Eurogroup

Brussels, 6 June 2019
(OR. en)

EG 9/19

EUROGROUP 9
ECOFIN 597
UEM 206

COVER NOTE

From:	Secretary-General of the European Commission, signed by Mr Jordi AYET PUIGARNAU, Director
date of receipt:	5 June 2019
To:	Mr Jeppe TRANHOLM-MIKKELSEN, Secretary-General of the Council of the European Union
No. Cion doc.:	COM(2019) 540 final
Subject:	COMMUNICATION FROM THE COMMISSION **Enhanced Surveillance update – Greece, June 2019**
Enclosed:	COM(2019) 540 final

Delegations will find attached document COM(2019) 540 final.

EUROPEAN
COMMISSION

Brussels, 5.6.2019
COM(2019) 540 final

COMMUNICATION FROM THE COMMISSION

Enhanced Surveillance update – Greece, June 2019

{SWD(2019) 540 final}

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BACKGROUND

Economic developments and policies in Greece are monitored under the European Semester for economic policy co-ordination and under the enhanced surveillance framework according to Regulation (EU) No 472/2013 [1]. The activation of enhanced surveillance for Greece [2] acknowledges the fact that over the medium term, Greece needs to continue adopting measures to address the sources or potential sources of economic and financial difficulties, while implementing structural reforms to support robust and sustainable economic growth.

Enhanced surveillance provides a comprehensive framework for monitoring economic developments and the pursuit of policies needed to ensure a sustainable economic recovery. It provides for a regular assessment of recent economic and financial developments in Greece, as well as for monitoring sovereign financing conditions and updates of the debt sustainability analysis. Enhanced surveillance also provides the basis for assessing the general commitment given by Greece to the Eurogroup of 22 June 2018 to continue and complete reforms adopted under the European Stability Mechanism (ESM) programme and to ensure that the objectives of the important reforms adopted under the financial assistance programmes are safeguarded. Greece reiterated these commitments in the Eurogroup statement of 5 April 2019 [3]. In that context, enhanced surveillance provides the basis for monitoring the implementation of specific commitments to complete key structural reforms started under the programme in six key areas by agreed deadlines up to mid-2022, namely: (i) fiscal and fiscal-structural policies, (ii) social welfare, (iii) financial stability, (iv) labour and product markets, (v) privatisation and (vi) the modernisation of public administration [4]. Fifteen specific commitments have a deadline of mid-2019, progress on which is assessed in this report.

This is the third enhanced surveillance report for Greece. It is issued alongside the assessment of Greece's Stability Programme and the Commission Recommendation for country-specific recommendations to Greece under the European Semester. This report is based on the findings of a mission to Athens between 6 and 8 May 2019 conducted by the Commission in liaison with the ECB [5]. The IMF participated in the context of its 2019 Article IV surveillance cycle, while the ESM participated in the context of its Early Warning System and in line with the Memorandum of Understanding of 27 April 2018 on working relations between the European Commission and ESM.

The Eurogroup on 22 June 2018 agreed that the package of debt relief measures for Greece should include incentives to ensure a strong and continuous implementation of the reform measures agreed in the programme. To this end, the implementation of some of the agreed debt measures will be made available to Greece subject to compliance with its commitments on reform continuity and completion, based on positive reports under enhanced surveillance, in semi-annual tranches up to mid-2022. Following the Eurogroup on 5 April 2019, the first tranche of policy-contingent debt measures was released, taking into account the assessment of the implementation of Greece's commitments for end-2018 in an updated enhanced surveillance report adopted by the Commission on 3 April 2019 [6].

(1) Regulation (EU) No 472/2013 of the European Parliament and of the Council of 21 May 2013 on the strengthening of economic and budgetary surveillance of Member States in the euro area experiencing or threatened with serious difficulties with respect to their financial stability, OJ L 140, 27.5.2013, p. 1.
(2) Commission Implementing Decision (EU) 2018/1192 of 11 July 2018 on the activation of enhanced surveillance for Greece, OJ L 211, 22.8.2018, p. 1, and Commission Implementing Decision (EU) 2019/338 of 20 February 2019 on the extension of enhanced surveillance for Greece.
(3) https://www.consilium.europa.eu/en/press/press-releases/2019/04/05/eurogroup-statement-on-greece-of-5-april-2019/
(4) https://www.consilium.europa.eu/media/35749/z-councils-council-configurations-ecofin-eurogroup-2018-180621-specific-commitments-to-ensure-the-continuity-and-completion-of-reforms-adopted-under-the-esm-programme_2.pdf
(5) ECB staff participated in the review mission in accordance with the ECB's competences and thus provided expertise on financial sector policies and macro-critical issues, such as headline fiscal targets and sustainability and financing needs. The review mission was preceded by a technical mission from 1 to 4 April.
(6) Given that half of last year's and the full amount of this year's instalments of the interest step-up margin were eligible for a waiver, the policy-contingent debt measures exceptionally amounted to some EUR 970 million. https://www.esm.europa.eu/press-releases/efsf-approves-reimbursement-and-reduction-step-interest-margin-greece

ECONOMIC OUTLOOK

Greece's economic recovery is expected to continue in 2019. Following an annual growth rate of 1.9% in 2018, real GDP growth is forecast to reach 2.2% in both 2019 and 2020, supported primarily by domestic demand. Private consumption has been a steady contributor to the recovery and is forecast to perform well again in 2019. Public consumption may support growth this year according to budgetary plans, though Greece's track record of underspending implies a downside risk. The same holds for public investment, while a rebound in residential investment suggests that the housing market is on a normalisation path against headwinds from the still shrinking supply of bank credit in this market segment. Buoyant export performance was a key growth driver in 2018, but is expected to moderate in 2019 amid a slowdown of the external environment. However, exports of goods and services are still forecast to increase by close to 5% in 2019 and close to 4% in 2020 in real terms.

