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COMMUNICATION FROM THE COMMISSION

Enhanced Surveillance – Greece, November 2019

{SWD(2019) 930 final}

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 implementation 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 allows 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 framework 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 programme and to ensure that the objectives of the important reforms adopted under the financial assistance programmes are safeguarded. In that context, enhanced surveillance monitors 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 ([3]). Fifteen specific commitments have a deadline of mid-2019, progress on which is assessed in this report.

This is the fourth enhanced surveillance report for Greece. It is issued alongside the assessment of Greece's 2020 Draft Budgetary Plan and serves also as a specific monitoring report under the macroeconomic imbalance procedure for Greece under the European Semester, which was identified as experiencing excessive imbalances in the 2019 European Semester. This report is based on the findings of a mission to Athens between 23 and 26 September 2019 conducted by the Commission in liaison with the European Central Bank ([4]). The International Monetary Fund participated in the context of its 2019 Article IV surveillance cycle, while the European Stability Mechanism 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 European Stability Mechanism.

([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), Commission Implementing Decision (EU) 2019/338 of 20 February 2019 on the prolongation of enhanced surveillance for Greece (OJ L 60, 20.2.2019, p. 17), Commission Implementing Decision (EU) 2019/1287 of 26 July 2019 on the prolongation of enhanced surveillance for Greece (OJ L 202, 31.7.2019, p. 110).

([3]) 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.

([4]) 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 16 to 20 September.

This report could serve as a basis for the Eurogroup to decide on the release of the second set of policy-contingent debt measures worth EUR 767 million. 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 under the European Stability Mechanism 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. Those measures include: (i) the return of income equivalent amounts stemming from central banks' holdings of Greek government bonds under the Securities Markets Programme and the Agreement on Net Financial Assets and (ii) a waiver for the step-up interest margin for certain loans provided by the European Financial Stability Facility for the period from 17 June 2019 until 31 December 2019.

This report concludes that Greece has taken the necessary actions to achieve its specific reform commitments for mid-2019. Further actions will be crucial to complete, and where necessary accelerate, reforms. This assessment takes into account the efforts of the new administration over the last months to implement the commitments, in the context of advancing a broader reform agenda, and its willingness to prepare them in close cooperation with the institutions.

ECONOMIC OUTLOOK

Economic growth in Greece continued in the first half of 2019 and is forecast to remain resilient amid external headwinds. Following a weaker-than-expected start of the year, growth is expected to regain momentum in the second half and reach 1.8% in 2019 overall, a notch below the 1.9% rate achieved in 2018. Private consumption and investment are likely to be the main contributors to growth this year and the next, on the back of a solid growth in disposable income and high consumer confidence levels in market surveys, which have already surpassed pre-crisis levels. The recovery in Greece is taking place against the backdrop of a weakening external environment. Nonetheless, supported by the announced cuts in taxes on labour and capital and continued gains in export market shares, growth is forecast to strengthen to 2.3% in 2020, above the euro area average of 1.2%.

Overall sentiment and expectations underline a positive momentum. The Economic Sentiment Indicator has improved strongly since the general election of July and capital controls have been fully lifted Greece has been active on international capital markets, where interest spreads have rapidly declined to historically low levels, over and above the generally favourable developments in the European sovereign bond markets. There have been upgrades in the assessment by rating agencies, also reflective the positive and constructive engagement with the European institutions. The challenge for the Greek authorities, and indeed European partners, will be to now sustain this overall very positive momentum.

Medium-term growth performance crucially depends on strengthening investment, which is still below the euro area average. In 2018, investment in Greece as percentage of GDP was the lowest in the EU and 7.7 percentage points below the euro area average of 20.6% of GDP. Raising investment levels to recover from the years of underinvestment during the crisis is of key importance for future economic growth. Flagship privatisation projects and attracting foreign direct investment will be central to increasing private investment. Increasing public investment, first by reaching the budgetary expenditure ceilings and then extending public investment beyond the current possibilities of the budget, would further stimulate growth due to the multiplier effect.

The labour market shows further improvements and unemployment continues to decline at a steady pace. Employment is forecast to grow above 2% in 2019 and 2020, driving the unemployment rate down from 19.3% in 2018 to around 17% this year and close to 15% in 2020. Inflation is expected to be muted in the short term on the back of the recent cuts in indirect taxes and oil price developments, and to increase moderately in the medium term.

The forecast is subject to upside and downside risks, with the risks to the downside being more pronounced. 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. The projection is contingent upon maintaining the reform path agreed under enhanced surveillance, including reforms in the resolution framework for non-performing loans, designed to ensure a sufficient reduction of non-performing loans and support bank credit.

FISCAL POLICIES AND OUTLOOK

Greece is on course to overachieve the agreed primary surplus target of 3.5% of GDP in 2019, the fifth year in a row when targets would be exceeded. This dissipates concerns that surfaced earlier this year that the adoption of fiscal measures in May 2019 would pose a risk for the achievement of the primary surplus target. These measures were maintained by the new administration. The May measures included: new settlement schemes (with 120 instalments) for debts on taxes and to social security funds and municipalities; a value added tax reduction on a selection of items; the reintroduction of a 13th monthly pension payment; and a reversal of an earlier reform of survivors' pensions. In addition, the personal income tax reform pre-legislated in 2017, which would have broadened the tax base and lowered rates in a fiscally neutral manner as of 2020, was abandoned. The fiscal cost of the May measures is currently estimated at 0.7% of GDP, lower than the 1.1-1.4% of GDP expected in the June enhanced surveillance report, on account of a lower-than-expected transfer of debts from the existing tax settlement schemes to the new scheme. The quality of these measures raised concerns given the objective to improve the quality of public finances and regarding their consistency with reforms adopted under the European Stability Mechanism programme. In July, the new administration amended the 120 instalments scheme, with a view to making it more attractive especially for businesses, and adopted a small cut in the Enfia property tax.

To ensure that the fiscal targets are met, the new administration revised spending ceilings downward to more realistic levels, while additional fiscal space was provided by additional tax revenues. The authorities reduced budget ceilings in both the ordinary (non-investment) budget and the public investment budget to take into account their persistent overestimation. This will improve the budget balance by 0.6% of GDP in 2019. The revision is partly carried over to the 2020 budget. The authorities have also developed an action plan to improve forecasting and monitoring of the public investment budget. Moreover, they adopted legislation to lay down the rules governing the development, management, financing, and implementation of the national component of the public investment budget to address its low execution. These efforts are long overdue and very welcome. The authorities are encouraged to use the fiscal space available under the budget ceilings fully to bolster the economic recovery. The fiscal outlook for 2019 has also been supported by favourable developments in revenues; mainly through a higher-than-expected participation of new debtors in instalment schemes and stronger value added tax revenues resulting also from a high growth in tourists' spending.

