greek GDP, see box 3 of the Commission services' technical assessment of the Stability Programme of Greece (2007-2010), (available also at http://ec.europa.eu/economy_finance/publications/publication12209_en.pdf).

¹⁰ http://epp.eurostat.ec.europa.eu/cache/ITY_PUBLIC/GDPGR/EN/GDPGR-EN.PDF

Leaving aside the effects of statistical revisions, systematic slippages in the execution of the Budget Laws in the period 2000-2007 reflect both, revenue shortfalls and a lack of control in primary expenditure. Between 2000 and 2004, the deficit rose by 3¾ percentage points (4¾ percentage points of GDP in cyclically-adjusted terms) marking a peak of 7.5% of GDP in 2004 (8% of GDP in cyclically-adjusted terms). Total government revenues fell, from 43% to 38% of GDP over the same period, whereas total expenditure declined by only 1¼ percentage points of GDP.

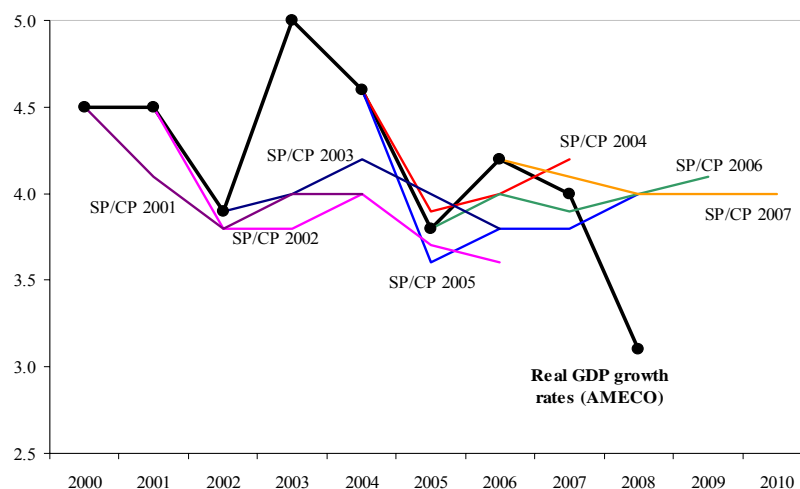
The under-achievement of annual budgetary targets continued in 2005 and 2007, hampering the fiscal adjustment projected by the December 2005 update of the Stability Programme. Between 2005 and 2007, the deficit declined by 2½ percentage points only. Total revenues increased by less than 2 percentage points of GDP, total expenditure increased by ¼ of a point of GDP.

Figure 1: Total revenue/expenditure and balance of general government (% GDP)



Deviations from budgetary targets can sometimes be explained by optimistic underlying economic assumptions accompanying the preparation of the Budget Laws (growth, employment, inflation and other important economic variables). However, this is not the case of Greece. Budgetary targets were set up based on economic projections that could be qualified as conservative. Real GDP growth projections provided in the successive updates of the Stability Programme of Greece were assuming an annual average growth of real GDP of 4¼% over the period 2000-2007, which largely coincide with the actual corresponding real GDP growth outcome (Figure 2).

Figure 2: Real GDP growth projections in successive stability programmes and budget laws (% change)



The origins of budgetary slippages in Greece have to be found in the budgetary processes and institutions, including the execution of the budget, encompassing both the collection of revenues and the control of current expenditures. On the revenue side, the projections of tax revenues have been persistently optimistic. In addition, the poor results of the Greek tax administration in the fight against tax evasion, as well as the proven difficulties in the prompt implementation of tax reforms, have played a significant role in the recorded revenue shortfalls. The steady decrease of tax revenues as a percentage of GDP since 2000 has taken place in a context of demand-driven growth, positive cyclical conditions and revenue-enhancing discretionary policies. It appears that factors associated with inefficiencies in tax administration, are hampering tax collection¹¹. Although recent efforts to improve tax administration seem to have lessened the impact of these inefficiencies in recent years, they are still significant. Revenue shortfalls would have been even larger in the absence of ad-hoc revenue enhancing measures that were implemented in the course of the year but had not been included in the Budget Law. On the expenditure side, weaknesses in the existing institutional framework of the budgetary process failed to prevent expenditure overruns, in particular in primary current expenditures. Moreover, the complexity of the current budget structure seems to have contributed to the failure in recording the Greek government accounts' in compliance with the ESA95 accounting rules, in particular the recording of military expenditure, the revenue and expenditure of social security funds, and the recording of EU structural funds-related revenue.

¹¹ Capo Servera M. – Moschovis G. (2008), "Tax revenue shortfalls in Greece", Country Focus, Vol. 3, Issue 5, 14.03.2008, DG ECFIN, European Commission

Table 1: Statistical revisions of deficit figures

| General government balance | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 |
|---|------|------|------|------|------|------|------|---|------|------|
| <i>% of GDP</i> | | | | | | | | | | |
| SP Dec. 2000 / Budget Law 2001 | 0.5 | 1.5 | 2.0 | | | | | | | |
| SP Dec. 2001 / Budget Law 2002 | | 0.8 | 1.0 | 1.2 | | | | | | |
| SP Dec. 2002 / Budget Law 2003 | | | -0.9 | -0.4 | 0.2 | 0.6 | | | | |
| SP Dec. 2003 / Budget Law 2004 | | | | -1.2 | -0.5 | 0.0 | | | | |
| SP Dec. 2004 / Budget Law 2005 | | | | | -2.8 | -2.6 | -2.5 | | | |
| SP Dec. 2005 / Budget Law 2006 | | | | | | -2.6 | -2.3 | -1.7 | | |
| SP Dec. 2006 / Budget Law 2007 | | | | | | | -2.4 | -1.8 | -1.2 | |
| SP Dec. 2007 / Budget Law 2008 | | | | | | | | -1.6 | -0.8 | 0.0 |
| EDP notification April of year t+1 for year t | 0.1 | -1.2 | -1.7 | -6.1 | -4.5 | -2.6 | -2.8 | | | |
| Actual balance (before the GDP revision) | -4.9 | -5.3 | -6.2 | -8.2 | -5.6 | -3.1 | | <i>Jan. 2009 Commission services forecast</i> | | |
| Actual Balance (AMECO) | -4.5 | -4.8 | -5.7 | -7.5 | -5.1 | -2.8 | -3.5 | -3.4 | -3.7 | -4.2 |

NOTE: The EDP notification of March 2005 has already taken into account the first wave of statistical revisions carried out in 2004 and had an impact on the 2004 budget execution

Table 2: Statistical revisions of debt figures

| General government gross debt | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 |
|---|-------|-------|-------|-------|-------|-------|-------|---|------|------|
| <i>% of GDP</i> | | | | | | | | | | |
| SP Dec. 2000 / Budget Law 2001 | 98.9 | 96.0 | 90.5 | | | | | | | |
| SP Dec. 2001 / Budget Law 2002 | | 97.3 | 94.4 | 90.0 | | | | | | |
| SP Dec. 2002 / Budget Law 2003 | | | 100.2 | 96.1 | 92.1 | 87.9 | | | | |
| SP Dec. 2003 / Budget Law 2004 | | | | 98.5 | 94.6 | 90.5 | | | | |
| SP Dec. 2004 / Budget Law 2005 | | | | | 108.0 | 103.9 | 99.9 | | | |
| SP Dec. 2005 / Budget Law 2006 | | | | | | 104.8 | 101.1 | 96.8 | | |
| SP Dec. 2006 / Budget Law 2007 | | | | | | | 100.1 | 95.9 | 91.3 | |
| SP Dec. 2007 / Budget Law 2008 | | | | | | | | 91.0 | 87.3 | 82.9 |
| EDP notification April of year t+1 for year t | 99.7 | 104.9 | 102.4 | 110.5 | 107.4 | 104.6 | 94.5 | | | |
| Actual balance (before the GDP revision) | 112.8 | 111.2 | 107.2 | 108.1 | 108.3 | 105.1 | | <i>Jan. 2009 Commission services forecast</i> | | |
| Actual Balance (AMECO) | 102.9 | 101.5 | 97.8 | 98.6 | 98.8 | 95.9 | 94.8 | 94.0 | 96.2 | 98.4 |

3. FISCAL GOVERNANCE IN GREECE

3.1. Greek budget overview

The Greek budget is comprised by the central government entities, while it does not include public enterprises and organizations, social security funds and hospitals, municipalities, prefectures and other public law entities. It only includes a brief description of the amounts transferred to these public entities, on the basis of which, the general government balance is formulated. As illustrated in Table 3, the general government imbalances have been traditionally fed by the central government deficit, while the local government sector has been broadly balanced and the social security sector was in surplus. However, local government balance has been actually hiding mounting deficits which were compensated by central government's financing. As a result, although central government represents around 56% of general government revenue and almost 64% of general government expenditure, almost 1/3 of general government resources and expenditures are not part of the budgetary process in Greece, which leads to a lack of a transparent, clear and consistent presentation of general government data.