The labour market shows further improvements, although the decline in unemployment halted in October 2018 at 18.6%, hovering around that level until February 2019. Employment still showed year-on-year growth of 2.4% in February, though this reflects earlier gains in employment rather than recent improvements. Detailed monitoring is foreseen to assess the impact of the recent increase of the minimum wage and the abolition of the sub-minimum wage on the pace of the recovery in the labour market. Inflation is expected to remain muted throughout 2019, and to pick up only beyond 2020 as the output gap closes.

Downside risks dominate the forecast in the short and medium term. The forecast is heavily reliant on technical assumptions regarding the full execution of the budget ceilings for investment and ordinary spending. Vulnerabilities in the banking sector and increasing wage costs might pose further challenges for the recovery of domestic demand and in particular of investment. In case of a stronger-than-expected deterioration in the external environment, or a higher pass-through to Greece, the recovery may prove to be more sluggish.

FISCAL POLICIES AND OUTLOOK

Greece over-achieved the agreed primary surplus target of 3.5% of GDP in 2018, largely due to continued under-execution of spending ceilings, notably on public investment. The general government headline balance recorded a surplus (1.1% of GDP) for the third year in a row, while the primary surplus monitored under enhanced surveillance reached 4.3% of GDP, well above target. The primary surplus would have been even larger, but the emerging fiscal space allowed the authorities to clear unforeseen liabilities following from a Court decision and pay a means-tested benefit to households at the end of 2018. For the most part, the under-execution of expenditure arises due to setting budget ceilings above the actual spending capacity of budgetary units and underlines the need for proper assessments of the state of play on major spending projects and realistic estimates of costs of new policies. These issues have occurred for a number of past years. The European institutions are supporting the authorities to address the reasons of the systematic underspending in order to improve budgetary practices and to fully utilise the resources available for public investment from both the EU and national sources to support growth.

The Commission 2019 spring forecast, published before the adoption of new fiscal measures on 15 May 2019, indicated that the primary surplus would reach 3.6% of GDP in 2019, which is considerably lower (by 0.5% of GDP) than the projection of the Greek authorities in their Stability Programme. The difference in the forecasts mainly arises due to the authorities' more favourable macroeconomic scenario and their approach to the allocation of the public investment budget between entities outside and inside general government. More specifically, this involves a re-assignment of part of the expenditure previously foreseen for investment to grants to state-owned enterprises, without the grants being used for additional spending by their recipients. This accounting operation has a balance-improving effect in the projection of the authorities (0.3% of GDP in 2019 and 0.2% of GDP in 2020). In the absence of adequate information on the nature or the specific recipients of the additional grants, this re-assignment of expenditure is not reflected in the projections of the European institutions. In contrast, the fiscal projections prepared by the European institutions assume full execution of the ceilings in line with standard practice.

In their Stability Programme, the Greek authorities announced their intention not to implement the pre-legislated income tax credit package, which was set to enter into force in January 2020. This means not proceeding with measures that broaden the tax base and create fiscal space of 1% of GDP for growth-enhancing reforms of the tax system.

On 15 May 2019, and thus after the submission of the Stability Programme, the authorities adopted a package of permanent fiscal measures which the European institutions estimate will have a fiscal cost of more than 1% of GDP in 2019 and beyond. The measures include new instalment schemes for debts on taxes and to social security funds and municipalities, reductions in selected VAT rates, the introduction of a 13th pension, and a reversal of an earlier reform of survivors' pensions. Projections by the European institutions show that the adoption of the fiscal measures on 15 May 2019 poses a risk for the achievement of the agreed primary surplus target of 3.5% of GDP in 2019 and beyond. The magnitude will depend on the take up of the new instalment schemes and their impact on existing ones. Moreover, and as outlined in the assessment of the Greek Stability Programme, the measures also raise concerns on the achievement of the medium-term budgetary objective (MTO) in structural terms in 2020. A re-assessment of compliance with the requirements of the preventive arm of the Stability and Growth Pact will be carried out in autumn 2019, including a revision of the applicable benchmark for net expenditure growth in 2020.

The quality of the fiscal measures adopted on 15 May 2019 is of concern given the objective to make public finances more growth-friendly and to direct a higher share of social spending towards groups who face the highest incidence of poverty. For example, the duration of the new instalment schemes is very long (120 monthly payments), and the schemes contain only limited provisions to assess the ability to pay; it is recalled that a key reform enacted in 2013 replaced all former settlement schemes by a single 'basic' scheme accessible under strict eligibility criteria. Lower VAT rates for food products, restaurants and food services, electricity and gas contrast with an important measure adopted in July 2015, while leaving in place the very high 24% standard rate and further increase the VAT gap, which is already the 2nd highest in the EU. Furthermore, the introduction of a permanent 13th pension and relaxation of the eligibility criteria for survivors' pensions partially alter measures adopted in 2012 and 2016 respectively. These reforms will increase public spending on pensions, which is already the highest as a share of GDP in the EU, and is in contrast to measures adopted in the 2019 budget which directs a higher share of spending on social benefits towards the young people and working-age population who face much higher risks of poverty. Overall, the adopted measures on pensions and VAT are targeted at consumption and will absorb a considerable amount of fiscal space that was envisaged in legislation adopted in 2017 for growth-enhancing reductions in labour and corporate tax rates.

The Greek authorities announced their intention to adopt a set of additional expansionary fiscal measures for 2020 in autumn this year. These include reductions in tax rates, as well as the introduction of a series of exemptions and tax expenditures or subsidies. The authorities have provided only a partial estimate of the fiscal impact of these measures, totalling EUR 1.2 billion or 0.6% of GDP. For now, these announcements remain statements of future policy intention and an assessment on the quality of the measures and their impact on the achievement of the agreed fiscal targets would only be carried out if detailed proposals are actually tabled.