Against this background, the European institutions project the primary surplus, per the definition monitored under enhanced surveillance, to reach 3.8% of GDP in 2019. The forecast for 2019 assumes that the payment of the Public Service Obligation to the Public Power Corporation of around EUR 200 million will be covered from the contingency reserve, and does not take into account any possible additional one-off measures that might be adopted later in 2019 to use the available fiscal space.

This means that Greece is expected to achieve a general government surplus of 1.3% of GDP in 2019. This is well above the euro area average of a deficit of 0.8% of GDP. Greece's public finance has been in surplus since 2016 on the back of the substantial fiscal consolidation efforts during the ESM programme but under-executed public investment have also played a role. The achievement of a general government surplus is consistent with the estimated substantial decrease in the structural balance (from 5.8% of GDP in 2016 to 3.0% in 2019), signalling that the underlying fiscal stance is becoming gradually less tight.

On the basis of the information included in the 2020 Draft Budgetary Plan, the Commission forecasts Greece to meet the primary surplus target of 3.5% of GDP (a continuous specific commitment), to achieve a general government surplus of 1.0% of GDP and to respect all the requirements of the Stability and Growth Pact in 2020. The draft budget includes a package of new growth-friendly measures worth 0.6% of GDP aimed to reduce distortionary taxes and increase family-oriented social benefits. The package includes a four percentage points reduction in the corporate income tax; reform of the personal income tax, which *inter alia* reduces the tax rate from 22% to 9% for incomes up to EUR 10,000 and increases the tax-free threshold for taxpayers with children; reduction in social security contributions by one percentage point for full-time salaried persons; and a reduction in the dividend tax from 10% to 5%. In addition, the package includes a new childbirth allowance of EUR 2,000. The government has also announced additional tax cuts for 2021 and beyond but these will not be legislated now. To ensure budget neutrality, the package is complemented in the Draft Budgetary Plan by 'fiscally equivalent' measures mainly of parametric but also of administrative nature and of a similar magnitude. These measures aim to increase the yield of indirect taxes, update the tax base for the property tax, and further reduce spending targets that have not been used in previous years.

While the full set of measures is broadly budgetary neutral, it is expected to improve the quality of public finances and boost growth in 2020. The cuts in taxes on capital and labour are important, positive steps in reducing Greece's effective corporate tax and the tax wedge on labour. All taxpayers are expected to benefit from the personal income tax reform, in particular those with lower incomes and the self-employed. In addition, full-time employees, including those with incomes below the non-taxable level, will benefit from the reduction in social security contribution. The growth-friendly tax shift from distortionary to less distortionary taxes such as the value added tax or the property tax is expected to stimulate private investment and employment, and contribute to higher productivity growth and private consumption. The reform does not address the relatively high non-taxable allowance for the personal income tax, which was part of the tax reform agreed with the institutions under the European Stability Mechanism programme in 2017 and originally due to enter into force in 2020. The final bill introducing the fiscal package for 2020, as published for public consultation, includes some minor additional measures that do not have an impact on the assessment of the fiscal policy for 2020.

Greece's public finances continue to face important fiscal risks related to pensions and public sector wages. While the Council of State has recently confirmed the constitutionality of the main pillars of the 2016 pension reform, some of its elements (including the provisions for supplementary pensions and accrual rates for long careers in the main pension) will need to be adjusted. The fiscal impact of addressing these aspects may still be significant; but the authorities have committed to sustain the possible additional fiscal costs within the budget ceiling of the Ministry of Labour for 2020. Moreover, the possible negative fiscal impact will also be substantially limited by the fact that key parts of the 2016 pension reform were found constitutional and the Council of State has not granted a right for retrospective financial compensation. However, the pension rights of public sector officials are still under scrutiny by the Court of Auditors. Regarding public sector wages, the high number of temporary staff and risks related to the broadening of the scope of exemptions from the unified wage grid remain a source of concern. The potential for overshooting the fiscal target of 3.5% of GDP through underspending in the public investment budget remains but has diminished.

FISCAL STRUCTURAL POLICIES

Based on the findings of a technical support study, the European institutions agreed that the valuation exercise to update Enfia property tax values (a specific mid-2019 commitment) should be rescheduled so as to facilitate making a more substantial reform of the objective property tax values system by the mid-2020 deadline. In particular, the new government agreed to initiate a major widening of the property tax base for the Enfia and other property taxes. The reform set out in a detailed timetable is expected to increase the tax base of the Enfia property tax by more than 20% in time for the 2020 Enfia tax exercise and improve the fairness and efficiency of the property tax system.

The authorities announced a suspension of the value added tax on new buildings for three years to boost the construction sector. The measure risks increasing the share of the shadow economy and is currently under scrutiny with respect to compliance with EU law. The European institutions have encouraged the authorities to develop alternative measures to address the problems encountered by the building sector in Greece and to combat the shadow economy.

Progress was made on important tax measures to increase liquidity in domestic corporate bond markets by opening them up to external investors. The authorities will abolish the withholding tax on domestically-listed corporate bonds for non-residents, thus bringing the withholding tax treatment of these bonds in line with the majority of EU Member States. A similar treatment will be adopted for purchases by international investors of direct bond issuances made by banks to meet the minimum requirement for own funds and eligible liabilities.

Given the accumulation of previous delays, the end-2019 target for staffing levels at the Independent Authority for Public Revenue is unlikely to be met; however, the new government has taken important commitments to swiftly adopt agreed complementary measures to further strengthen the capacity of the Independent Authority and enhance its attractiveness to highly qualified candidates. The staff level of the Independent Authority at the end of the third quarter of 2019 reversed the negative trend observed in 2018 but remains some 1,000 persons short of the target set for end-2019. The recent approval of an additional 600 hires is a step in the right direction. The new government has committed to complete the ground-breaking human resources reforms to allow the Independent Authority to recruit and retain highly qualified personnel and also allocated the needed budget. This will phase-in a position-based remuneration system for the first time in the Greek public administration. The authorities have committed to adopt the grading legislation by end-2019 and the supplementary wage grid in time to allow the new system to come into effect as of 1 July 2020. To ensure a sufficient level of self-reliance in the day-to-day IT operations, the production of a road map by end-2019 has been agreed between the Independent Authority and the General Secretariat for Information Services to clarify their respective competencies. Finally, the authorities have confirmed that an appropriate building has been identified that will allow to host, by end-2020, all of the headquarter services of the Independent Authority that are currently scattered in 13 buildings.