Table 3: Government finance statistics by sector

| Net lending (+) / net borrowing (-) % of GDP | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 |
|--|-------------|-------------|-------------|-------------|-------------|-------------|-------------|
| Central gov. | -6.0 | -7.3 | -8.3 | -9.5 | -6.3 | -4.4 | -5.2 |
| Local gov. | 0.1 | 0.0 | 0.0 | -0.1 | -0.1 | -0.1 | 0.0 |
| SSF | 1.4 | 2.5 | 2.5 | 2.2 | 1.1 | 1.4 | 1.5 |
| EDP adjustments | -0.1 | 0.0 | 0.0 | -0.1 | 0.2 | 0.3 | 0.3 |
| General Government | -4.5 | -4.8 | -5.7 | -7.5 | -5.1 | -2.8 | -3.5 |

The state budget in Greece is composed of two parts, the ordinary annual budget and the public investment programme¹². This split has survived since mid-1950s, when the reconstruction of the country after the 2nd World War and the Civil war made earmarking of funds for infrastructure works and public investments, vital for Greece's development¹³. The public investment programme is formulated by the Secretariat General for Public Investment in the Ministry of Economy and Finance and includes all investment programmes financed and/or co-financed by the Community Structural Funds (CSF). The ordinary budget in turn, is prepared by the General Accounting Office (GAO) as an expenditure-oriented budget, including all revenue and expenditure plans for all central government entities (ministries and regions). The Greek budget is a very detailed technical document of around 14,000 line items of expenditure and many detailed tables. Such a detailed classification system makes it extremely difficult to have an overall view of the budget and derive any output and performance information. In addition, part of the central government's activities are financed through "special accounts" and earmarked funds, managed by the line ministries, agencies and other central government entities, which are not included in the ordinary budget and not covered by the same rules and regulations as the financial flows of central government.

¹² For a more detailed description of the structure of the budget and the procedures, see OECD "Budgeting in Greece", 2008. Also (in greek), Ράπανος, Β. (2007), Σύνταξη και εκτέλεση του κρατικού προϋπολογισμού: ευρωπαϊκή εμπειρία και η ελληνική πραγματικότητα, IOBE, Αθήνα.

¹³ A number of OECD countries, such as France, have previously had a ministry of planning (Commissariat Général du Plan) that focused on investment and countries such as the United Kingdom and the Netherlands maintain a separate process for capital budgeting, but integration of capital and current budgets has become the norm in OECD (<http://www.oecd.org/dataoecd/59/20/42007249.pdf>).

3.2. Budget preparation

The preparation of the budget starts in the 1st quarter of the year before the budget year, with the update of the macroeconomic forecast included in the December update of the stability and growth programme. In early spring, the Council of Ministers (the Cabinet) decides on the main orientations of fiscal policy. Later in spring, the GAO informs the line ministries on the fiscal policy priorities¹⁴ for the budget year and on the deadlines for their budgets' submission¹⁵. A similar procedure is followed for the public investment programme, by the Secretariat General for Public Investment.

By mid-June, all line ministries submit their ordinary budgets to the GAO, and their investment budgets to the Secretariat for Public Investments, launching a long process of political consultation between the Ministry of Economy and Finance and the line ministries, which in case of disagreement may be arbitrated by the Prime Minister. The discussions on tax legislation are carried out separately by the tax authorities who do not know how large overall expenditure will be. Consequently, an eventual higher-than-expected amount of total expenditure resulting from the intra-ministerial consultation would require changes in the tax legislation and additional tax enhancing measures. By the 1st Monday of October, the GAO submits the preliminary draft budget to the standing committee on economic affairs of Parliament and makes it public on the ministry's web-site. The Parliament's role is traditionally limited to a restrained reshuffling between line ministries' budgetary appropriations, without modifying the headline figures or correcting possible unrealistic revenue and expenditure estimations.

Not later than the 21st November, the government submits the final draft budget to Parliament, which according to the constitutional deadline should be adopted by the 31st December at the latest. Discussions last for more than 1 month in the parliamentary committees and 5 days in the general assembly; however, the parliamentary involvement is rather weak in scrutinizing suggested government policy. Although the Greek Constitution gives the necessary power to Parliament to amend the submitted budget proposal, the parliamentary standing orders impose strong procedural restrictions and prescribe a strict voting procedure of accept-or-reject vote on the budget proposal. These restrictions actually eliminate the possibility of an in-depth discussion on substantial amendments and generally lead to the adoption of the budget proposal unaltered.

3.3. Budget execution

The budget execution is the responsibility of the line ministries, monitored by the Fiscal Audit Office. Budget execution procedures focus on ensuring the legality and propriety of each expenditure of the central government entities. However, there is no budget policy analysis or performance assessment for the projects or activities financed through the budget. Moreover, the extremely detailed structure of the budget law makes the budget execution process

¹⁴ Interestingly, the macro-economic forecasts prepared by the Ministry of Economy and Finance are not used in the line ministries' budget preparations; instead, they develop their own forecasts.

¹⁵ The document prepared and sent by the GAO does not inform the line ministries and regions about the macro-economic forecast and thus, they are not obliged to use specific parameters, like inflation, unemployment, GDP growth rate. Each entity develops its own indicators, which makes the coordination and evaluation of the submissions from line ministries very difficult and raises questions on the budget's consistency.

practically inflexible, while any necessary mid-term adjustment in expenditure should follow a very long, bureaucratic and time consuming process, even for very small amounts.

The budget execution procedure includes a number of rules to prevent overspending, which however are not explicitly linked with the overall budgetary targets. According to these rules, Fiscal Audit Offices may not issue payment orders for any expenditure exceeding the appropriation limits or the allocation set in the budget line item for that particular item. However, exceptions to the overspending rules can take place in certain circumstances. Those additional expenditures just have to be covered by relevant appropriations in the following budget, hence expenditure overruns can easily occur, since there are not really binding (both legal or political) constraints.

The accounting of the budgetary execution is on a cash-basis. The National Statistical Office (NSO) in turn, uses the accounting recordings and the monthly budget execution reports compiled by the GAO, in order to prepare the national accounts for the central government, on the basis of the ESA 95 rules. For the other general government entities however, in the absence of a unitary consistent accounting system in all sectors¹⁶, the NSO uses mostly sectoral surveys. The problematic reporting mechanism and procedures, coupled with the lack of a common accounting basis between all sectors and entities in the public sector, has raised a number of questions about the quality and reliability of Greek consolidated national accounts.

3.4. Budget audit

The current audit and control arrangements are actually part of the global budget execution process, while there are no internal audit provisions, neither for the GAO nor the line ministries. The Hellenic Court of Audit (HCA), which is the Supreme Audit Institution (SAI) of Greece and the highest judicial authority for matters pertaining to public finances, is actually an external audit institution, which however has no authority on units other than the central government items. The (HCA) focuses on the legality and regularity of public expenditure, while it does not perform any quality or performance control of the expenditure. In addition, there are certain categories of expenditure (such as the military expenditure), in which it has no authority to intervene. It submits to the Parliament the results of its post-audit work and its annual report with a lag of 2 years. Although the report highlights problems and weaknesses identified and mainly related with the legality of public expenditure, there is no serious discussion in the Parliament, partly because it relates to previous public spending.

4. ASSESSMENT OF THE BUDGETARY PROCESS AND INSTITUTIONS

The literature on budgetary procedures pinpoints a number of basic features of the budget process that may influence the budgetary outcomes, efficiency of public spending and the overall quality of public finances. A seven dimension framework, covering all three budget process stages, namely planning, legislation and implementation includes, (a) transparency, top-down budgeting techniques, performance budgeting, multiannual planning horizon, prudent economic assumptions, and centralisation of the budget process¹⁷. OECD/World

¹⁶ There are five different accounting systems in the public sector, apart from the main one of the state budget; one each for hospitals, social security funds, municipalities, prefectures and other public law entities.

¹⁷ European Commission (2007), Public finances in EMU – 2007, European Economy, No. 3

Bank database provides information for a sample of 18 EU countries¹⁸, concerning each one of the dimensions presented above. Based on this information and data, the European Commission¹⁹ constructed a number of indices and an overall index whose scores reflect the quality of the specific budgetary feature for each country. According to this exercise, Greece has been found to have the weakest budgetary procedures, ranking last out of the countries of the sample (18th place). In particular, Greece was ranked among the three lowest in all seven categories of the budgetary process quality. Although there were several technical improvements in the budgetary framework in the recent past, these were only limited to procedural matters and did not tackle any of the structural weaknesses of the Greek budgetary process, which make it vulnerable to recurring fiscal slippages and fully expose it to the political cycle.

First different budget procedures, which would include all general government expenditure items in gross terms²⁰, makes the budgetary process insufficiently inclusive and opaque. Indeed, the lack of a consistent accounting system for all sectors is making the statistical governance of public finances hard and hardly adaptable to national accounts and ESA95 procedures. Moreover, the fiscal authorities have limited supervision over the expenditure management of the public entities, both inside and outside the central government, being unable to perform a comprehensive and proactive control to prevent fiscal slippages. Even at the level of the central government, the Greek budget lacks transparency, due to the unclear and imprecise distribution of powers and responsibilities between the ministries and within the government entities. In addition, the government has given up the right to control a part of public resources, which is reflected by the extensive use of extra-budgetary accounts and extra-budgetary transactions²¹.