The Greek authorities have also announced their intention to revisit the agreement reached with European partners in June 2018 as regards the annual primary surplus targets of 3.5% of GDP up to 2022. Linked to this, the authorities are considering transferring part of the cash reserves generated by the 2016-2018 fiscal over-performance to an escrow account. Any proposal which alters the agreement reached with European partners in June 2018 would need to be discussed at the Eurogroup in the context of an updated debt sustainability analysis.

Greece's public finances continue to face important fiscal risks with respect to ongoing court cases and the possible broadening of exemptions from the unified wage grid. No new information on the pending case on pensions has become available since the publication of the second enhanced surveillance report, and the ruling by the Council of State on the constitutionality of the cuts in seasonal bonuses is yet to be published. In addition, risks to the integrity of the unified wage bill have already started to materialise and remain a source of concern. They stem mainly from the decision to exempt certain officials at the Ministry of Finance from the unified wage grid in October 2018, a decision that has been extended to other public entities since. While the cost of this measure is relatively contained, it increases the likelihood of legal challenges by other groups of public officials and/or of further discretionary extensions. Establishing a unified wage grid was one of the key reforms implemented under the financial assistance programmes. In the event of court rulings overturning key structural elements of reforms agreed under the programme, the recurrent fiscal implications of such rulings should be largely addressed by actions within the same policy area.

FISCAL STRUCTURAL POLICIES

Greece has made progress in the reform of the ENFIA property tax valuation framework, though preparations for a mid-2019 realignment of property values have not yet been completed. Considerable progress has been made on the operational, IT and legal aspects of the valuation process, and there has been agreement that a new nationwide valuation exercise by valuers is not needed in mid-2019 (which had been a specific commitment). At the same time, work still needs to be completed for a partial realignment of property tax values in 2019, which the authorities have been working towards as an intermediate step towards fully aligning property tax zonal values with market prices by 2020.

Progress is underway on other smaller tax policy reforms. With the help of technical support, reviews are currently underway of the system of Stamp Duty and of the potential individual liability of corporate managers for tax offences.

The hiring of staff to the Independent Authority for Public Revenue (IAPR) remains slow. Only a marginal increase was observed during the first quarter of 2019: if the current hiring trend remains, there is a risk that the specific commitment for end-2019 may not be met. In addition, a number of complementary measures were adopted earlier in the year to ensure the continued strengthening of the IAPR's capacity and follow-up actions are expected for the next months, in particular related to Human Resource reform, implementation of the strategic Blueprint and IT arrangements.

Progress on other commitments and reform items is mixed. On customs, continued progress has been made in delivering on the anti-smuggling strategy and the fuel tank action plan. Work on promoting electronic payments is proceeding well, while on the other hand the planned asset registry has not been completed. Finally, a recent law amendment raises potential overlaps between the responsibilities of General Secretariat for IT Systems and the IAPR, and it is essential that a cooperation framework is agreed.

The results for the first quarter of 2019 on key performance indicators set by the IAPR present a mixed picture. Tax collection has been weaker than targeted, while key performance indicators in most other areas, including collection after audits, are being met. The Joint Centre for the Collection of Social Security Debt (KEAO) continues to meet its targets for the collection of social security debt, which are more ambitious than for the preceding year, though debt collection in April 2019 decreased year-on-year. IAPR and KEAO are working towards strengthening their co-operation within a coherent framework. In this context, the adoption of relevant legislation to allow KEAO to apply the IAPR's classification of the persons/entities considered to have 'uncollectable' debt should be adopted without further delays.

New instalment schemes were adopted for tax, social security and municipal debt with up to 120 monthly instalments. This alters a key reform enacted in 2013 that replaced former settlement schemes by a single 'basic' scheme accessible under strict eligibility criteria in a manner which reinstates design problems of earlier schemes. While the scope of the social security debt is more targeted, as its focus is on the self-employed and it links entitlements to contributions, the new instalment scheme on taxes does not include any specific prioritisation for eligibility or any prior viability assessment. In light of past experience, the announcement of a new instalment scheme may have contributed to weakening revenue collection and can create risks to payment discipline.

Progress with arrears clearance remains disappointing. The Greek authorities have committed to clear the stock of arrears, avoid the accumulation of new arrears (a continuous action) and to complete the implementation of reforms identified by the Hellenic Court of Auditors by mid-2019. Despite the fact that the net stock of arrears has decreased since the end of the programme, the pace of reduction has significantly slowed and new arrears continue to be created in some sectors. The end-March 2019 stock of net arrears stood at EUR 1.4 billion, and while EUR 0.3 billion lower than the end of programme (August 2018), this is the same level as at end-December 2018. Of the total EUR 7 billion disbursed for arrears clearance during the programme, EUR 0.1 billion remain unused by end-April 2019.

The authorities are currently implementing structural measures to address the bottlenecks of arrears management, based on the recommendations of systemic nature issued by the Hellenic Court of Auditors. To this end, the authorities have made progress with the implementation of two action plans, in the fields of responsibility of General Accounting Office and the IAPR respectively. The overall implementation of the reforms in both action plans will be assessed by the Hellenic Court of Auditors in mid-2019 in the context of their follow-up audit.

A way forward was agreed on the abolition of *ex ante* audits performed by the Hellenic Court of Auditors for entities outside central government. The authorities have amended relevant legislation so as to ensure that hospitals and the social benefits agency are no longer subject to *ex ante* audits, while the abolition will take place at end-July 2019 for the remaining extra-budgetary funds and municipalities in light of capacity considerations. The authorities have committed to undertake a set of specific supplementary actions, with a view to ensuring that the abolition of *ex ante* audits, which brings Greece closer in line with international practice, runs smoothly. The authorities will need to stick with the full arrears clearance plan and implement complementary actions targeting the structural sources of arrears creation.

