

## 5. GREECE

### Fiscal rebalancing to strengthen ongoing recovery

*Economic growth slowed in the first half of the year but is expected to remain resilient, against the headwinds of a weaker external environment. The ongoing recovery is likely to be supported by gains in export market shares and fiscal policy measures aiming to stimulate investment and reduce labour costs. The general government balance is projected to record a surplus in 2019 for the fourth year in a row, which should facilitate a rapid reduction in public debt. Greece is projected to achieve its agreed fiscal targets, while at the same time improving the quality of its public finances.*

#### Economic growth continues, but at a slightly lower pace

Real GDP growth decreased in the first half of 2019 to 1.5% (y-o-y). The lacklustre performance of growth in the first quarter (1.1% y-o-y) was due to a decrease in net exports as well as a decline in government consumption. These were partly reversed in the second quarter (1.9%) but headline growth remained below the 2018 average.

Despite higher disposable incomes through improving labour market conditions, private consumption declined by -0.1% (y-o-y) in the first half of 2019. In light of strong improvements in business and consumer confidence during the summer, consumption is expected to accelerate in the second half of 2019.

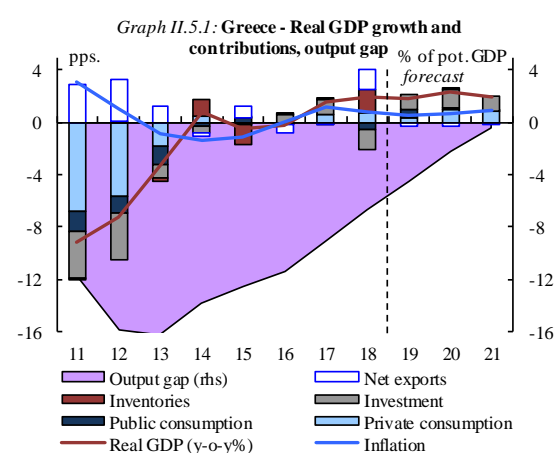
#### Reform efforts are expected to have a positive effect on growth, amid external headwinds ...

The subdued outlook for the euro area economy is set to dampen export growth, though this effect is likely to be cushioned somewhat by the solid market share gains being made by Greek exports.

In addition, the shift in the composition of tax revenues towards less distortionary taxes accompanied by social policy measures, is expected to support investment and employment growth. Against this background, GDP growth is projected to strengthen to 2.3% in 2020 before easing to 2.0% in 2021.

Employment growth is expected to remain above 2% in 2019 and 2020 and to slowly moderate thereafter, bringing the unemployment rate to 14% in 2021. Inflation has been revised down to 0.5% in 2019 due to the impact of the VAT reduction in the second quarter as well as the lower-than-expected rise in oil prices. In 2020 and 2021, inflation is expected to increase to 0.6% and 0.9%, respectively, in line with the ongoing

recovery and inflationary pressure from the tax reforms.



Downside risks to the outlook stem from a slowdown in foreign demand, as well as a persistent under-execution of the budget targeted for public investment. Upside risks are related to the marked improvement in business and consumer sentiment, which has yet to be translated into significant increases in spending. Improved access to finance and bank lending would also provide further upside lift to growth.

#### ...which facilitates the achievement of fiscal targets

Greece's headline budget balance is forecast to record a surplus of 1.3% of GDP in 2019, which would mark its fourth year in a row in surplus. This forecast is supported by favourable revenue collection, on the back of strong growth in disposable incomes as well as a reduction in the spending ceilings, which have helped to accommodate permanent measures worth 0.7% of GDP adopted in spring 2019. The primary surplus monitored under enhanced surveillance is now projected to reach 3.8% of GDP in 2019. The forecast assumes that the pending Public Service Obligation payment for Public Power Corporation

will be covered from the contingency reserve and no additional package of social spending will be paid on top of the current plans because it was not announced with a sufficient level of detail.

The forecast for 2020 incorporates planned cuts in distortionary taxes and a limited increase in family-oriented social benefits. The package (worth 0.6% of GDP) includes a 4 percentage points reduction in the corporate income tax, a reform of personal income taxation that introduces a new rate of nine percent for the lowest incomes, and a reduction in social security contributions for full-time employees. The package is accompanied by measures ensuring fiscal neutrality, supporting a higher collection of indirect taxes and revisions in spending ceilings. Overall, Greece is expected to achieve its primary surplus targets in 2020 and 2021.