Second, the lack of effective mechanisms to ensure budgetary discipline within the budget year creates a reliability problem to the Greek budget. Although budget plans appear to rely on reasonable macroeconomic projections, costs and implications of new tax or social policies are not properly assessed during the preparation phase, creating problems to the budget execution. However, there are no rules on how to compensate an emerging expenditure overrun or a revenue shortfall that may appear in the course of the year. Likewise, there are no specified procedures about the treatment of windfall revenues or possible expenditure savings in a budgetary chapter; thereby these can be used for new spending initiatives by the line ministries and regions. Furthermore, any new measures or decisions on new policies within the budget year are completely separated from the budgetary process, to the extent that there is no standard calculation about the budgetary impact from the adopted changes.

Finally, in spite of the multi-year impact of many spending programs included in the budget, and despite the fact that the Stability and Growth Pact requires fiscal projections for three years beyond the budget year, the budget process lacks a multi-year budgetary framework and

¹⁸ The OECD and the World Bank conducted a comprehensive survey on national budget procedures in 44 countries, both OECD-members and others, including 18 EU member states. The nine EU member states not included are Bulgaria, Cyprus, Estonia, Latvia, Lithuania, Luxembourg, Malta, Poland and Romania.

¹⁹ European Commission (2007), Public finances in EMU – 2007, European Economy, No. 3

²⁰ The OECD best practices for budget transparency state that expenditures should be presented in gross terms in the budget. In addition ear-marked revenue and user charges should be clearly accounted for separately. This should be done regardless of whether particular incentive and control systems provide for the retention of some or all of the receipts by the collecting agency (<http://www.oecd.org/dataoecd/32/0/40357919.pdf>).

²¹ Extra budgetary funds - special accounts and earmarked funds which may from time to time receive replenishment from budgetary resources - but which are not covered by the same rules and regulations as the financial flows of the budget. There may be good reasons for establishing these funds and thereby exempt certain transactions from standard budgetary procedures.

its formulation refers only to the forthcoming budget year. Although the planned medium-term fiscal strategy is submitted to the Parliament each year, in the course of the update of the Stability and Growth programme, it has only informative character and is not vested with a sufficient degree of political commitment, neither by the executive nor by the legislative branches. The medium-term targets do not represent a fixed path for the spending items and thus, although the successive updates of the stability programme have repeatedly presented increasingly ambitious multi-year adjustment paths, these plans do not effectively impact on budgetary policy. On the contrary, expenditure cutting with short-term measures (budgetary freezes, investment projects cancelation, fiscal gimmickry, one-off deficit reducing measures), have often been used by all Greek governments for political purposes, resulting in rebounding expenditure in the forthcoming years. Hence, the lack of an effective multi-annual fiscal framework, has not contributed to achieve a sustained reduction in the current primary expenditure-to-GDP ratio.

Overall, the Greek budgetary framework lacks transparency, clarity, flexibility and a medium-term perspective, and thus does not support policy analysis and accountability, while there is no kind of binding expenditure ceilings or any numerical fiscal rules in place. With these characteristics, the budget cannot give a comprehensive picture of how the government's policy objectives are represented in its spending and revenue plans. In addition, without some indication of the objectives underlying spending, it is basically impossible to judge how efficiently and effectively the budget accomplishes its objectives. On top of these weaknesses, the reporting on the execution of the budget is essentially addressed at checking the legality of budgetary transactions and how closely actual spending complies with the budgeted amounts, without any kind of assessment of how efficient and cost-effective the spending was.

5. THE REFORM OF THE BUDGETARY PROCESS: IMPLEMENTATION OF PROGRAMME BUDGETING

From the analysis in the previous sections a double motivation for reforming Greek fiscal governance can be drawn: (i) persistent fiscal slippages stemming from expenditure overruns and repetitive statistical upward revisions of the government deficit which have undermined a prompt fiscal consolidation strategy with long-lasting results, (ii) the lack of an effective and transparent fiscal framework to ensure budgetary discipline and consistency with the medium-term targets set in the updates of the stability and growth programmes.

The 2008 budget law launched a reform package of measures for the modernization of fiscal management, the improvement of the budgetary process and the shift to a more transparent and flexible programme based budgetary system. A program budgeting pilot for the Ministry of Culture was presented in the 2008 budget law, while a pilot for all ministries will be introduced in the 2009 budget law. These pilots are applied in parallel with the current system which remains the official budget. However, although the broad lines of the project were presented in the 2008 and 2009 budget laws and the December 2007 and 2008 updates of the stability and growth programme, both the state of play and the implementation timeframe of the reform are not clear.

The planned budgetary reform will apply a unitary and consistent classification to the ordinary budget, the public investment programme and the extra budgetary funds, forming an actual unitary budget. However, it is not clear whether it will include public entities outside the central government. To this end, the program budgeting system should reduce the number of line items and should classify public expenditure by functions, programs and actions, in order to increase flexibility and improve the comprehensiveness of the system, on the basis of

measurable results. According to the Greek authorities, this will enhance the efficiency control of public expenditure and the cost-effectiveness of various actions, while it would also strengthen budgetary transparency. In addition a multiyear planning perspective would be introduced, in order to maintain the fundamental elements of fiscal strategy in the medium term. However, according to the information available, it is not clear whether such a perspective would be legally binding and institutionally linked with the stability and growth programme of Greece.

In the context of the ongoing global budgetary reform, the Greek government introduced in August 2008 a package of measures for improving the public expenditure management and increasing transparency. According to the new measures, the majority of the extra-budgetary accounts are incorporated in the state budget, while an inter-ministerial committee is established, responsible for the management and control of the expenditures accounted by public entities not included in the state budget (hospitals, municipalities, prefectures and organizations), which in the past were responsible for a significant part of systematic expenditure overruns. In addition, public entities are obliged to submit annual financial statements and balance sheets. The recently adopted measures should (or will) give to the ministry of economy and finance the central control for all expenditure items in the general government sector, and will improve the reporting and quality of public finance statistics. These measures are included in the 2009 budget and constitute the first concrete steps to the budgetary reform direction.

Although the on-going reforms touch several aspects of the budget process, the key goal to introduce a new philosophy of public finance management and make the budget a strategic tool for better fiscal governance may not be fully fulfilled, since the scope of the reform is limited. Indeed, the reform only tackles procedural aspects of the budget process, mainly in its preparation phase. Moreover, it is not clear whether any binding expenditure or fiscal ceilings would be introduced in the reformed budgetary system, alongside a timely and regular monitoring mechanism. Expenditure ceilings would facilitate a top-down procedure in the preparation phase of the budget and would allow the medium-term budgetary impact of policy decisions to be fully taken into account. In addition, they would increase the control of the government on public expenditure management, and thus prevent fiscal slippages. However, in the absence of any kind of fiscal ceilings, the risk of fiscal slippages remains.

Finally, the ongoing reform does not seem to tackle the reliability "deficit" of the Greek budgetary system. The degree of political commitment and coordination between various levels of the government is not clear, while the reform does not introduce any governmental or independently surveillance authority to continuously check the compliance and consistency of the fiscal policy (monitoring of the implementation of budget plans, the compliance with the targets, recommendations for corrective steps in the event of slippages, etc.). To this end, budgetary targets should be vested with a sufficient degree of political commitment, by the executive and the legislative branches, being the result of proper coordination between various levels of government, in order to ensure sufficient commitment of all actors. Moreover, the creation of mechanisms to monitor compliance and fiscal discipline should be necessary, with particular attention to the design of enforcement procedures. Defining clearly ex- ante the actions to be taken in case of noncompliance would signal a strong commitment to respect the rules. Good quality of monthly and quarterly budgetary statistics and regular reporting will allow timely identification of non-compliance and facilitate a prompt corrective action.

However, despite its limitations, the ongoing reform can improve to some extent the transparency and accountability of public finances. It can also contribute to rationalise public spending and improve the quality and composition of government expenditure, with a positive

impact on economic efficiency. But the feasibility of the ongoing and planned measures will depend on the extent to which the existing rigidities in the Greek fiscal system can be successfully overcome.

6. FISCAL POLICY CHALLENGES AND PROSPECTS

As shown in previous sections, deficit overruns reflect a lack of control of public expenditure, in particular of current primary expenditure, not only in periods of fiscal expansion, but also in periods of fiscal consolidation. The current budgetary process and institutional framework in Greece have failed to ensure the achievement of the annual budgetary targets set in Budget Laws. The Greek government's recent reform agenda for the budget process, which is in line with the Council recommendations, seems insufficient. Improving the budgetary process by increasing its transparency, spelling out the budgetary strategy within a longer time perspective and effectively implementing mechanisms to monitor, control and improve the efficiency of primary expenditure is needed to prevent persistent fiscal slippages. Moreover, in the absence of an effective control of primary expenditure, the low quality of the fiscal adjustment observed in recent years, which has been basically based on revenue-enhancing measures, has been proven to be unsustainable in the medium-term.