The authorities will amend the basic instalment scheme with a view to facilitating the repayment of tax debts. The agreed changes make the scheme more flexible, *inter alia* by extending the maximum number of instalments to 24 or 48 depending on the type of the tax (from the current 12 and 24 instalments), and increase the incentives for staying in the scheme until the debt is settled fully. It is important for the credibility of this revised scheme that the authorities have committed not to open further new *ad hoc* instalment schemes.

The new administration has adopted a new broad action plan to clear the remaining stock of arrears by 2021, following a lack of progress under the previous plan since the end of the programme. As of end-August 2019, the stock of arrears monitored under enhanced surveillance remained high at EUR 1.3 billion compared with EUR 1.7 billion a year earlier. This is substantially above the zero arrears target at the conclusion of the European Stability Mechanism programme. The new action plan aims to bring the net stock of arrears down to EUR 1 billion by December 2019 and to fully clear arrears by end-2020, with the exception of EUR 140 million for pension claims that would be cleared by June 2021. The plan tackles the main challenges of arrears clearance and is accompanied by a number of legal, administrative and IT actions to achieve its objectives.

Measures to avoid the creation of new arrears (a specific mid-2019 commitment) are in the pipeline, but will require more time to be designed and implemented fully. The Hellenic Court of Auditors, in its follow-up audit, noted that progress had been made on most of its recommendations; but some of the key recommendations will require more time, also in view of the very short period elapsed since its first audit. As part of the new Clearance action plan, the authorities will establish a Steering Committee by Ministerial decision to ensure a timely implementation of both the clearance plan and the plan against accumulation of new arrears. The remaining *ex ante* audits by the Hellenic Court of Auditors for the extra-budgetary funds and local governments were phased out as envisaged.

The implementation of the Treasury Single Account and the Unified Chart of Accounts remain broadly on track. The full implementation of the Treasury Single Account by end-2019 will require some additional work but is progressing well overall. Regarding the Unified Chart of Accounts, the new government created a Steering Committee to oversee the project and took some initial steps to implement the chart of accounts also in the public investment budget; but greater clarity is needed as to its full implementation in this area.

SOCIAL WELFARE

The Council of State has confirmed the constitutionality of the main elements of the 2016 pension reform, but some of its aspects will need to be amended. The authorities are elaborating proposals to address the issues raised by the Council of State ruling and have committed to find solutions to contain the cost of the necessary amendments within the budget of the Ministry of Labour for 2020. However, the Second Chamber of the Court of Auditors has recently reached an opposite conclusion regarding pension rights of public sector officials compared to the Council of State decision, which creates additional uncertainty.

The collection of the 2018 clawback of healthcare expenditure (a specific mid-2019 commitment) has been delayed on account of changes in the repayment schedule, though the needed legislation will enter into force shortly. The start of the collection, originally planned by June, was affected by the authorities' decision to extend the maximum repayment period for the clawback up to 120 monthly instalments. Although most providers are expected to repay within five years, the change still results in an overall dilution of payments and worsens the liquidity situation of the Health Fund. The European institutions have encouraged the authorities to step up efforts in this area.

The authorities plan to take a number of steps to rationalise health care spending, which could reduce clawback in the medium and long-term, the ambition of which will need to be commensurate with some of the recent steps going in the opposite direction. The authorities plan to establish a national cancer registry and a Health Technology Assessments Agency, to strengthen the Drug Negotiating Committee and step up the work on the development of clinical protocols, as well as other actions. These are all steps in the right direction though their impact is expected to materialise only in the longer term. At the same time, the authorities have delayed the annual update of the price bulletin, which usually leads to a downwards revision of pharmaceutical prices, and intend to eliminate the 25% entry fee for innovative drugs. Both these measures potentially increase the amount of clawback in the coming months.

Progress towards mid-2020 commitments to increase the share of centralised procurement for hospital expenditure and to consolidate the network of health care providers is slow. Nonetheless, the authorities remain committed to the reform and plan to reshape the recently established central procurement body to increase its flexibility and efficiency in the medium term. With technical support provided through the European Commission, the authorities have also made progress in updating the hospital reimbursement scheme. It will be important for the authorities to further build on the progress made.

The authorities paused the opening of additional health care centres to reconsider the most suitable structure of delivery of primary health care, though they have signalled their intention to preserve the fundamentals of the already legislated reform. As a result, in the next six months the opening of at most ten additional primary health care units is considered feasible. The timeline for the introduction of key features of the reform, such as compulsory registration with a family doctor and gatekeeping functions, is yet to be clarified.

Regarding social policy, the reform of the disability benefits framework (a specific mid-2019 commitment) is advancing but with significant technically-related delays outside the control of the authorities. While the upgrading and simplification of the administrative processes to determine disability status is progressing, the new approach to determine disability status based on both medical and functional assessment is still to be adopted. The new methodology should have been developed on the basis of the results of a pilot project which encountered delays for reasons outside the control of the authorities. A revised timeline will be agreed once the evaluation is received: provided the evaluation is available shortly, a concept paper on the reform should be available by February and the reform undertaken by June 2020.

The specific end-2019 commitments on the completion of the Social Solidarity Income scheme and a review of subsidies for local public transport remain on track. The authorities have completed the second pillar of the Social Solidarity Income scheme – social inclusion –and work is underway on the third pillar, which relies on the provision of active labour market services to help the recipients of the scheme (re-)enter the labour market. To achieve this, the authorities are developing a more systematic approach to the design and management of the active labour market services, which has been tested and should be gradually expanded following its evaluation. Regarding the upcoming review of the system of subsidies for local public transport, the authorities have confirmed their commitment to assess the appropriateness of the current system of subsidised fares for local public transport by the end of 2019, and to follow up on eventual recommendations to improve the system.

FINANCIAL SECTOR POLICIES

The liquidity situation of Greek banks has further improved and there are signs that the banks' market access is gradually re-established but legacy risks and challenges remain high. Banks continue to face a large stock of non-performing loans, while other challenges persist, such as the fragile profitability and the strong sovereign-bank nexus, including through the high share of deferred tax credits in banks' capital. Going forward, the Greek banking sector is faced with the challenge of boosting its resilience and accelerating the reduction of non-performing loans, while improving its ability to finance growth.

The improving liquidity situation of Greek banks and increased depositor confidence led to the complete lifting of capital controls as of 1 September 2019 (a continuous specific commitment). In the first nine months of 2019, banks' private sector deposits have increased by about 3.5% and the emergency liquidity assistance was fully repaid in the beginning of the year. Whilst the abolition of capital controls normalises the functioning of the Greek economy and is supportive for confidence building, it places even more importance on accelerating efforts to strengthen the banking system and underpin depositor confidence.