The fiscal outlook also reflects the recent Court ruling on the 2016 pension reform and the authorities' commitment to accommodate the

possible fiscal impact of the follow-up legislation within the agreed spending ceilings of the Ministry of Labour. However, the forecast remains subject to uncertainty in view of another Court case on pensions that is still ongoing, while additional pressure could arise from past policy initiatives affecting the public wage bill and the increasing number of temporary personnel. The upside risks from overstated budget ceilings have somewhat diminished but remain substantial.

The headline balance is forecast to deteriorate by 0.3 percentage points of GDP in 2020 and slightly improve in 2021. The projected decrease in 2020 is driven by the payment of the first tranche of the contingent debt-relief measures in 2019 and the expected decrease in the primary surplus in 2020. In view of the projected narrowing of the output gap, the structural balance is projected to gradually decline over the forecast horizon, reaching about 1.2% of GDP in 2021. Greece's public debt-to-GDP ratio is expected to fall significantly from 181.2% in 2018 to 163.1% in 2021.

Table II.5.1:

**Main features of country forecast - GREECE**

	2018			Annual percentage change						
	bn EUR	Curr. prices	% GDP	00-15	2016	2017	2018	2019	2020	2021
GDP	184.7	100.0		0.1	-0.2	1.5	1.9	1.8	2.3	2.0
Private Consumption	125.6	68.0		0.2	0.0	0.9	1.1	0.5	1.5	1.4
Public Consumption	35.4	19.1		0.6	-0.7	-0.4	-2.5	3.4	0.3	0.1
Gross fixed capital formation	20.5	11.1		-3.8	4.7	9.1	-12.2	10.1	12.5	8.1
of which: equipment	9.4	5.1		-1.3	-11.4	22.2	-10.2	11.1	12.8	9.1
Exports (goods and services)	66.7	36.1		3.1	-1.8	6.8	8.7	4.3	3.4	3.0
Imports (goods and services)	67.2	36.4		1.0	0.3	7.1	4.2	5.1	4.0	3.0
GNI (GDP deflator)	183.7	99.5		0.0	-0.3	1.7	1.2	1.9	2.2	1.9
Contribution to GDP growth:		Domestic demand		-0.2	0.4	1.6	-1.3	2.1	2.5	2.0
		Inventories		0.0	0.1	0.0	1.8	0.0	0.0	0.0
		Net exports		0.4	-0.7	-0.1	1.5	-0.3	-0.3	0.0
Employment				-0.4	0.5	1.5	1.7	2.2	2.2	1.4
Unemployment rate (a)				14.5	23.6	21.5	19.3	17.3	15.4	14.0
Compensation of employees / head				2.1	-0.9	0.5	1.3	0.4	1.1	2.0
Unit labour costs whole economy				1.7	-0.3	0.6	1.1	0.7	1.0	1.4
Real unit labour cost				0.0	0.0	0.0	0.5	0.0	0.1	-0.2
Saving rate of households (b)				-	-	-	-	-	-	-
GDP deflator				1.7	-0.2	0.6	0.5	0.8	0.9	1.6
Harmonised index of consumer prices				2.3	0.0	1.1	0.8	0.5	0.6	0.9
Terms of trade goods				0.0	-2.3	1.2	-1.0	0.5	0.2	0.7
Trade balance (goods) (c)				-14.2	-9.3	-10.3	-9.9	-10.7	-11.2	-11.1
Current-account balance (c)				-8.9	-1.1	-1.0	-1.1	-0.8	-1.1	-0.9
Net lending (+) or borrowing (-) vis-a-vis ROW (c)				-7.2	0.4	0.1	-0.1	0.5	0.3	0.6
General government balance (c)				-8.1	0.5	0.7	1.0	1.3	1.0	1.1
Cyclically-adjusted budget balance (d)				-6.3	6.5	5.5	4.5	3.7	2.2	1.3
Structural budget balance (d)				-	5.8	5.2	5.1	3.0	1.8	1.1
General government gross debt (c)				130.1	178.5	176.2	181.2	175.2	169.3	163.1

(a) as % of total labour force. (b) gross saving divided by adjusted gross disposable income. (c) as a % of GDP. (d) as a % of potential GDP.