Over the recent years, Greece has recorded strong economic growth, driven by buoyant private consumption and dynamic investment activity, while employment growth accelerated significantly. However, high inflation differentials with the euro area persist, and, in spite of a significant productivity growth, this is leading to competitiveness losses and a widening current account deficit. Behind the external imbalances lie prominently the fiscal weaknesses. Despite high nominal growth, Greece has been recording frequent general government deficits above 3% of GDP, maintaining a high debt and facing the costs of population ageing, an increase in the cost of the public health system and other current expenditures. This public expenditure pattern is worrying not only because external borrowing is not always channelled to productive investments, but also because the easiness of external borrowing is dependent on the credibility and sustainability of public finances. Moreover, in the light of the impact of the ongoing global economic and financial crisis on the Greek economy, mirrored also by the rising spread between Greek and German government bond yields, the implied re-pricing of risks puts further pressure on the debt burden.

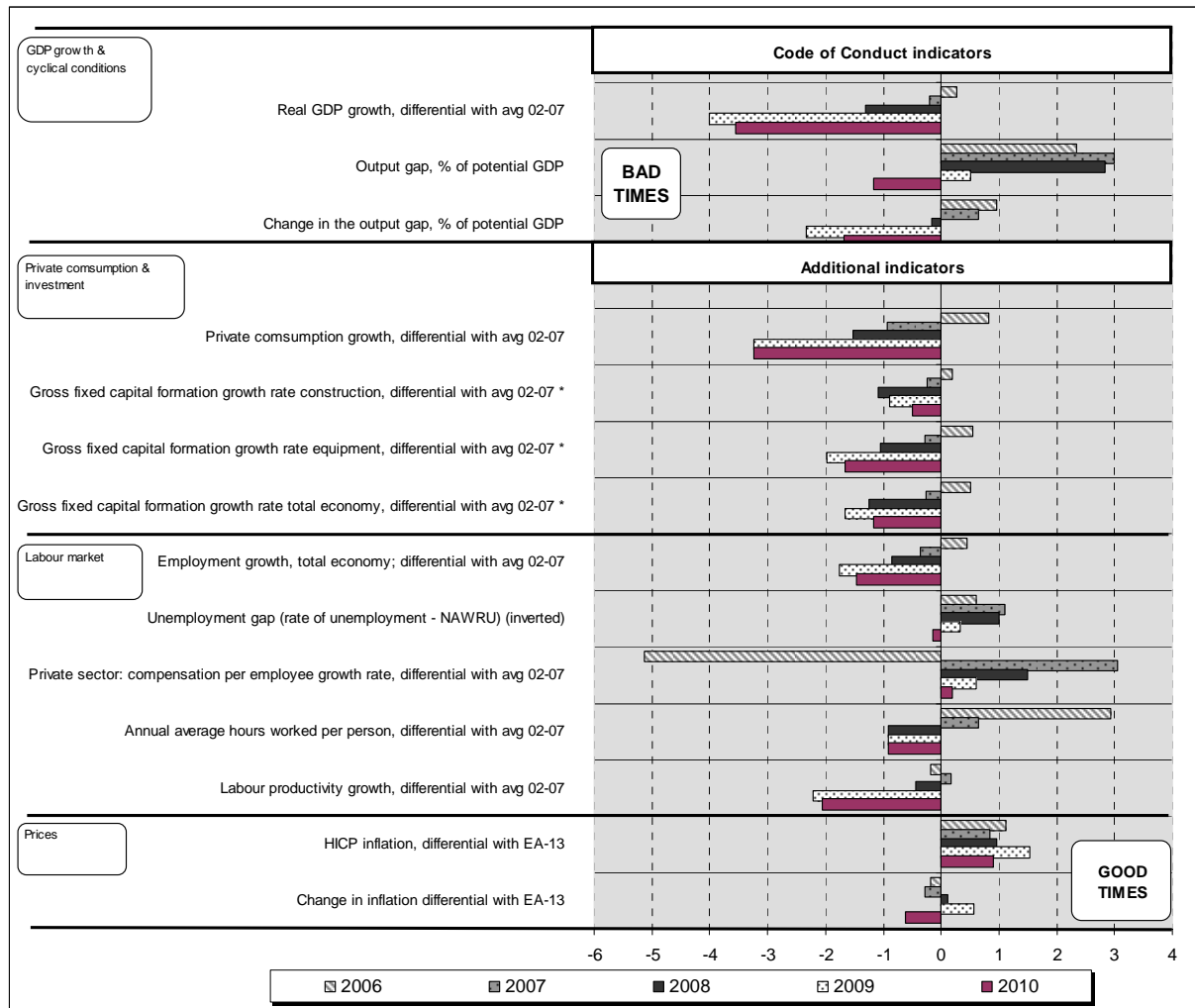
In this context it is important to highlight the leading role of the public sector, which is by far the largest employer of the Greek economy, in aggregate wage developments. Wage moderation in the public sector would have positive effects on the wage developments of the private sector, thus improving the functioning of labour and product markets. Combined with a rise of domestic savings and comprehensive structural reforms to support growth and job creation, it should also help reduce the external deficit and ease inflationary pressures. Moreover, improvements in the tax administration would lessen the need to resort to discretionary measures, which could put pressure on inflation (increases in indirect taxes), introduce additional distortions and further erode the competitiveness of the economy (increases on direct taxes), or worsen the relatively high unemployment rate (increases in social contributions).

Greece is facing the challenge to restore investors' confidence and achieve substantial fiscal consolidation, while improving the quality of public finances and correcting the factors behind the large domestic and external imbalances of the economy. Given also the high level of public-debt, strengthening the fiscal consolidation path, based on permanent measures to

control current primary expenditure including public wages, would be paramount to achieve sound and sustainable public finances in Greece.

ANNEX 2. ADDITIONAL TABLES AND FIGURES

Figure 1: Good and bad economic times



Source: Commission services' January 2009 forecast (COM) and successive stability programmes

Table 1: Budgetary implementation in 2008

| | 2007 | | 2008 | |
|--|-------------|---------|-------------|---------|
| | Planned | Outcome | Planned | Outcome |
| | SP Dec 2007 | COM | SP Dec 2007 | COM |
| Government balance (% of GDP) | -2.7 | -3.5 | -1.6 | -3.4 |
| Difference compared to target | -0.8 | | -1.8 | |
| <i>Of which</i> : due to a different starting position end 2007 | | | -0.8 | |
| due to different revenue / expenditure growth in 2008 | | | -1.0 | |
| p.m. Denominator effect and residual ^{2,3} | | | -0.1 | |
| <i>p.m. Nominal GDP growth (planned and outcome)</i> | | | 7.0 | 7.3 |
| Revenue (% of GDP) | 39.9 | 40.0 | 41.1 | 39.9 |
| Revenue surprise compared to target ¹ | 0.1 | | -1.2 | |
| <i>Of which</i> : due to a different starting position end 2007 | | | 0.1 | |
| due to different revenue growth in 2008 | | | -1.1 | |
| p.m. Denominator effect ² | | | -0.1 | |
| p.m. Residual ³ | | | -0.1 | |
| <i>p.m. Revenue growth rate (planned and outcome)</i> | | | 10.2 | 7.2 |
| Expenditure (% of GDP) | 42.6 | 43.4 | 42.7 | 43.4 |
| Expenditure surprise compared to target ¹ | -0.8 | | -0.7 | |
| <i>Of which</i> : due to different starting position end 2007 | | | -0.8 | |
| due to different expenditure growth rate in 2008 | | | 0.1 | |
| p.m. Denominator effect ² | | | 0.1 | |
| p.m. Residual ³ | | | 0.0 | |
| <i>p.m. Expenditure growth rate (planned and outcome)</i> | | | 7.3 | 7.1 |
| Notes: | | | | |
| ¹ A positive number implies that the outcome was better (in terms of government balance) than planned. | | | | |
| ² The denominator effect captures the mechanical effect that, if GDP turns out higher than planned, the ratio of revenue or expenditure to GDP will fall because of a higher denominator. Although the denominator effect can be very significant for revenue | | | | |
| ³ The decomposition leaves a small residual that cannot be assigned to the previous components. The residual is generally small, except in some cases where planned and actual growth rates of revenue, expenditure and GDP differ significantly. | | | | |
| <i>Source: Commission services</i> | | | | |