The pace of reduction of the non-performing loans accelerated in 2019 but levels remain very high. Non-performing loans in the Greek banking system peaked in March 2016 at EUR 107.2 billion or 48.8%. The pace of decline in non-performing loans has accelerated since 2018, reaching 45.4% and 43.6% of total customer loans at end-2018 and mid-2019, respectively. This was overall in line with the operational targets set by the four systemic banks, under the oversight of the supervisory authority. While the non-performing loans ratio remains very high, the recent acceleration in the pace of reduction of the non-performing loans is more pronounced in absolute terms: the stock decreased to EUR 75.4 billion by end-June 2019, i.e. by EUR 13.5 billion or 15% year-on-year. For the coming years, the four systemic banks plan to further substantially reduce non-performing loans to EUR 26 billion or 19.2% by end-2021. To this end, additional efforts will be needed by both banks and the authorities: banks will need to accelerate 'organic' resolution activities for the non-performing loans and strengthen efforts to identify and adequately address strategic defaults, while the authorities are expected to ensure that the legal framework and the judicial system are able to efficiently support the resolution of non-performing loans.

Systemic initiatives, like the Hercules asset protection scheme, can help clean up the balance sheet of Greek banks. Under the scheme, each bank may transfer non-performing loans to separately managed Special Purpose Vehicles, which may issue junior, mezzanine and senior notes, with a state guarantee for the senior notes. In exchange for the guarantee offered, the state will receive remuneration at market terms. External servicer companies will manage the assets. In October 2019, the Commission concluded that the scheme, which is similar to the Italian Guarantee on Securitization of Bank Non-performing Loans scheme, does not constitute State aid within the meaning of Article 107 (1) of the Treaty on the Functioning of the European Union.

The focus now falls on completing the design of the asset protection scheme and commencing its swift implementation. Participation in the scheme is voluntary, while the envelope of guarantees could support a substantial de-recognition of non-performing loans for all banks. The current improvement in sovereign financing conditions provides an opportunity for banks to achieve a relatively low price for the state guarantee, though market risk needs to be taken into account. The success of the scheme will, inter alia, depend on the balance of regulatory capital gains, guarantee related expenses and losses stemming from the sales of notes to the investors. The scheme will run for 18 months, with the possibility of renewal. The authorities could also explore additional measures, including complementary schemes, to further support the health of the banking sector.

The authorities are working on a range of initiatives to strengthen the resolution framework for non-performing loans, though there is scope to accelerate the pace of implementation. The implementation of the actions outlined below is monitored and assessed under enhanced surveillance as part of the **continuous specific commitment** to *"continue to implement reforms aimed at restoring the health of the banking system, including non-performing loans resolution efforts"*.

- **Electronic auctions:** Despite progress in the first semester of 2019, the majority electronic auctions continue to be cancelled or suspended, or have failed due to lack of interest among bidders, and most of the successfully auctioned real estate assets are still acquired by banks. Identified impediments leading to the cancellation or suspension of e-auctions due to procedural abuse are currently under assessment. The Greek authorities have established a working group to assess the extent of the problem as well as other potential impediments, in order to define and recommend the necessary mitigating measures. The authorities have provided an initial analysis of the reasons for the above *status quo*, and committed to providing a full report shortly.
- **Backlog of household insolvency cases:** The elimination of the backlog of cases at courts in the context of the household insolvency framework (a specific end-2021 commitment) remains significantly behind schedule. It is key for the authorities to increase the processing capacity of magistrate's courts in order to achieve full elimination of the backlog, including cases created under the new primary residence protection regime, by end-2021, via the elaboration of an appropriate updated action plan by end-December 2019. The European institutions have encouraged the authorities to assess the change in numbers of cases in the past (processed cases vs. inflows of new incoming cases) and present adequate measures to anchor the projected path of the elimination of the backlog by end-2021.

- **Tax treatment of write-offs:** An amendment reinstating the favourable tax treatment of loan write-offs that had expired at the end of 2018 for restructurings made up to end-2019 is currently in public consultation. The relevant provision stipulates that the amount of the write-off will not be considered as an income of the debtor and will be exempted from the tax levied on donations. This addresses the disincentives to restructurings caused by the expiry of the previous tax treatment.
- **Primary residence protection:** Following the launch of the electronic platform in summer 2019, the measure was approved by the Commission under the state-aid rules. The authorities have undertaken amendments to the framework and the IT platform to facilitate applications. They intend to prolong the scheme by four months and terminate it by end-April 2020. While such a technical delay could help increase the uptake of the scheme from its current low levels, it slows down the normalisation of payment culture. The authorities have also committed to accelerate the work on the harmonisation of insolvency frameworks. The institutions will report on the completion of both elements under enhanced surveillance. Under the new framework, it would be warranted to ensure the free enforcement of all collateral including primary residences, which would help normalize the banking sector's credit provision to the economy.
- **Insolvency framework:** Preparatory work on the harmonization and integration of the bankruptcy and insolvency regimes has started. The elaboration of a well-defined and systemically consistent unified framework is highly desirable, and should be entrusted to a law-drafting committee and be effected without undue haste but in a holistic and technically thorough manner. The authorities have drafted a concept paper as a basis for the elaboration of a draft new single insolvency framework by end-April 2020, which sets out the basic objectives of this reform.
- **Code of Civil Procedure:** Progress with assessing the implementation of the reformed Code of Civil Procedure is underway but behind schedule, due to inherited delays. On the basis of stakeholder consultation, the relevant working group is currently conducting a comprehensive evaluation of the reform. Its work will be followed by the formation of a law-drafting committee that will draft potentially requisite amendments to be adopted by the end of 2020.
- **Financial training of judges:** The authorities reported further progress in the provision of financial training to judges, notably in the area of household insolvency. Two draft Presidential Decrees were submitted to the Council of State for the required constitutionality assessment. The authorities are also proceeding with the appointment of clerical court staff, an action which has been subject to considerable delays.
- **Legal safeguards for bank officials dealing with restructuring cases:** An amendment to the Penal Code aiming at addressing the issues of pending court cases against bank officials involved in past debt restructurings, and the protection of these officials in the context of ongoing and future restructurings has been adopted. The impact of this legislation in the context of the Greek legal framework will be monitored under enhanced surveillance.
- **State guarantees:** In September 2019, the backlog of called loan guarantees by the state remained considerable and increased since the previous report largely due to an increase in claims by the banking sector, despite efforts to accelerate the processing rate. The authorities have presented an updated action plan and a corresponding seven-year payment plan for the clearance of the EUR 2 billion stock of guaranteed loans called by commercial banks. The action plan aims to deal with bottlenecks in cooperation with banks, while

strengthening human resources at the General Accounting Office and upgrading the IT framework. Taking into account *inter alia* the long lag from the time the guarantees were called, which for some dates back to 2012, the authorities are seeking scope for a payment profile not exceeding four years with adequate measures to ensure its credibility.