As regards other public financial management reforms, the authorities are moving forward with implementing a Treasury Single Account at the Bank of Greece and with setting up a Unified Chart of Accounts. Some progress on the Treasury Single Account has been made in the first months of 2019 though the most important measures still remain to be taken. An important intermediate step was the rollout of the Unified Chart of Accounts for the 2019 State budget, and the authorities will need to further build on this with a view to ensuring full implementation of the Unified Chart of Accounts by 2023.

SOCIAL WELFARE

The authorities have recently passed legislation that repeals important elements of the pension reforms adopted in 2012 and 2016 and leads to an increase in spending on pensions as a share of GDP. In May 2019, the authorities repealed the 2016 reform of the survivor's pensions that modernised and aligned the pension entitlements to standard practices of other Member States, loosening eligibility criteria and increasing entitlements. Furthermore, the authorities have reinstated a permanent 13^{th} pension that had been eliminated in 2012. Both measures will decrease the relative share of social benefits benefiting the young and working age population where the risk of poverty is much higher than for pensioners.

The pace of collection of the health care clawbacks has seen a recent improvement, and collection of the clawback for 2018 is currently ongoing (mid-2019 specific commitment). Around one third of the clawback has been completed for outpatient pharmaceuticals and drugs circulated through pharmacies affiliated with the national health insurance fund, while for privately provided services the amount for 2018 has not been quantified yet. There are also still some backlogs in the clawbacks for previous years. Despite improvements in collection, the generation of new clawbacks is high and has been increasing over time to levels which may soon become unsustainable. This underlines the need for more sustained efforts to implement structural measures designed to curb supply-induced demand. In this respect, some recent measures, including changes to the repricing mechanism for pharmaceuticals, go in the wrong direction and may exacerbate the situation as regards the balance of burden sharing between the public sector and private companies.

The roll-out of primary health care is proceeding but at a slow pace and with marked disparities across the country. The authorities fulfilled the end-2018 commitment of opening at least 120 primary health care units, and have meanwhile exceeded the target with 124 openings. However, the broader roll-out of primary health care occurs at a slow pace and with uneven distribution across the country, partly due to challenges with the recruitment of general practitioners.

Progress on centralised health procurement continues at a slow pace, with staff constraints translating into still limited capacity to launch new tenders. Reaching the necessary minimum staffing level will be a key determinant of the capability of the centralised procurement body for healthcare to operate effectively and systematically to realise the potential savings coming from central procurement.

In the area of social welfare, a new housing benefit for renters has been introduced, further enhancing the effectiveness of the Greek social welfare system. The scheme addresses housing cost overburden by providing a means-tested subsidy to low-income households for paying the rent on their primary residence. As of end-April 2019, some 240 000 applications have been accepted, corresponding to some 630 000 individuals (close to 6% of the Greek population), a result in line with initial expectations.

The reform of the system of disability benefits is advancing but with significant delays. Upgraded and simplified procedures are being gradually introduced throughout the country. The new approach to determine disability status based on both medical and functional assessment (whose application is a mid-2019 specific commitment) is to be developed on the basis of a pilot project that received technical support of the World Bank. In view of administrative delays, the evaluation of the pilot is only set to be completed by the end of the year, implying that the project can only be concluded in 2020. A revised timeline detailing the intermediate steps and a final deadline for adoption should be defined.

The Social Solidarity Income scheme is reaching its maturity. In the first four months of 2019, the scheme reached about 270 000 households (about 500 000 individuals), for an annual expenditure of around EUR 680 million. This is slightly lower than last year, likely reflecting a combination of more effective controls and eligibility checks and the general improvement of the economic and social situation. Meanwhile the implementation of the second and third pillars of the Social Solidarity Income (an end-2019 specific commitment), is progressing. With respect to the second pillar (social inclusion), a network of Community Centres has been established throughout the country with the support of the European Social Fund, expanding the provision of social services at local level in a coordinated way. For the third pillar (labour market integration), the authorities are shifting to a more systematic approach to the design and management of active labour market policies, which is currently tested in a pilot project.

FINANCIAL SECTOR POLICIES

The situation of the financial sector continues to be challenging with improvements occurring at a very slow pace and remaining significant vulnerabilities. On a positive note, the liquidity situation of Greek banks has further improved. Greek banks still rely primarily on their internal capacity to generate capital, which has been further weakened by their low profitability due to their poor asset quality. Although broadly adequate, the capital position of the banking system slightly deteriorated during 2018 in a context of low profitability and weak asset quality, while deferred tax credits continue to account for a sizeable part of core tier 1 capital. Non-performing loans (NPLs) have been gradually decreasing, but remain elevated, amounting to EUR 81.8 billion at end-2018 in comparison with a peak of EUR 107.2 billion in March 2016. This translates into a NPL ratio of 45.4%, which is 1.8 percentage points lower than the previous year. Despite the progress made to date, further major efforts are required to achieve a faster NPL reduction.

Work is ongoing on a range of initiatives to strengthen the NPL resolution framework, but the pace of implementation remains uneven, and additional efforts are warranted. More specifically:

- The conduct of electronic auctions is proceeding across the territory, though at a somewhat slowing pace. Still, a large share of auctions (approximately two-thirds in the first quarter of 2019 according to data provided by the Greek authorities) is cancelled, suspended or is unsuccessful. No action has been taken so far to address these issues. The issue of possible procedural abuses is under assessment by the authorities together with the Hellenic Bank Association (with report due in September 2019), and mitigating actions should be enacted in the context of the ongoing review of the implementation of the Greek Code of Civil Procedure.