Table 2: Evolution of budgetary targets in successive programmes

| | | 2007 | 2008 | 2009 | 2010 | 2011 |
|--|---------------------------|---------------|--------------|--------------|--------------|--------------|
| Real GDP (% change) | SP Jan 2009 | 4.0 | 3.0 | 1.1 | 1.6 | 2.3 |
| | COM Jan 2009 | 4.0 | 2.9 | 0.2 | 0.7 | n.a. |
| | <i>SP Dec 2007</i> | <i>4.1</i> | <i>4.0</i> | <i>4.0</i> | <i>4.0</i> | <i>n.a.</i> |
| HICP inflation (%) | SP Jan 2009 | 3.0 | 4.3 | 2.6 | 2.5 | 2.4 |
| | COM Jan 2009 | 3.0 | 4.3 | 2.5 | 2.7 | n.a. |
| | <i>SP Dec 2007</i> | <i>2.9</i> | <i>2.8</i> | <i>2.7</i> | <i>2.6</i> | <i>n.a.</i> |
| Output gap ¹ (% of potential GDP) | SP Jan 2009 | 2.2 | 1.9 | 0.3 | -0.8 | -1.0 |
| | COM Jan 2009 ² | 3.0 | 2.8 | 0.5 | -1.2 | n.a. |
| | <i>SP Dec 2007</i> | <i>1.3</i> | <i>1.2</i> | <i>1.2</i> | <i>n.a.</i> | <i>n.a.</i> |
| Net lending/borrowing vis-à-vis the rest of the world (% of GDP) | SP Jan 2009 | -12.1 | -12.8 | -11.4 | -10.8 | -10.0 |
| | COM Jan 2009 | -12.1 | -11.7 | -11.2 | -11.6 | n.a. |
| | <i>SP Dec 2007</i> | <i>-12.8</i> | <i>-12.7</i> | <i>-12.5</i> | <i>-12.2</i> | <i>n.a.</i> |
| General government revenue (% of GDP) | SP Jan 2009 | 39.9 | 40.0 | 41.0 | 41.1 | 41.2 |
| | COM Jan 2009 | 40.0 | 39.9 | 40.8 | 40.0 | n.a. |
| | <i>SP Dec 2007</i> | <i>39.900</i> | <i>41.1</i> | <i>41.7</i> | <i>42.3</i> | <i>n.a.</i> |
| General government expenditure (% of GDP) | SP Jan 2009 | 43.4 | 43.7 | 44.7 | 44.3 | 43.8 |
| | COM Jan 2009 | 43.4 | 43.4 | 44.5 | 44.2 | n.a. |
| | <i>SP Dec 2007</i> | <i>42.6</i> | <i>42.7</i> | <i>42.5</i> | <i>42.3</i> | <i>n.a.</i> |
| General government balance (% of GDP) | SP Jan 2009 | -3.5 | -3.7 | -3.7 | -3.2 | -2.6 |
| | COM Jan 2009 | -3.5 | -3.4 | -3.7 | -4.2 | n.a. |
| | <i>SP Dec 2007</i> | <i>-2.7</i> | <i>-1.6</i> | <i>-0.8</i> | <i>0.0</i> | <i>n.a.</i> |
| Primary balance (% of GDP) | SP Jan 2009 | 0.6 | 0.3 | 0.80 | 1.2 | 1.7 |
| | COM Jan 2009 | 0.6 | 0.6 | 0.6 | 0.0 | n.a. |
| | <i>SP Dec 2007</i> | <i>1.2</i> | <i>2.4</i> | <i>3.1</i> | <i>3.8</i> | <i>n.a.</i> |
| Cyclically-adjusted balance ¹ (% of GDP) | SP Jan 2009 | -4.4 | -4.5 | -3.8 | -2.8 | -2.2 |
| | COM Jan 2009 | -4.8 | -4.7 | -3.9 | -3.7 | n.a. |
| | <i>SP Dec 2007</i> | <i>-3.4</i> | <i>-2.4</i> | <i>-2.3</i> | <i>n.a.</i> | <i>n.a.</i> |
| Structural balance ³ (% of GDP) | SP Jan 2009 | -4.4 | -4.5 | -4.3 | -2.8 | -2.2 |
| | COM Jan 2009 | -4.6 | -5.0 | -4.7 | -3.7 | n.a. |
| | <i>SP Dec 2007</i> | <i>-3.1</i> | <i>-2.4</i> | <i>-2.3</i> | <i>n.a.</i> | <i>n.a.</i> |
| Government gross debt (% of GDP) | SP Jan 2009 | 94.8 | 94.6 | 96.3 | 96.1 | 94.7 |
| | COM Jan 2009 | 94.8 | 94.0 | 96.2 | 98.4 | n.a. |
| | <i>SP Dec 2007</i> | <i>93.4</i> | <i>91.0</i> | <i>87.3</i> | <i>82.9</i> | <i>n.a.</i> |

Notes:

¹Output gaps and cyclically-adjusted balances according to the programmes as recalculated by Commission services on the basis of the information in the programmes.

²Based on estimated potential growth of 3.2%, 2.7%, 2.8% and 2.5% respectively in the period 2008-2011.

³Cyclically-adjusted balance excluding one-off and other temporary measures. One-off and other temporary measures are 0.4% of GDP in 2008 and 0.5% in 2009 (all deficit-reducing) according to the most recent programme and 0.4% of GDP in 2008 and 0.8% in 2009 (all deficit-reducing) in the Commission services' January interim forecast.

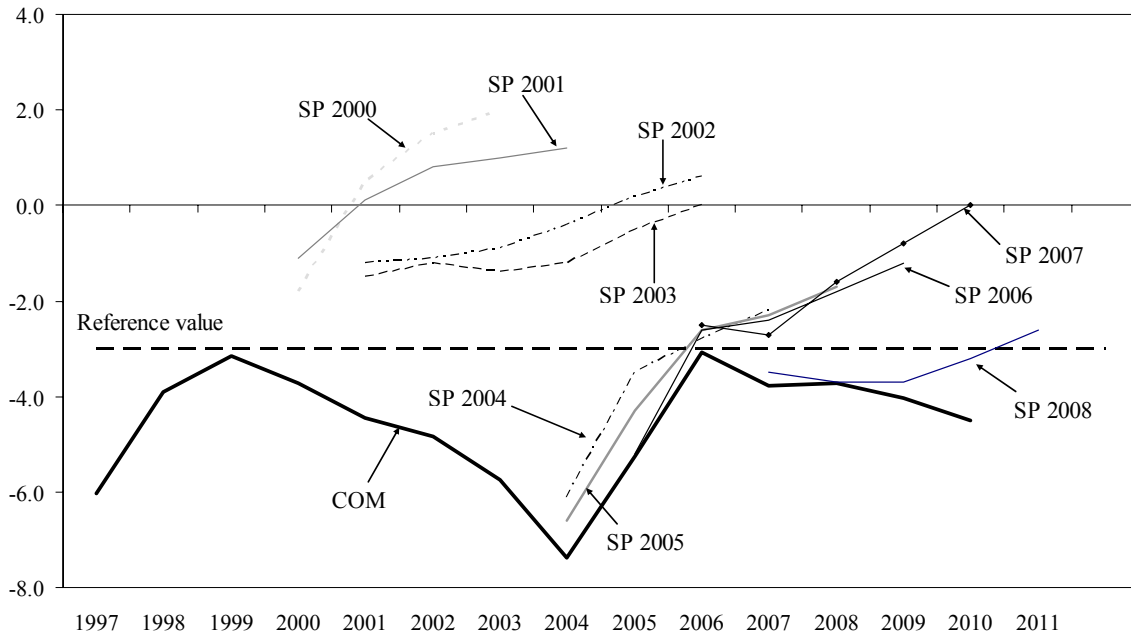
Source:

Stability programme (SP); Commission services' January 2009 interim forecasts (COM); Commission services' calculations