The Hellenic Financial Stability Fund continued exercising its shareholding rights in the four systemic banks, contributed to non-performing loans resolution polices and improved their governance. The Fund as a shareholder evaluated and approved several divestments, challenged banks' strategies and policies and contributed to non-performing loans reduction policies. By October 2019, banks have mostly implemented the recommendations of the Fund from the 2017 board performance and governance review, which focused primarily on the banks' risk management culture, compliance and internal control frameworks. The implementation of the Fund's divestment strategy approved in 2018 is in its first, preparatory phase, where the Fund aims to effectively challenge the banks' strategies and the business models to promote value-enhancing initiatives. Discussions between the Fund and the Ministry of Finance on the potential involvement of other authorities in the final stage of the divestment and the legal protection for the Fund's governing bodies and staff have not been concluded yet. The preservation of independence of the Hellenic Financial Stability Fund is a cornerstone in the process toward restoring the health of the banking sector.

LABOUR MARKET

The authorities committed to continue monitoring labour market and wage developments and intend to conduct an ex post assessment of the recent increase in the minimum wage. This exercise will benefit from technical support from the World Bank, provided through the European Commission, and its results are intended to feed into the next minimum wage review in 2020.

The authorities are on track to complete the implementation of an action plan to fight undeclared work for 2017-2019 by end-2019 and are preparing a follow up. The current action plan promotes an integrated approach to undeclared work, including measures to reinforce the cooperation among different institutions and improve the capacity to detect undeclared work. The authorities will design a follow-up to the action plan, after an *ex post* evaluation of all implemented measures will have been completed through technical support provided through the European Commission. These measures have been accompanied by a number of additional recent steps to encourage work in the formal economy and to limit the abusive use of part-time work, which often masks undeclared full-time work. These notably include an increase in the overtime remuneration for part-time workers and the expansion of the employment registration system allowing it to cover also non-standard forms of employment. In 2020, the government is also planning to introduce a digitalised system for the recording of working time.

The new Development Bill of October 2019 introduced a number of changes to the collective bargaining framework. The Bill introduces the possibility of opting out from sectoral-level bargaining for certain businesses. It also amends the procedure for the extension of sectoral agreements that is no longer automatic, but at the discretion of the Minister of Labour subject to specific conditions. Other new elements include the creation of a public registry for employer associations and for trade unions in order to better verify their representativeness, and a restriction to the unilateral recourse to arbitration. It remains to be seen how these changes will affect collective bargaining in practice. While the new requirements for the extension of collective agreements may reduce the incentives for sectoral-level bargaining, the opt-out possibilities – if taken up by the social partners – may promote social dialogue both at firm and at sector level.

The new government has embarked on an ambitious programme of reforms aimed at modernising the education system and bringing it closer to good practice. This impetus is welcome and long overdue in view of long-standing challenges, including inefficient allocation of resources, low autonomy, poor educational outcomes, skill mismatches, and weaknesses in the governance of higher education institutions.

PRODUCT MARKETS AND COMPETITIVENESS

Although there are few product market and competitiveness reform commitments with a deadline relevant to this enhanced surveillance cycle, it is worth stressing that key structural reforms in this vital area have been initiated under the programme and will require several years of sustained implementation, so as to secure a lasting improvement in the business environment, investment and growth. Broad-based structural reforms initiated in recent years have already started to improve the functioning of Greece's product markets. Greece's exports market shares are expanding and foreign direct investment is on an upward trend, albeit from a very low level. However, further efforts will be needed to close Greece's sizeable investment gap and to improve Greece's ranking in comparative international competitiveness indicators. Long-standing weaknesses include registering property and enforcing contracts, while there is also significant scope for catching-up in the fields of digital economy, product market regulation and competitiveness at regional level.

The new administration has signalled its intention to pursue a strongly pro-growth and investment policy agenda. Since entering into office, the government has taken a number of initial steps that pave the way towards improving the business landscape. This has included legislation to foster the transition to a 'digital state', improve the quality of legislation, and advance legal codification. The administration is also taking first steps towards a coordinated approach to promoting the outward orientation of the Greek economy, where there is scope for a much more ambitious strategy. Progress with rebalancing the economy towards promising export-oriented sectors such as the agricultural and agro-food, tourism, transport and logistics and high-tech sectors, including through the development of smart specialisation strategies, would help strengthen the current account and redress the very negative and deteriorating net international investment position.

Further measures have been introduced, through the recently adopted Development Law. Amongst others, they include the alignment of the nuisance classification system to the environmental classification, which is harmonised with relevant EU legislative acts, the reduction of licensing requirements, and the development of a Single Digital Map to provide clarity and transparency on land use rules to investors, as well as changes in spatial planning to accelerate major investment projects.

The government is off to a good start in terms of launching initiatives to strengthen the business environment and is planning further actions to streamline regulatory processes and stimulate investment in key sectors. Indeed, it is essential to provide sustained certainty and greater incentives to investors. To that end, the government has indicated that it will continue to prioritise further actions on rationalising and expediting the licensing process, notably in relation to environmental licensing. This would be particularly important for boosting investment, especially in activities of high economic impact, as would further actions to review the land use and licensing framework in Attica, and to strengthen enforcement mechanisms.

To guide the completion of the investment licensing reform, which is part of the specific commitments up to 2022, the new administration has produced revised action plans. According to the revised plans, the authorities commit to meeting the deadlines set out under the enhanced surveillance framework. Nonetheless, previous delays have made conforming to some reform elements more challenging (i.e. on the simplification of legislation in the 24 sectors not yet covered by the investment licensing reform and on the development of tools for the environmental domain of the inspection framework). It will thus be key that the government commits adequate resources to the process. As regards the review of the nuisance classification, the authorities have committed to align this system with the environmental classification system by mid-2020, in line with the relevant provision included in the recently adopted Development Law, a year earlier than the commitment deadline. Furthermore, the work on the tendering procedure on the relevant IT system, due to be completed by end-2019, appears to be largely on track. Lastly, the authorities have committed to safeguarding the integrity of critical reform gains achieved, and to this end it is expected that a formalised mechanism will be established.