- The process of the gradual elimination of the backlog of cases in the context of the household insolvency framework is significantly behind schedule. Collection and processing of data on the clearing of court backlogs in the household insolvency framework is ongoing; its completion should support the elaboration of a revised action plan by the authorities by end-June 2019, while the impact of the new mechanism for the protection of primary residences should be factored in later in the year. Preliminary data points to an increase of cases in the first quarter of 2019, whilst the authorities in their indicative trajectory envisaged a reduction. Therefore it is important to increase processing capacity to achieve the full elimination of the backlog of cases by 2021.

- Following the adoption of primary and secondary legislation establishing a new system for the protection of eligible primary residences in support of the restructuring of non-performing loans, technical work on the electronic platform is ongoing. The complexity of the process has led to a revision of the initial time frame, with the platform now scheduled to be operational by end-July 2019. This should not affect its planned expiry at the end of 2019 however it might adversely affect the enforcement procedure in the second and third quarter of 2019. With respect to the required State aid approval of the protective framework by the Commission, the Greek authorities intend to submit the official request shortly. An important pending issue regarding the effectiveness of the new framework in the context of NPL resolution is the required enactment of an extension of the tax treatment of write-offs that expired at the end of 2018, which should be undertaken in a timely manner.

- The Greek authorities committed in the context of the second enhanced surveillance report to harmonize and improve in the coming months in a holistic fashion the bankruptcy and insolvency regimes. The Greek authorities proposed to address the issue either through a law-drafting committee or by means of a working group. While no proposal has been received so far, they committed to present a more concrete proposal shortly.

- Work on the evaluation of the implementation record of the reformed Code of Civil Procedure is ongoing, and advancing towards completion of the data-gathering phase.

- The authorities reported further progress in the provision of financial training to judges, notably in the area of household insolvency. The authorities have also continued with the appointment of successful candidates of recently completed personnel selection competitions for court clerks.

- While the use of the out-of-court workout mechanism recorded modest increases up to the first quarter of 2019, recently adopted legislative amendments to the framework are of concern. These amendments have further extended its cut-off date regarding the time limit set to the inclusion of debt in the restructuring, for the second time since the adoption of the law. The stipulation of a firm cut-off date is an important feature of this mechanism because it discourages strategic default planning and thereby helps avert moral hazard.

- The large stock of called loan guarantees by the state is subject to a low processing rate and a high rejection rate. The action plan adopted by the authorities in March 2019 is so far on track, but does not allow for a full clearance of the guarantees called in a reasonable timeline. Some additional measures are considered to address the clearance process issue, notably the temporary recruitment of personnel.

- Well-designed systemic initiatives could be helpful elements in the toolkit of NPL resolution. Further efforts are needed in scrutinizing all available policy options that could support all banks in a swift NPL reduction. The authorities are continuing their work on an Asset Protection Scheme, but to date there has been no progress in exploring whether the scheme can also be complemented through an Asset Management Company.

In line with Greece's Eurogroup commitments, the status of the Hellenic Financial Stability Fund will remain unchanged and it will continue its efforts to achieve its ultimate goal of reprivatising its stakes in the systemic banks in the coming years. The potential involvement of the authorities in the final stage of implementing the Funds' divestment strategy is still under discussion. In early May 2019, the appointments to the vacant positions both in the Executive Board (including the Deputy Chief Executive Officer) and the General Council of the Fund have finally been enacted.

LABOUR MARKET

The Greek authorities continue monitoring labour market and wage developments and intend to conduct an ex-post assessment of the recent increase in the minimum wage. To this end, the Ministry of Labour has been developing a monitoring tool based on administrative data. According to preliminary data, employment growth in the private sector was robust in the first months following the increase in the minimum wage (February-April 2019), with a large increase in the number of registered contracts. The use and integration of additional data sources should enable a more robust estimation of the effects of recent policy changes, and technical support to this effect from the World Bank is expected to start in June 2019.

The action plan to fight undeclared work is progressing smoothly. A higher number of inspections was carried out in 2018 compared to the previous year, and data from inspection results show a positive picture, with a steady reduction in the incidence of undeclared work in high-risk sectors.

A new provision on the rules for dismissal (whereby a dismissal is not valid if it is not based on a 'valid reason'), was adopted in May 2019. According to the Greek authorities, this provision does not appear to materially alter the current rules, as the right of employees not to be dismissed without a 'valid reason' had already been introduced in the Greek legal system with the ratification of the Revised European Social Charter in 2016. It remains to be seen to what extent the new provision, which the authorities argue aims at enhancing legal clarity will affect the overall number of dismissals, lead to an increase in litigation, with a higher number of dismissal decisions being challenged in court, and/or lead to an improved processing of such cases by the courts.

The Greek educational system faces long-standing challenges. These include inadequate allocation of resources, low autonomy, poor educational outcomes, skill mismatches, and weaknesses in the governance of higher education institutions. In the absence of a comprehensive prior evaluation, it is unclear how the current policy of upgrading technical education institutions to universities will improve the fragmented higher education landscape or the need to make tertiary education more relevant for the labour market. In this context, it is recalled that the 2018 OECD country review on Greece (7) made specific policy recommendations to improve the quality and efficiency of the system.

PRODUCT MARKETS AND COMPETITIVENESS

Notwithstanding progress over the last years, Greece still faces major challenges as regards competitiveness. This is illustrated in its stagnating or even slightly deteriorating performance in a range of widely used competitiveness metrics (such as the World Bank Doing Business ranking) (8). An improved business environment would also contribute to addressing the structural component of sluggish productivity growth by tackling the crisis-induced investment gap, the emigration of skilled labour and the still high long-term unemployment.

More needs to be done on export promotion to reach the authorities' export/GDP target of 50% by 2025. The pace of implementation of two related action plans has been mixed. Efforts should focus on increasing the exporters' base, as well as the export propensity of the Greek economy as a whole. Further work is also required on removing unnecessary procedural impediments to trade and increasing the openness of the economy, including through the further streamlining of customs procedures with the help of technical support provided through the Commission services.