Table 3: Assessment of tax projections

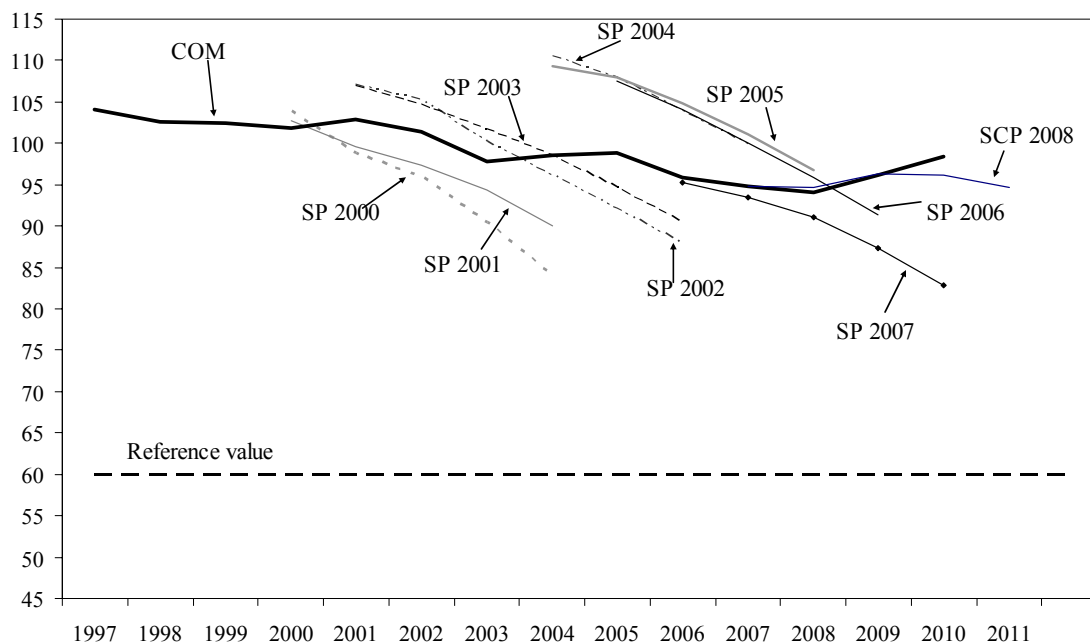
| | 2009 | | | 2010 | | | 2011 |
|---|------|-----|-------------------|------|------------------|-------------------|------|
| | SP | COM | OECD ³ | SP | COM ¹ | OECD ³ | SP |
| Change in tax-to-GDP ratio (total taxes) | 2.0 | 1.6 | 0.1 | -0.2 | -0.5 | 0.1 | 0.0 |
| Difference (SP – COM) | 0.4 | | / | 0.4 | | / | / |
| <i>of which</i> ² : | | | | | | | |
| - discretionary and elasticity component | 0.0 | | / | 0.0 | | / | / |
| - composition component | 0.1 | | / | 0.1 | | / | / |
| Difference (COM - OECD) | / | 1.5 | | / | -0.6 | | / |
| <i>of which</i> ² : | | | | | | | |
| - discretionary and elasticity component | / | 1.2 | | / | -0.9 | | / |
| - composition component | / | 0.7 | | / | 0.7 | | / |
| p.m.: Elasticity to GDP | 2.5 | 2.4 | 1.1 | 0.9 | 0.6 | 1.1 | 1.0 |
| Notes: | | | | | | | |
| ¹ On a no-policy change basis. | | | | | | | |
| ² The composition component captures the effect of differences in the composition of aggregate demand (more tax rich or more tax poor components). The discretionary and elasticity component captures the effect of discretionary fiscal policy measures as well as variations of the yield of the tax system that may result from factors such as time lags and variations of taxable income that do not necessarily move in line with GDP, e.g. capital gains. The two components may not add up to the total difference because of a residual component, which is generally small. | | | | | | | |
| ³ OECD ex-ante elasticity relative to GDP. | | | | | | | |
| Source: | | | | | | | |
| Commission services' January 2009 interim forecasts (COM); Stability programme (SP); Commission services' calculations; OECD (N. Girouard and C. André (2005), "Measuring Cyclically-Adjusted Budget Balances for the OECD Countries", OECD Working Paper No. 434). | | | | | | | |

Figure 2: Government balance projections in successive programmes (% of GDP)



Source: Commission services' January 2009 interim forecast (COM) and successive stability programmes

Figure 3: Debt projections in successive programmes (% of GDP)



Source: Commission services' January 2009 interim forecast (COM) and successive stability programmes

Table 4: Long-term age-related expenditure: main projections

| (% of GDP) | 2004 | 2010 | 2020 | 2030 | 2040 | 2050 | Change 2010- 50 |
|-----------------------------------|------|------|------|------|------|------|-----------------|
| Total age-related spending | 8.9 | 8.7 | 8.7 | 9.1 | 9.7 | 10.2 | 1.5 |
| - Pensions | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. |
| - Healthcare | 5.1 | 5.4 | 5.6 | 5.9 | 6.5 | 6.8 | 1.4 |
| - Long-term care | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. |
| - Education | 3.5 | 3.1 | 2.9 | 3.0 | 3.0 | 3.1 | 0.0 |
| - Unemployment benefits | 0.3 | 0.3 | 0.2 | 0.2 | 0.2 | 0.2 | -0.1 |
| Property income received | 1.0 | 0.9 | 0.9 | 0.8 | 0.8 | 0.7 | -0.2 |

Source: Economic Policy Committee and Commission services, 2006.

Table 5: Sustainability indicators and the required primary balance (excluding pensions and long-term care)

| Value | 2008 scenario | | | Programme scenario | | |
|---|---------------|-----|-----|--------------------|------|-----|
| | S1 | S2 | RPB | S1 | S2 | RPB |
| Value | 3.9 | 3.8 | 2.9 | 0.6 | 0.6 | 2.8 |
| <i>of which:</i> | | | | | | |
| Initial budgetary position (IBP) | 2.7 | 2.9 | - | -0.4 | -0.3 | - |
| Debt requirement in 2050 (DR) | 0.7 | - | - | 0.6 | - | - |
| Long-term change in the primary balance (LTC) | 0.4 | 0.9 | - | 0.4 | 0.9 | - |

Source: Commission services.

Table 6: Additional factors

| | Impact on risk |
|---|-----------------------|
| Debt and pension assets | - |
| Decline in structural balance until 2010 in COM January 2009 interim forecast | + |
| Significant revenues from pension taxation | na |
| Alternative projection of cost of ageing | - |
| Strong decline in benefit ratio | na |
| High tax burden | na |
| Non-age related budgetary measures with intertemporal effect | na |

*Note: '-' : factor tends to increase the risk to sustainability, '+' : factor tends to decrease the risk to sustainability.
'na' : not applicable.*

Alternative projections are often presented in the programmes, whose assumptions often diverge from the common method. Projections currently discussed in the Economic Policy Committee but not yet published, are for the time being also considered "unofficial".

An explanation on these factors can be found in chapter IV of: European Commission (2006), The long-term sustainability of public finances in the European Union, European Economy No. 4/2006.

Source: Commission services.

ANNEX 3. COMPLIANCE WITH THE CODE OF CONDUCT AND TABLES FROM THE PROGRAMME

The programme adheres to the code of conduct for stability and convergence programmes as far as its table of contents is concerned, notably follows the model structure in Annex 1 of the code of conduct.

As far as data requirements are concerned, the programme update provides almost all compulsory and most of the optional data prescribed by the code of conduct as amended by the September 2007 EFC. However, the programme has a few gaps in the required and optional data²².

The tables on the following pages show the data presented in the January 2008 update of stability programme, following the structure of the tables in Annex 2 of the code of conduct. Compulsory data are in bold, missing data are indicated with grey-shading.

²² In particular, general government expenditure by function and information on debt developments and the components of stock-flow adjustment (differences between cash and accruals, net accumulation of financial assets, valuation effects and other), liquid financial assets and net financial debts are not provided.

Table 1a. Macroeconomic prospects

| | ESA Code | 2007 | 2007 | 2008 | 2009 | 2010 | 2011 |
|--|-------------|----------|----------------|----------------|----------------|----------------|----------------|
| | | Level | rate of change | rate of change | rate of change | rate of change | rate of change |
| 1. Real GDP | B1*g | 182000.0 | 4.0 | 3.0 | 1.1 | 1.6 | 2.3 |
| 2. Nominal GDP | B1*g | 228200 | 7.0 | 7.4 | 3.8 | 4.2 | 4.9 |
| Components of real GDP | | | | | | | |
| 3. Private consumption expenditure | P.3 | 130800 | 3.0 | 2.3 | 1.9 | 2.0 | 2.1 |
| 4. Government consumption expenditure | P.3 | 29100 | 7.7 | 3.1 | 3.5 | 1.0 | 1.0 |
| 5. Gross fixed capital formation | P.51 | 44400 | 4.9 | -8.9 | -0.5 | 3.0 | 3.5 |
| 6. Changes in inventories and net acquisition of valuables (% of GDP) | P.52 + P.53 | 200.0 | 0.1 | 2.0 | 0.2 | -0.2 | -0.3 |
| 7. Exports of goods and services | P.6 | 43600 | 3.1 | 3.9 | 1.5 | 2.5 | 3.3 |
| 8. Imports of goods and services | P.7 | 66200 | 6.7 | 0.4 | -1.8 | 2.2 | 2.6 |
| Contributions to real GDP growth | | | | | | | |
| 9. Final domestic demand | | - | 4.6 | 0.3 | 1.8 | 2.2 | 2.4 |
| 10. Changes in inventories and net acquisition of valuables | P.52 + P.53 | - | 1.1 | 1.9 | -1.7 | -0.5 | 0.0 |
| 11. External balance of goods and services | B.11 | - | -1.6 | 0.8 | 1.0 | -0.2 | -0.1 |

Table 1b. Price developments

| | ESA Code | 2007 | 2007 | 2008 | 2009 | 2010 | 2011 |
|--|----------|-------------|----------------|----------------|----------------|----------------|----------------|
| | | Level | rate of change | rate of change | rate of change | rate of change | rate of change |
| 1. GDP deflator | | <i>n.a.</i> | 2.9 | 4.3 | 2.7 | 2.6 | 2.5 |
| 2. Private consumption deflator | | <i>n.a.</i> | 3.2 | 4.2 | 2.6 | 2.5 | 2.4 |
| 3. HICP¹ | | <i>n.a.</i> | 3.0 | 4.3 | 2.6 | 2.5 | 2.4 |
| 4. Public consumption deflator | | <i>n.a.</i> | 3.2 | 4.5 | 2.9 | 2.5 | 2.4 |
| 5. Investment deflator | | <i>n.a.</i> | 2.2 | 4.4 | 2.7 | 2.3 | 2.2 |
| 6. Export price deflator (goods and services) | | <i>n.a.</i> | 2.4 | 4.8 | 2.6 | 2.5 | 2.4 |
| 7. Import price deflator (goods and services) | | <i>n.a.</i> | 3.0 | 6.0 | 1.4 | 1.8 | 1.7 |

¹ Optional for stability programmes.