In the area of land use, reforms are advancing. Forest maps for some 95% of the country have been completed, materially reaching the target of completing the drafting of the last phase of forest maps (**a specific mid-2019 commitment**). Out of these maps, some 44% have been ratified, and thus become definitive. Cadastral mapping has been completed for around a third of the 39 million property rights in Greece, and the remaining part is in progress. The declaration of properties for cadastral mapping is picking up, and the authorities are considering further steps to accelerate the process. The setup of the institutional framework for the cadastre is advancing but proving challenging. In particular, given that in spring the integration of mortgage offices into the new cadastral agency has been proceeding slower than planned, the authorities have committed to accelerate the transition to the new entity. Positive legislative steps have been taken in the area of spatial planning, aimed at accelerating the implementation of local spatial plans and the approval of major investments (special spatial plans).

The authorities have undertaken efforts to stabilise the finances of the energy incumbent, Public Power Corporation, and have announced ambitious energy market reforms, which will affect the timeline for the implementation of the target model for electricity (a specific mid-2019 commitment). The decisive steps taken by the authorities to shore up Public Power Corporation’s finances have been reflected in a positive half-year financial report, which was an important signal for markets. The authorities are currently developing measures to tackle the longer term challenges of arrears and strategic defaulters. The authorities decided to cancel the last scheduled auction in October under NOME (*Nouvelle Organisation du Marché de l'Electricité*), which was put in place as a transitional measure while energy market reforms took place to open up to competition. One such reform was the implementation of the target model; this is on track for delivery by the new deadline of June 2020. Coupling with neighbouring markets should follow. The authorities’ proposals to speed up delivery of the forward market are welcome.

The authorities have proposed an ambitious plan for the longer-term transformation of the energy market in Greece, and have communicated their intention to formally submit revised antitrust remedies in January 2020. The core of the energy strategy involves closing down all lignite-fired capacity by 2028, with a significant share of closures taking place much earlier. The government is also considering taking further steps to open up the market to competition. If these plans are fully implemented, major developments with a target model-based, open market that is less reliant on fossil fuels and open to expanding its renewables capacity could already be observed in 2020. While the direction of this longer-term strategy is welcome, further more immediate steps are needed to address Public Power Corporation's market dominance, such as through the ongoing antitrust procedure. Data on the market shares of the Public Power Corporation indicate that competitors are entering the market on the retail and wholesale side, but its dominant position and its exclusive access to lignite-fired generation remain a concern. In this context, it should be noted that, against a background of legal uncertainty and lack of transparency, no bids were received for the second round of the tender for the lignite divestiture in July 2019 (a pending specific end-2018 commitment which had seen delays). The failure of this divestiture resulted in a breach of the anti-trust commitment, so an alternative remedy has to be found. The authorities formally communicated their intention to submit revised remedies in January 2020.

Greece's gas market is still small, but growing. The completed sale of the transmission grid, the Natural Gas Transmissions System Operator, as well as the ongoing sale of the Public Gas Corporation will lead to further market opening and investment on the domestic level, whilst ongoing progress with projects such as the Bulgaria-Greece Interconnector and growing liquefied natural gas imports show Greece's potential to become a regional energy hub. The authorities are revisiting the planned sale of the Public Gas Corporation though the revised plan is encouraging, involving the sale of a larger government stake and provisions to ensure full unbundling.

HELLENIC CORPORATION OF ASSETS AND PARTICIPATIONS AND PRIVATIZATIONS

The work of Hellenic Corporation of Assets and Participations on the key areas covered by the commitments to the Eurogroup is continuing. The implementation of the strategic plan (**a continuous commitment**) is ongoing and the Board review is progressing. The Corporation's board has completed the review/replacement for most of its subsidiaries of state-owned enterprises (**a specific mid-2019 commitment**), in line with technical feasibility. This includes the appointment of new board members at Hellenic Post and Public Power Corporation, thus facilitating the changes needed at these companies. The authorities have engaged meaningfully with the Hellenic Corporation of Assets and Participations' reform. They have materially improved the situation of low caps on director remuneration for the bigger non-listed state-owned enterprises under the Corporation, through a legal amendment, thereby facilitating the process of board reviews going forward. Since the publication of the third enhanced surveillance report in June 2019, the Corporation has made further progress in improving corporate governance in the state-owned enterprises. The first consolidated financial accounts for the group for the year 2018 were prepared and submitted for approval to the General Assembly. The implementation of the coordination mechanism, which governs the interaction between the authorities and Corporation regarding the mandates and objectives of the state-owned enterprises under the Corporation, was relaunched in October with priority attached to four SOEs (central markets of Athens and Thessaloniki, Corinth Canal and the national fairs organiser Helexpo). The mandates and deliverables for these state-owned enterprises are expected to be finalised soon since significant preparatory work has been done by Corporation and discussed with the competent authorities.

The authorities have greatly strengthened momentum in the privatisation process. The updated Asset Development Plan has been adopted (**a continuous commitment**) and progress with ongoing transactions has accelerated in the last three months. In particular:

- **Hellinikon, (development of the site of the former Athens International airport, a pending specific end-2018 commitment):** The authorities have attached great emphasis and strongly engaged in the transaction, intensifying significantly the efforts to complete the conditions precedent to allow the transfer of shares to the preferred investor, Lamda. The overall recent progress is significant and the financial closing could be feasible in the coming months.
- **Marina of Alimos (a specific mid-2019 commitment):** the preferred investor was selected on 16 April 2019. The Court of Audit approved the tender procedure on 26 June 2019. The next steps are procedural. Thus, satisfactory progress is being made in the tender for the long-term concession of the marina of Alimos, although the financial closing is not expected before end-2019.
- **Hellenic Petroleum (a specific mid-2019 commitment):** No binding offers were submitted for the joint sale (along with PanEuropean Oil and Industrial Holdings S.A., the other strategic shareholder of Hellenic Petroleum) of a majority stake (50.1%) and thus there was no positive outcome of the specific transaction. The financial closure is thus inevitably subject to significant delays. The Hellenic Republic Asset Development Fund, the Taiped, was given the technical mandate to explore all options available towards proceeding with the transaction. The ultimate decision as to the structure and the timing lies with the Greek authorities and should be determined on the basis of what provides the best commercial and strategic value for Greece. The approach is expected to be clarified and a timeline finalised by end- 2019.
- **Sale of 30% of the Athens International Airport:** Open issues on corporate governance, which had delayed the transaction, were resolved by the authorities. The tender process is thus proceeding. Ten investment schemes expressed on 29 October 2019 their interest (Phase A) to acquire the 30% stake in the company. The binding offers are expected to be submitted in early 2020, and the financial closing of the transaction is expected before the end of 2020.
- **Public Gas Corporation:** The authorities are considering changes in its corporate restructuring and demerging into Commercial (wholesale and retail gas supply) and Infrastructure (gas distribution networks) units, while the Corporation's interests in international strategic gas infrastructure projects would be transferred to a new corporate entity. The corporate structure is a policy choice to be made by the authorities, provided that it is in accordance with the principles of the agreed term sheet of June 2018. The Greek authorities have indicated their intention to proceed with the full divestment of their stake (65%) in both Commercial and Infrastructure units and thus increase the expected privatization proceeds, while also facilitating the unbundling of the gas market.
- **Egnatia motorway concession:** given previous delays and obstacles, a number of actions are still needed before the submission of binding offers (related inter alia to the implementation of the toll pricing policy approved by the Commission, construction and operation of toll stations, and the safety certification of bridges and tunnels). The authorities have stressed their commitment to unblock the transaction; however determined follow-up will be needed.