On the investment licensing reform, significant work is underway. Despite delays in certain areas, the reform appears to be broadly on track with deadlines on specific investment licensing commitments for the outer years (ICT system, inspections framework law, extension of simplification, reform of nuisance classification). Whilst continued efforts to complete reform commitments are welcome, the adequacy of existing control mechanisms to contain the risk of potential policy reversal remains uncertain. Greater engagement of all stakeholders is needed to safeguard the integrity of reforms implemented thus far and ensure completion of the reform in the future.

It is important to assess the actual impact of product market reforms adopted in recent years so that they can be fine-tuned and strengthened where needed. An impact assessment conducted by the Centre of Planning and Economic Research on reforms in the areas of pharmacies, over-the-counter drugs and Sunday retail trading suggests that these reforms have already had a positive effect on competition and job creation. The Centre of Planning and Economic Research will provide an updated impact assessment of these reforms in September 2019 and further, undertake an impact assessment of prior reforms affecting engineers (including public engineers), lawyers, and private clinics.

The cadastre project has further progressed in the recent months. The Commission has taken the decision to co-finance with structural funds the last set of contracts (about EUR 84 million), and a technical support is made

(7) Education for a Bright Future in Greece, OECD, April 2018

(8) The challenges facing the business environment in Greece were discussed in the context of the European Semester Conference organised by the European Commission in collaboration with the Foundation for Economic & Industrial Research (IOBE) in Athens, in March 2019. https://ec.europa.eu/info/events/integrating-greece-european-semester-policy-framework-2019-mar-20_en

available [9]. The current round of declaration of properties around the country is progressing satisfactorily, with an electronic platform in place and a sizeable number of cadastral offices operating across Greece. That said, progress with the establishment of the future institutional framework for the cadastre has been mixed, and the government has committed to strengthen the team implementing the migration into the new Agency and to prepare a detailed plan for the integration of the mortgage offices to meet the deadlines set with the advice of the World Bank.

The preparation of the forest maps (a mid-2019 commitment) is expected to be on time. As of May 2019, forest maps for 55% of the territory have been uploaded for consultation, of which maps for 41% of the territory are already ratified; the maps for 98% of the territory are expected to be produced by July 2019. The remaining 2% of the country's forest maps have been contracted in May 2019 and will be finished by February 2020. A recent decision by the Council of State raised questions about the temporary exclusion of "building concentrations" from the forest maps. The authorities intend to adopt legislation swiftly in order to address the Council of State's concerns and avoid implications for the timely completion of the forest maps.

Progress with the implementation of energy market reforms has slowed notably during the past few months. The divestiture of PPC's lignite plants (a delayed end-2018 specific commitment) was relaunched after the first deadline resulted in no bids being accepted. A new timeline had been agreed which should close by the end of June 2019,which should include a fairness opinion on any offers. A unilateral decision extending the process deadline to July 15th was made by PPC following consultation with the Ministry of Energy and Environment, and as such, the closure will not be made within the agreed deadline. Whilst Greece has made some initial steps towards the introduction of the target model for the electricity market (mid-2019 specific commitment), it seems clear at this juncture that the go-live of the intraday, day-ahead and balancing markets, already delayed from the initial plan of April 2019, will not occur until 2020. These delays will have knock-on effects for Greece's coupling with the neighbouring markets of Italy and Bulgaria. Meanwhile the NOME electricity auctions continued with its allocated quantities, and the delays to the lignite divestiture meant that a planned correction mechanism was not triggered. On a positive note, PPC's market share has slowly receded to below 77% in March 2019, down from 80% at the time of the last enhanced surveillance report but still some way off the original programme objective of PPC's market share going to below 50% by 2020. The recently-released 2018 financial results for PPC show a strong decline in profitability and a worsening of cash flow issues, which calls for determined efforts to address structural issues, including pricing policy and arrears collection. Meanwhile, reforms in the gas market have advanced overall, with the completion of the sale of the transmission network operator DESFA and the split of the gas supply company DEPA into commercial and infrastructure parts, with a view to preparing the agreed privatisation transactions in line with unbundling requirements. The Renewable Energy Source (RES) account maintained its surplus, but cash flow issues remain, affecting RES producers.

HELLENIC CORPORATION OF ASSETS AND PARTICIPATIONS (HCAP) AND PRIVATISATIONS

Greece made commitments to European partners in June 2018 to continue and complete the important work of HCAP, which gathers under a single institutional structure a significant portfolio of assets and shareholdings in public enterprises. The Eurogroup statement of June 2018 foresees that the strategic plan of HCAP will be implemented on a continuous basis. In addition, the authorities committed to complete the review, and replacement if required, of Board members of all state-owned enterprises (SOEs) by mid-2019. The implementation of the strategic plan has proceeded as planned and the Board review is progressing well. Up to the present, HCAP has appointed 39 Board members (executive and non-executive) in its direct and other subsidiaries. That said, in order to ensure that the process can be sustained over time in an effective manner, it is necessary to ensure competitive remuneration of professional Board members.

Progress has also been made in improving corporate governance in the SOEs that form part of HCAP. The implementation of the coordination mechanism that governs the interaction between the authorities and HCAP regarding the mandates and objectives of the SOEs under HCAP has been launched and it is at an advanced stage for the first four SOEs. However, recent legislation and actions in certain sectors (e.g. regional

(9) Commission Implementing Decision C(2019)299 of 23.1.2019 approving the financial contribution to the major project "Compilation of the preliminary cadastral base-maps and development of the cadastral database for public presentation in the areas of the 4th generation of cadastral surveys" selected as part of the operational programme "Competitiveness, Entrepreneurship and Innovation" in Greece.

airports) appear to potentially overlap with the function of the coordination mechanism, or to affect the HCAP's rights in respect of certain assets transferred to it, which should be rectified and avoided going forward.