Table 1c. Labour market developments

| | ESA Code | 2007 | 2007 | 2008 | 2009 | 2010 | 2011 |
|--|----------|---------|----------------|----------------|----------------|----------------|----------------|
| | | Level | rate of change | rate of change | rate of change | rate of change | rate of change |
| 1. Employment, persons¹ | | 4701.7 | 1.3 | 1.1 | 0.2 | 0.6 | 0.7 |
| 2. Employment, hours worked ² | | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. |
| 3. Unemployment rate (%)³ | | 406.9 | 8.0 | 7.5 | 8.0 | 8.0 | 7.9 |
| 4. Labour productivity, persons⁴ | | n.a. | 2.7 | 1.9 | 0.9 | 1.0 | 1.6 |
| 5. Labour productivity, hours worked ⁵ | | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. |
| 6. Compensation of employees | D.1 | 79000.0 | 10.8 | 9.8 | 7.1 | 4.3 | 4.5 |
| 7. Compensation per employee | | n.a. | 9.1 | 7.6 | 6.1 | 3.4 | 3.5 |

¹Occupied population, domestic concept national accounts definition.

²National accounts definition.

³Harmonised definition, Eurostat; levels.

⁴Real GDP per person employed.

⁵Real GDP per hour worked.

Table 1d. Sectoral balances

| % of GDP | ESA Code | 2007 | 2008 | 2009 | 2010 | 2011 |
|---|----------|-------|-------|-------|-------|-------|
| 1. Net lending/borrowing vis-à-vis the rest of the world | B.9 | -12.1 | -12.8 | -11.4 | -10.8 | -10.0 |
| <i>of which :</i> | | | | | | |
| - Balance on goods and services | | -10.5 | -9.9 | -8.4 | -8.2 | -7.8 |
| - Balance of primary incomes and transfers | | -3.6 | -4.7 | -4.7 | -4.3 | -3.9 |
| - Capital account | | 1.9 | 1.7 | 1.7 | 1.7 | 1.7 |
| 2. Net lending/borrowing of the private sector | B.9 | -8.6 | -9.1 | -7.7 | -7.6 | -7.4 |
| 3. Net lending/borrowing of general government | EDP B.9 | -3.5 | -3.7 | -3.7 | -3.2 | -2.6 |
| 4. Statistical discrepancy | | n.a. | n.a. | n.a. | n.a. | n.a. |

Table 2. General government budgetary prospects

| | ESA Code | 2007 | 2007 | 2008 | 2009 | 2010 | 2011 |
|---|--------------------------|-------------|-------------|-------------|-------------|-------------|-------------|
| | | Level | % of GDP | % of GDP | % of GDP | % of GDP | % of GDP |
| Net lending (EDP B.9) by sub-sector | | | | | | | |
| 1. General government | S.13 | -7900 | -3.5 | -3.7 | -3.7 | -3.2 | -2.6 |
| 2. Central government | S.1311 | -11200 | -4.9 | -6.3 | -6.2 | -4.6 | -3.9 |
| 3. State government | S.1312 | <i>n.a.</i> | <i>n.a.</i> | <i>n.a.</i> | <i>n.a.</i> | <i>n.a.</i> | <i>n.a.</i> |
| 4. Local government | S.1313 | -100 | -0.1 | 0.0 | 0.7 | 0.0 | 0.0 |
| 5. Social security funds | S.1314 | 3300 | 1.5 | 2.6 | 1.8 | 1.3 | 1.3 |
| General government (S13) | | | | | | | |
| 6. Total revenue | TR | 91100 | 39.9 | 40.0 | 41.0 | 41.1 | 41.2 |
| 7. Total expenditure | TE ¹ | 99000.0 | 43.4 | 43.7 | 44.7 | 44.3 | 43.8 |
| 8. Net lending/borrowing | EDP B.9 | -7900 | -3.5 | -3.7 | -3.7 | -3.2 | -2.6 |
| 9. Interest expenditure | EDP D.41 | 9300 | 4.1 | 4.0 | 4.5 | 4.4 | 4.3 |
| 10. Primary balance² | | 1400 | 0.6 | 0.3 | 0.8 | 1.2 | 1.7 |
| 11. One-off and other temporary measures³ | | <i>n.a.</i> | -0.5 | 0.4 | 0.5 | 0.0 | 0.0 |
| Selected components of revenue | | | | | | | |
| 12. Total taxes (12=12a+12b+12c) | | 46000.0 | 20.2 | 19.9 | 22.0 | 21.8 | 21.8 |
| 12a. Taxes on production and imports | D.2 | 27500 | 12.1 | 11.9 | 12.3 | 12.4 | 12.4 |
| 12b. Current taxes on income, wealth, etc | D.5 | 18100 | 7.9 | 7.8 | 9.3 | 9.0 | 9.0 |
| 12c. Capital taxes | D.91 | 400 | 0.2 | 0.2 | 0.4 | 0.4 | 0.4 |
| 13. Social contributions | D.61 | 31800 | 13.9 | 14.2 | 14.2 | 14.2 | 14.2 |
| 14. Property income | D.4 | 2100 | 0.9 | 0.9 | 0.8 | 0.8 | 0.8 |
| 15. Other⁴ | | 12100 | 5.4 | 4.8 | 4.0 | 4.3 | 4.4 |
| 16=6. Total revenue | TR | 91100 | 39.9 | 40.0 | 41.0 | 41.1 | 41.2 |
| p.m.: Tax burden (D.2+D.5+D.61+D.91-D.995)⁵ | | | 31.9 | 31.9 | 34.0 | 33.7 | 33.7 |
| Selected components of expenditure | | | | | | | |
| 17. Compensation of employees + intermediate consumption | D.1+P.2 | 37000 | 16.2 | 16.3 | 17.0 | 16.8 | 16.6 |
| 17a. Compensation of employees | D.1 | 25200 | 11.0 | 11.3 | 12.0 | 11.9 | 11.7 |
| 17b. Intermediate consumption | P.2 | 11800 | 5.2 | 5.0 | 5.0 | 4.9 | 4.9 |
| 18. Social payments (18=18a+18b) | | 39300 | 17.2 | 18.0 | 18.6 | 18.6 | 18.6 |
| 18a. Social transfers in kind supplied via market producers | D.6311, D.63121, D.63131 | <i>n.a.</i> | <i>n.a.</i> | <i>n.a.</i> | <i>n.a.</i> | <i>n.a.</i> | <i>n.a.</i> |
| 18b. Social transfers other than in kind | D.62 | 39300 | 17.2 | 18.0 | 18.6 | 18.6 | 18.6 |
| 19=9. Interest expenditure | EDP D.41 | 9300 | 4.1 | 4.0 | 4.5 | 4.4 | 4.3 |
| 20. Subsidies | D.3 | 300 | 0.1 | 0.1 | 0.1 | 0.1 | 0.1 |
| 21. Gross fixed capital formation | P.51 | 6700 | 3.0 | 3.0 | 2.7 | 2.7 | 2.7 |
| 22. Other⁶ | | 6400 | 2.8 | 2.3 | 1.8 | 1.9 | 1.7 |
| 23=7. Total expenditure | TE ¹ | 99000.0 | 43.4 | 43.7 | 44.7 | 44.3 | 43.8 |
| p.m.: Government consumption (nominal) | P.3 | 38100 | 16.7 | 16.7 | 17.2 | 17.1 | 16.8 |

¹Adjusted for the net flow of swap-related flows, so that TR-TE=EDP B.9.

²The primary balance is calculated as (EDP B.9, item 8) plus (EDP D.41, item 9).

³A plus sign means deficit-reducing one-off measures.

⁴P.11+P.12+P.131+D.39+D.7+D.9 (other than D.91).

⁵Including those collected by the EU and including an adjustment for uncollected taxes and social contributions (D.995), if appropriate.

⁶D.29+D4 (other than D.41)+ D.5+D.7+D.9+P.52+P.53+K.2+D.8.

Table 3. General government expenditure by function

| % of GDP | COFOG Code | 2006 | 2011 |
|---|-----------------|------|------|
| 1. General public services | 1 | n.a. | n.a. |
| 2. Defence | 2 | n.a. | n.a. |
| 3. Public order and safety | 3 | n.a. | n.a. |
| 4. Economic affairs | 4 | n.a. | n.a. |
| 5. Environmental protection | 5 | n.a. | n.a. |
| 6. Housing and community amenities | 6 | n.a. | n.a. |
| 7. Health | 7 | n.a. | n.a. |
| 8. Recreation, culture and religion | 8 | n.a. | n.a. |
| 9. Education | 9 | n.a. | n.a. |
| 10. Social protection | 10 | n.a. | n.a. |
| 11. Total expenditure (=item 7=23 in Table 2) | TE ¹ | n.a. | n.a. |

¹Adjusted for the net flow of swap-related flows, so that TR-TE=EDP B.9.