- **Regional ports:** the authorities are positive with respect to providing flexibility of choice on the privatisation transaction structure (i.e. master concession, sub-concession, sale of equity) for each port. The consultants of Taiped are expected to deliver shortly the relevant study and the authorities to enact a necessary legal amendment providing Taiped the flexibility of choice, so that the tender procedure for the first two ports can be launched.

PUBLIC ADMINISTRATION AND JUSTICE

The selection process of Administrative Secretaries (an end-2018 commitment) has been cancelled and replaced by the establishment of a Permanent Secretary post and by a significant change in the delegation of signature powers for individual acts from the political to the administrative level. However, in order to safeguard the achievements in terms of de-politicisation of the public administration and institutional continuity, the authorities have committed that the adopted measures are implemented without delay and the selection process for Directors and Heads of Division continues in accordance with the existing legal framework. The authorities have also committed to reintroduce an open selection process for senior management posts at legal entities of public and private law by May 2020 and to adopt measures to create permanent organisational structures at the Presidency Office. An independent assessment of the selection process for the Administrative Secretaries (**a specific mid-2019 commitment**) has been completed.

The far-reaching legislation on the functioning of the central administration, which was the first major legislation brought forward by the new government, introduced a number of key provisions to modernise the public administration, including strengthening the government's centralised coordination capacity. Given that weak coordination has been one of the long-standing weaknesses of the public administration, reinforcing the role and resources of the government's Presidency Office is an important reform. Further, this major codification law consolidates the role of the Council of Ministers and sets out specific provisions for the annual programming and monitoring of the government's priorities. The law also includes provisions for harmonising and strengthening the legislative process across the central administration, including improving the impact assessment process.

Reforms adopted during the programme period, such as the mobility scheme and performance assessment, continue to be implemented with overall good participation. It is important for the credibility of the mobility scheme reform that transfers are speeded up. In this respect, the authorities have committed to introduce legal provisions by end-2019 that will ensure that the selection process of the mobility scheme will go faster. This is a welcome initiative as it would further enhance the credibility of this scheme amongst the general government entities.

The new administration has also taken actions to implement other ongoing reforms in this area, such as the human resources management strategy and legal codification, and to introduce targeted improvements, further demonstrating their commitment to reform herein. The mobility cycle launched in August 2018 is advancing with minor delays, while performance assessments for 2018 have been completed (both are **specific mid-2019 commitments**). The new administration has committed to a road map to complete the human resources management strategy by 2023. In addition, each jobholder will be linked with a specific job description/position by the end of 2019. Non-complying general government entities will not be able to request new hires. As concerns the legal codification, it is important that the ongoing review of the national portal for codification be completed swiftly so as to ensure a timely start of the tender procedure.

Hires of permanent staff remain within the hiring target set by the authorities in their budget and the Medium-term Fiscal Strategy, and the authorities are taking action to regain control of hiring of temporary staff. The hiring benchmark for the hires or temporary staff (i.e. yearly average of temporary staff in 2016) was estimated to have been surpassed by 1,500 when the previous enhanced surveillance report was published (data covering up until February 2019) while the current estimate exceeds the benchmark by 5,200 (data up until September 2019). A recent amendment removed a number of important exceptions from the regular hiring rules for temporary staff, which should increase control over hiring by the Ministry of Interior and hopefully result in a gradual decrease of temporary staff.

A few recent salary provisions raise some concerns about the integrity of the unified wage grid. These salary provisions place specific staffing groups in some priority services at the most senior remuneration grade and also extend scope/coverage of the 'personal difference' allowance. The authorities have committed to reinforce and centralise control of the unified wage grid reform and hiring procedures by establishing an inter-ministerial working group with the mandate to present specific measures by end-2019, which will be implemented by January 2020.

The government has adopted legislation to promote the transition to a digital State, with the new Ministry of Digital Governance taking a leading role. The Ministry is tasked with creating a digital public administration through delivering a series of major IT projects. Projects to be pursued in the short-term include the development of a single digital identity for the authentication of all transactions with the State, the simplification of specific administrative procedures for citizens and businesses, and the setting up of a unified platform (gov.gr) to bring together information and electronic services offered by the State. In the medium- to long-term, the Ministry aims at further developing the infrastructure for 5G networks and promoting the interoperability of public systems and registries. The authorities are also revising the existing National Digital Strategy setting the framework for the digital transformation of the public administration and the economy as a whole.

The new administration has committed to proceed with the third phase of the Single Payment Authority reform, which has been subject to significant delays. The third phase will establish an integrated information system and increase the authority's mandate to include clearing tasks, thus improving public financial management. This will require a number of actions, including legislative amendments, an IT project to be launched in January 2020, and the establishment of a joint working group to review the current clearance processes.

Progress with the implementation of commitments in the area of justice has been uneven. The legislation on mandatory electronic filing and processing of legal documents in administrative jurisdictions was adopted in October 2019 but will become effective only as of January 2021, a year later than expected under this end-2019 specific commitment. At the same time, the implementation of the second phase of the Integrated Judicial Case Management System, a mid-2020 commitment, is advancing. The tendering procedure (**a specific mid-2019 commitment**), which had been subject to delays, was completed in November 2019, and the publication of the tender is due by December 2019, upon completion of ongoing administrative proceedings at the Ministry of Digital Governance. The key objective of the reform is to enhance quality and efficiency of the judiciary through a uniform IT environment.