Implementation of the Asset Development Plan is key to stimulate private investment, increase efficiency, and provide financing to the State. In June 2018, the authorities made a specific commitment to Eurogroup partners to implement the Asset Development Plan, which will be updated every six months, and in this context to complete the transactions on Hellenic Petroleum (HELPE) and the marina of Alimos by mid-2019. Further commitments were taken for end-2019 and beyond. In addition, the transaction on Hellinikon (development of the site of the former Athens International Airport, end-2018 specific commitment) has remained pending despite good progress, taking into account the complexity of the project. On Hellinikon, the authorities have continued the efforts to complete the conditions precedent to allow the transfer of shares to the preferred investor. If the authorities continue the strong efforts, financial closing could be feasible in the coming months.

Progress on the transactions in the Asset Development Plan which are due to be completed in 2019 (mid and end-2019 specific commitments) is behind schedule, with progress in smaller transactions being offset by delays elsewhere. The state of play can be summarised as follows:

- Marina of Alimos: The preferred bidder was selected in an e-auction procedure of April 2019; progress is satisfactory although the financial closing is not expected before the fourth quarter of 2019.

- The Hellenic Petroleum (HELPE) transaction is subject to delays as no binding offers were submitted for the joint sale. Agreement has been reached with the Greek authorities so that the Hellenic Republic Asset Development Fund (TAIPED) is given the technical mandate to explore all options available towards proceeding with the transaction.

- The sale of 30% of Athens International Airport (AIA): the process remains stalled in view of disagreements between the Greek authorities and AviAlliance, shareholder of 40% stake in AIA, regarding the corporate governance rights accompanying the 30% stake post sale. The Greek authorities committed to seek an immediate resolution of the issue, with a view to launching the tender process for the sale of 30% of AIA by end-June 2019.

- DEPA - Public Gas Corporation: the invitation for the expression of interest for the sale of 50% plus one share of DEPA Commercial is expected to be published in the coming weeks and it should be in accordance with the term sheet agreed between the authorities and the European institutions.

- The Egnatia transaction entails the award of a long-term concession for the operation and maintenance of the motorway and its three vertical axes. In January 2019, the authorities agreed to a number of actions to deal with the recurrent obstacles to the concession. Most of the agreed actions due so far have been implemented in line with technical feasibility. It is imperative that the authorities complete all the outstanding actions needed to allow the submission of binding offers to take place.

- Regional Ports: There is significant investor interest to operate specific and/or combined port activities/services by means of sub-concession agreements in the ports of Alexandroupolis, Kavala, (end-2019 specific commitments), Igoumenitsa and Kerkyra (mid-2021 specific commitments). The Expression of Interest for the two ports, however, requires the prior issuance of a Joint Ministerial Decision that will include the specific activities subject to sub-concession as well as the fees to be paid by the sub-concessionaires to the relevant port authorities.

PUBLIC ADMINISTRATION AND JUSTICE

Overall, progress has been made with the specific mid-2019 commitments in the area of public sector reform. Regarding the preparation of an independent assessment of the delayed selection process of Administrative Secretaries, the authorities have requested technical support from the Commission and the final assessment is expected to be completed by June 2019, with follow-up actions due by September 2019; at the same time, the pace of appointments of Administrative Secretaries remains very slow. The selection process for all 90 Directors-General has been completed, while one third of Directors have been appointed (with the rest expected by end-July), and the recruitment of Heads of Division is expected to be launched by end-June and completed by October. The 3rd mobility cycle that was launched in August 2018 is progressing; while the process is subject to delays and impediments should be addressed, the gradual increase in the number of entities and applications for each cycle is a welcome signal that the public sector has embraced this public administration reform. The performance assessment cycle for 2018 is expected to be completed on time.

Continued progress has been made towards establishing an integrated Human Resource Management System, which should be on track to be completed by end of 2019. More specifically, 745 general government entities (approximately half of the total) have completed their digital organigrams, with close to 135 000 job descriptions completed (i.e. for around 70% of all positions). Once this exercise has been successfully completed, it will provide the main elements for the integrated Human Resource Management System.

Progress with the streamlining of the existing job classification system, with a view to aligning it to the functions referred to in the generic job descriptions, has been limited. Whilst the first meeting of the inter-ministerial working group in May was a welcome first step, the authorities would need to speed up the implementation of its road map, also taking full advantage of the technical support provided.

Progress has been made in terms of legal codification with the adoption of a law that strengthens the mandate of the Central Codification Committee, but work on inter-ministerial coordination has stalled. It is important to clearly define the operational modalities of the legal codification process and the allocation of roles, including between the Central Codification Committee and the Ministries. Technical work for the preparation of a unified Labour Law Code and Code of Labour Regulatory Provisions (a mid-2020 specific commitment) has started but concrete progress is awaited. On inter-ministerial coordination, no concrete progress has been reported since the adoption of an inter-ministerial manual in June 2018, and an update on actions initiated and planning for actions to be launched is expected to be prepared by the General Secretariat for Coordination in time for the next enhanced surveillance report.

The European institutions continue to carefully monitor the scale of recruitments in the public sector. The hiring plan for 2019 as well as for 2020-2022, as included in the 2018 Medium-Term Fiscal Strategy, seems to be respecting the one-in-one-out hiring rule for recruitments of new permanent staff in the public sector, though the ceiling for temporary staff has not been respected in 2018. It is estimated that the number of temporary staff will need to be reduced by approximately 1 550 persons in 2019, in order for the overall size of the public sector to be maintained. Regarding effective monitoring, the agreed actions to improve the reporting of the census are still to be implemented, while updated staffing figures for 2019 are yet to be uploaded on the census' website.