Table 4. General government debt developments

| % of GDP | ESA Code | 2007 | 2008 | 2009 | 2010 | 2011 |
|---|----------|------|------|------|------|------|
| 1. Gross debt¹ | | 94.8 | 94.6 | 96.3 | 96.1 | 94.7 |
| 2. Change in gross debt ratio | | -1.1 | -0.2 | -1.7 | -0.2 | -1.4 |
| Contributions to changes in gross debt | | | | | | |
| 3. Primary balance² | | 1.4 | 0.6 | 0.3 | 0.8 | 1.2 |
| 4. Interest expenditure³ | EDP D.41 | 4.1 | 4.0 | 4.5 | 4.4 | 4.3 |
| 5. Stock-flow adjustment | | 1.8 | 2.6 | 1.5 | 0.5 | 0.5 |
| <i>of which:</i> | | | | | | |
| - Differences between cash and accruals ⁴ | | n.a. | n.a. | n.a. | n.a. | n.a. |
| - Net accumulation of financial assets ⁵ | | n.a. | n.a. | n.a. | n.a. | n.a. |
| <i>of which:</i> | | | | | | |
| - privatisation proceeds | | n.a. | n.a. | n.a. | n.a. | n.a. |
| - Valuation effects and other ⁶ | | n.a. | n.a. | n.a. | n.a. | n.a. |
| p.m.: Implicit interest rate on debt⁷ | | 4.9 | 5.1 | 5.3 | 5.2 | 5.0 |
| Other relevant variables | | | | | | |
| 6. Liquid financial assets⁸ | | n.a. | n.a. | n.a. | n.a. | n.a. |
| 7. Net financial debt (7=1-6) | | n.a. | n.a. | n.a. | n.a. | n.a. |

¹As defined in Regulation 3605/93 (not an ESA concept).

²Cf. item 10 in Table 2.

³Cf. item 9 in Table 2.

⁴The differences concerning interest expenditure, other expenditure and revenue could be distinguished when relevant.

⁵Liquid assets, assets on third countries, government controlled enterprises and the difference between quoted and non-quoted assets could be distinguished when relevant.

⁶Changes due to exchange rate movements, and operation in secondary market could be distinguished when relevant.

⁷Proxied by interest expenditure divided by the debt level of the previous year.

⁸AF1, AF2, AF3 (consolidated at market value), AF5 (if quoted in stock exchange; including mutual fund shares).

Table 5. Cyclical developments

| % of GDP | ESA Code | 2007 | 2008 | 2009 | 2010 | 2011 |
|--|----------|------|------|------|------|------|
| 1. Real GDP growth (%) | | 4.0 | 3.0 | 1.1 | 1.6 | 2.3 |
| 2. Net lending of general government | EDP B.9 | -3.5 | -3.7 | -3.7 | -3.2 | -2.6 |
| 3. Interest expenditure | EDP D.41 | 4.1 | 4.0 | 4.5 | 4.4 | 4.3 |
| 4. One-off and other temporary measures¹ | | -0.5 | 0.4 | 0.5 | 0.0 | 0.0 |
| 5. Potential GDP growth (%) | | 3.6 | 3.2 | 2.8 | 2.4 | 2.4 |
| contributions: | | | | | | |
| - labour | | 0.7 | 0.7 | 0.6 | 0.6 | 0.6 |
| - capital | | 1.2 | 1.1 | 1.0 | 1.0 | 1.0 |
| - total factor productivity | | 1.7 | 1.4 | 1.2 | 0.8 | 0.7 |
| 6. Output gap | | 1.8 | 1.6 | -0.1 | -0.9 | -1.0 |
| 7. Cyclical budgetary component | | 0.7 | 0.7 | 0.0 | -0.3 | -0.5 |
| 8. Cyclically-adjusted balance (2 - 7) | | -4.2 | -4.4 | -3.7 | -2.8 | -2.2 |
| 9. Cyclically-adjusted primary balance (8 + 3) | | -0.1 | -0.4 | -0.8 | -1.5 | -2.2 |
| 10. Structural balance (8 - 4) | | -3.7 | -4.8 | -4.2 | -2.8 | -2.2 |

¹A plus sign means deficit-reducing one-off measures.

Table 6. Divergence from previous update

| | ESA Code | 2007 | 2008 | 2009 | 2010 | 2011 |
|--|----------|------|------|------|------|------|
| Real GDP growth (%) | | | | | | |
| Previous update | | 4.1 | 4.0 | 4.0 | 4.0 | n.a. |
| Current update | | 4.0 | 3.0 | 1.1 | 1.6 | 2.3 |
| Difference | | -0.1 | -1.0 | -2.9 | -2.4 | n.a. |
| General government net lending (% of GDP) | EDP B.9 | | | | | |
| Previous update | | -2.7 | -1.6 | -0.8 | 0.0 | n.a. |
| Current update | | -3.5 | -3.7 | -3.7 | -3.2 | -2.6 |
| Difference | | -0.8 | -2.1 | -2.9 | -3.2 | n.a. |
| General government gross debt (% of GDP) | | | | | | |
| Previous update | | 93.4 | 91.0 | 87.3 | 82.9 | n.a. |
| Current update | | 94.8 | 94.6 | 96.3 | 96.1 | 94.7 |
| Difference | | 1.4 | 3.6 | 9.0 | 13.2 | n.a. |

Table 7. Long-term sustainability of public finances

| % of GDP | 2000 | 2007 ¹ | 2010 | 2020 | 2030 | 2050 | 2060 |
|--|------|-------------------|------|------|------|------|------|
| Total expenditure | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. |
| Of which: age-related expenditures | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. |
| Pension expenditure | 10.8 | 11.7 | 13.2 | 17.1 | 21.4 | 24.0 | 24.1 |
| Social security pension | 10.8 | 11.7 | 13.2 | 17.1 | 21.4 | 24.0 | 24.1 |
| Old-age and early pensions | n.a. | 8.8 | 9.9 | 13.1 | 16.3 | 17.9 | 17.7 |
| Other pensions (disability, survivors) | n.a. | 2.9 | 3.3 | 4.0 | 5.1 | 6.1 | 6.4 |
| Occupational pensions (if in general government) | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. |
| Health care | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. |
| Long-term care (<i>this was earlier included in the health care</i>) | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. |
| Education expenditure | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. |
| Other age-related expenditures | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. |
| Interest expenditure | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. |
| Total revenue | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. |
| Of which: property income | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. |
| <i>Of which</i> : from pensions contributions (or social contributions if appropriate) | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. |
| Pension reserve fund assets | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. |
| <i>Of which</i> : consolidated public pension fund assets (assets other than government liabilities) | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. |
| Assumptions | | | | | | | |
| Labour productivity growth | n.a. | 2.5 | 2.9 | 1.8 | 1.7 | 1.7 | 1.7 |
| Real GDP growth | n.a. | 3.8 | 2.9 | 1.3 | 1.0 | 1.2 | 1.4 |
| Participation rate males (aged 20-64) | n.a. | 78.8 | 78.5 | 76.2 | 75.9 | 76.7 | 76.4 |
| Participation rates females (aged 20-64) | n.a. | 55.2 | 60.1 | 60.0 | 60.6 | 61.2 | 61.0 |
| Total participation rates (aged 20-64) | n.a. | 67.1 | 69.4 | 68.3 | 68.4 | 69.1 | 68.8 |
| Unemployment rate | n.a. | 8.5 | 6.2 | 6.2 | 6.2 | 6.2 | 6.2 |
| Population aged 65+ over total population | n.a. | 0.2 | 0.2 | 0.2 | 0.3 | 0.3 | 0.3 |

¹In the SP there are data for year 2007 instead of year 2005 as foreseen in the CoC.

Table 8. Basic assumptions

| | 2007 | 2008 | 2009 | 2010 | 2011 |
|--|------|------|------|------|------|
| Short-term interest rate¹ (annual average) | 4.3 | 4.6 | 2.1 | 2.8 | 2.7 |
| Long-term interest rate (annual average) | 4.3 | 4.0 | 3.1 | 3.3 | 3.0 |
| USD/€ exchange rate (annual average) (euro area and ERM II countries) | 1.37 | 1.47 | 1.38 | 1.38 | 1.38 |
| Nominal effective exchange rate (for countries not in euro area or ERM II) exchange rate vis-à-vis the € (annual average) | n.a. | n.a. | n.a. | n.a. | n.a. |
| World excluding EU, GDP growth | 5.6 | 3.9 | 1.2 | 3.3 | 3.5 |
| EU GDP growth | 2.9 | 1.0 | -1.8 | 0.5 | 2.0 |
| Growth of relevant foreign markets | 5.7 | 3.2 | 1.0 | 3.0 | 4.0 |
| World import volumes, excluding EU | 7.2 | 4.1 | -1.3 | 3.6 | 4.0 |
| Oil prices (Brent, USD/barrel) | 72.5 | 98.5 | 52.1 | 61.7 | 60.0 |

¹If necessary, purely technical assumptions.

* * *