The mandatory mediation framework, which had been twice postponed, will soon become effective. The amendments ensure conformity of the mediation framework with the Greek Constitution and EU law, reduce the categories of disputes subject to mandatory mediation and the minimum cost of mediation, and modify a number of procedural and technical aspects of the framework.

The implementation of the national anti-corruption action plan is proceeding. The vast majority of the more than 100 actions are considered by the authorities as completed, with the remainder having been launched. Sustained implementation will be key. In August 2019, the implementation of the plan, which is a mid-2021 specific commitment, became part of the mandate of the new independent National of Transparency Authority, which will be fully operational in 2020. The agency brings together a number of functions previously followed by different bodies and will be endowed with greater institutional capacity to fight corruption.

The legislative amendments adopted in June 2019 which downgrade the status of active bribery from felony to misdemeanour are a concern. The relevant amendments to the Criminal Code and Criminal Procedure Codes attracted criticism from the Group of States against Corruption and the Organisation for Economic Co-operation and Development's Working Group on Bribery. The draft positions published for public consultation in October 2019 do not to address these concerns fully. The findings of a planned joint mission by Group of States against Corruption and the Organisation for Economic Co-operation and Development could provide useful guidance to the authorities on appropriate further actions, including legal amendments.

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. The case against former the Hellenic Statistical Authority President A. Georgiou related to charges filed in connection with fiscal statistics has been irrevocably dismissed. An appeal introduced by Mr. Georgiou in a civil defamation lawsuit is scheduled to be heard in January 2020. In the case against the Committee of Experts, a further positive development has materialised since the last enhanced surveillance report: as there was no appeal launched against the ruling by the chamber formation of the Athens Court of Appeal, the dismissal of the charges against the Committee of Experts stands irrevocably in force.

OVERALL ASSESSMENT OF PROGRESS WITH REFORM COMMITMENTS

The new administration has made a swift start and confirmed, immediately after taking office, its intention to stick to the reform path agreed under the enhanced surveillance framework. The government has engaged positively and constructively with the European institutions and a high level of openness and willingness to engage is widespread at all levels. The government has taken important steps to improve coordination of economic policies, which will be instrumental to ensuring a timely completion of Greece's specific commitments.

The flagship reforms adopted thus far by the new administration and its overall growth-friendly narrative have been well received by the markets. Greek bond yields have decreased to historical lows (with 3-month bills at negative rates) over and above the generally favourable developments in the European sovereign bond markets, capital controls have been phased out earlier than expected and economic sentiment is at pre-crisis levels. The ongoing economic recovery continues to drive down the high unemployment rate and growth is forecast to strengthen in 2020 on the back of the announced cuts in taxes on labour and capital. The improved economic prospects have started to pass through to Greece's sovereign bond ratings, and it will be key for the new administration to remain focused as it will be under scrutiny from investors for quite some time, amidst economic weakening among Greece's trade partners.

The government has presented a Draft Budgetary Plan that complies with the agreed fiscal targets, respects all the requirements of the Stability and Growth Pact in 2020, and announces a major tax reform for 2020. The new administration offset the fiscal impact of the measures adopted in May 2019 by revising spending ceilings downward to more realistic levels, while additional fiscal space was provided by additional tax revenues. Moreover, the government designed a package of growth-friendly measures for 2020 that shift taxes from capital and labour to less distortionary taxes such as the value added tax or property tax, and increase social spending on families with children. The policy package will be implemented in a balance-neutral manner, and will improve the quality of public finances and boost growth in 2020. The European institutions project that the agreed primary surplus targets of 3.5% of GDP will be exceeded in 2019 and met in 2020, which is equivalent to general government surpluses of 1.3% of GDP in 2019 and 1.0% of GDP in 2020.

While important reforms have been undertaken, it will be key to sustain the momentum in order to deliver on the number of ambitious action plans going ahead. Key areas of privatisation, the business environment and digital governance have seen a positive momentum, and new initiatives were adopted for ensuring an effective collective bargaining framework or are being developed for strengthening of the banking sector. In this context, the authorities have gone well beyond the specific commitments given to the Eurogroup. Important reforms in the areas of land use, property tax and the tax administration are advancing. The authorities have developed sound reform plans to remedy the inherited delays, which affected a number of commitments given to European partners, most notably on the clearance of arrears, public administration reform, and energy market reforms. Where appropriate, these plans include alternative or complementary measures of equivalent merit to commitments given to Eurogroup. The authorities are in the process of catching up with the financial sector reforms but the plans will need to be firmed up going forward. The sustained implementation of these reforms will be closely monitored in the successive enhanced surveillance reports so as to ensure that the specific commitments given to the Eurogroup in June 2018 remain effective.

Greece has taken the necessary actions to achieve its specific reform commitments for mid-2019. Further actions will be crucial to complete, and where necessary accelerate, reforms. This assessment takes into account the efforts of the new administration over the last months to implement the commitments, in the context of advancing a broader reform agenda, and its willingness to prepare them in close cooperation with the institutions.

SOVEREIGN FINANCING

Encouraged by the marked decrease in bond yields, Greece continued to build its presence on the government bond market by issuing bonds in July and re-opening the books of an earlier issuance in October. The Public Debt Management Agency tapped the market for the third time this year in July by issuing a 7-year bond at a re-offered yield of 1.9%. Another record-low yield of 1.5% was achieved in October with a 10-year bond. Greece's yield spreads vis-à-vis German Bunds continued to moderate, reaching 1.9 percentage points on the 10-year tenure in September 2019, down from 3.5 percentage points a year ago. The improving financing situation has started to be reflected in Greece's sovereign credit ratings. The cash buffer account was not used in this reporting period. State cash reserves, which include this cash buffer account of EUR 15.7 billion and other reserves, remained high at around EUR 20.3 billion as of end-September 2019. The available reserves are sufficient to cover sovereign financing needs of more than two years ahead.

The partial early repayment of the loans from the International Monetary Fund, which is expected to take place by end-November, is a welcome step and an important positive signal. After the completion of national procedures, the governing bodies of the European Stability Mechanism and the European Financial Stability Facility waived their right for a proportional repayment on 28 October. The transaction will be financed through funds raised earlier this year and is expected to have a positive but limited impact on debt sustainability, as most of the amounts due would have to be paid by the end of 2020. Nonetheless, this is a welcome step as it helps reduce the foreign exchange rate risk, generates savings and sends the right signal to the markets.

An update of the debt sustainability analysis has been carried out. The baseline scenario shows the debt remaining on a downward path, though it remains above 100% of GDP until 2041. Greece's gross financing needs will hover around 10% of GDP until 2032 and remain around 14% of GDP at the end of the forecast horizon.