Recently adopted salary provisions pose risks to the unified wage grid, and a number of decisions to complete this reform remain pending. Although the actual fiscal cost of recent decisions to expand the coverage of 'personal differences' for some Ministries is small, it raises structural problems and fiscal risk as other Ministries may seek similar salary provisions. If specific salary provisions and adjustments to the hiring process for permanent staff are being considered for independent authorities, it would be preferable if these provisions would be part of a systematic approach rather than *ad hoc* exceptions to the current legal framework.

The Greek authorities are proceeding with the preparatory stage of the second phase of the Integrated Judicial Case Management System, activated earlier this year and scheduled for finalisation by mid-2020. In this context, completion of the tendering procedure for the electronic filing of legal documents to the courts is a mid-2019 specific commitment, and the proceedings for the public consultation of the draft tender texts regarding the projects of the second phase are to be finalised shortly. Furthermore, the implementation of the electronic filing of court documents (legal writs), already available in a number of courts, is proceeding, supported by legal and technical work to facilitate its full roll-out.

In the area of anti-corruption, the authorities have continued their efforts, led by the General Secretariat for Anti-corruption. A number of legal initiatives promoted by the Secretariat are to be introduced to the Parliament, relating to whistleblowing, internal auditing and the Secretariat's mandate. In particular, the law on internal audit is expected to be adopted shortly and ahead of the newly elected local administrations assuming their function. The authorities also committed to accelerate work on the establishment of a coordination mechanism for corruption cases, although no concrete progress has been made during this reporting period.

The Commission has continued to monitor developments in relation to the legal proceedings against the members of the Committee of Experts of TAIPED and the former President and senior staff of the Hellenic Statistical Authority (ELSTAT). In the case against former ELSTAT President A. Georgiou related to charges filed in connection with fiscal statistics, the Athens Court of Appeal issued a ruling in his favour that was published on 8 March 2019. As the Supreme Court Prosecutor did not file an appeal, the ruling stands in force and the excessive deficit case has been irrevocably dismissed. This is a very welcome development. Regarding other pending cases, an appeal introduced by Mr Georgiou in a defamation lawsuit is scheduled to be heard in May 2019. Regarding the Committee of Experts, there has been a positive development since the last enhanced surveillance report, in the form of the issuance of an exculpatory ruling by the chamber formation of the Athens Court of Appeal (not yet published). The Commission will continue to closely monitor developments in both procedures to report back in the context of enhanced surveillance.

OVERALL ASSESSMENT OF PROGRESS WITH REFORM COMMITMENTS

Greece is at an important juncture as regards policy choices needed to deliver a sustained and lasting economic recovery. Greece has made a reasonable start to the post programme environment since the expiry of the ESM programme in August 2018. Real growth and employment creation has been maintained, and Greece once again overachieved its primary surplus target in 2018. Albeit with some delay, the completion of specific reform commitments due for the end of 2018 allowed the implementation of additional debt measures worth EUR 970 million in April 2019. Greece has also started to regain market access and benefited from upgrades from rating agencies. However, significant legacy effects of the crisis remain as reflected in high levels of public debt, NPLs and unemployment. Reducing these imbalances will require many years of sustained implementation of institutional and structural reforms initiated in recent years to modernise the economy and the state, as well as many years of economic growth.

The pace of reform implementation has slowed in recent months and the consistency of some measures with commitments given to European partners is not assured. Whilst there are a few policy areas where reform implementation continues (e.g. some issues related to the cadastre, Hellinikon), there is a risk that most of the 15 specific commitments for mid-2019 will not be completed on schedule. In some cases, such as reforms in the field of social welfare (disability assessments), public administration (appointment of the Administrative Secretaries) and energy (implementation of the target model), these delays risk running to several months The Commission also underlines the importance for the Greek authorities to take steps that will enable ongoing privatisation tenders (e.g. HELPE, Egnatia, Athens International Airport) to proceed smoothly in the second half of 2019.

Projections by the European institutions indicate that, following the adoption of fiscal measures in May 2019, there are risks to the achievement of the agreed primary surplus target of 3.5% of GDP in 2019 and beyond, as well as for the compliance with the medium-term budgetary objective in 2020. The quality of the recent fiscal measures is of concern given the objective to make public finances more growth-friendly and to direct a higher share of social spending towards groups who face the highest incidence of poverty.

SOVEREIGN FINANCING

After the successful bond issuance in January, Greece tapped the markets for a second time in March 2019. Taking advantage of the improving market environment and a ratings upgrade, the Public Debt Management Agency proceeded with the issuance of a 10-year government bond for the first time since 2010, raising EUR 2.5 billion at a re-offered yield of 3.9% amid strong demand. Greece’s yield spreads have since improved further in April: the spread vis-à-vis the German Bund reached on average 340 percentage points on the 10-year tenure. However, in the more recent period, Greek bonds experienced pressure in particular after the announcements of new fiscal measures on 7 May. State cash reserves stood high at EUR 24.3 billion at the end of March; including the cash reserves of general government entities in the Treasury Single Account, the reserves reached EUR 33.7 billion.

The technical update of the debt sustainability analysis shows that the assessment of the sustainability of Greece’s debt is broadly unchanged. The baseline scenario shows the debt remaining on a downward path, though it remains above 100% of GDP until 2048. Greece’s gross financing needs will hover around 10% of

GDP until 2032 and remain around 17% of GDP at the end of the forecast horizon. It is not yet possible to fully incorporate the recent fiscal measures into the DSA as further analysis is required on their impact on growth and more clarity needed on the orientation of policies over the medium-term. But policies that affect negatively the primary balance surplus and growth potential would have a negative impact on the trajectory of debt.