Hellenic Fiscal Council

Summary of Autumn Report - November 2019

Fiscal performance during the first nine months of 2019 has been solid since the primary balance of the General Government increased on a cash basis by almost one billion Euros (+21,4%), compared to the same period of 2018. This increase can be attributed to a surge in revenues (by more than 2 billion Euros) coming from cash inflows that do not count towards the Enhanced Surveillance definition of the primary surplus (flows from ANFAs, SMPs and privatizations are precluded). Despite that and given last year's fiscal over-performance, the primary surplus target of 3,5% is within reach while marginal overshooting is likely.

Tax revenues in almost all tax categories do not show remarkable yearly variation while expenditures increased modestly due to an increase in the wage bill as a result of seniority wage rises and elevated social security contributions.

Under-execution in the Public Investment Budget is common for this time of the year as expenditure was limited to just 38,3% until the end of September. At present no safe conclusions can be derived on how this segment of the overall budget will evolve but past experience and the specificities of public expenditure indicate that under-execution is likely to continue until the end of 2019. From a strict fiscal view and taking into account the commitment on a specific primary surplus target, the aforementioned under-execution is conducive towards a "favourable" fiscal outcome. However, under a wider economic perspective, it can only have an adverse growth effect in the medium-term.

General Government's (GG) arrears have been stabilized to around the same amount as last year's, approximately 2,5 billion euros, as a result of a reduction in the arrears of the GG's subsectors and an increase in the pending tax returefunds. Reducing the stock of arrears to a significant lower level, if not completely wiping it out, remains an open challenge for the fiscal administration of the State.

There has also been an improvement in the overdue obligations to the State as the accumulation rate is the lowest in the last 6 years. However, their stock remain high, and in particular in obligations concerning tax and social security contributions.

Public debt remains at a high level albeit de-escalating starting from this year. This development is further facilitated by the low borrowing cost of the Greek State, the commitment towards primary surpluses as well as the growth dynamics. Gross

Financial Needs (GFN) for the next years remain constrained and manageable thanks to the implementation of the short and medium term debt-relief measures.

The Hellenic Fiscal Council considers that the achievement of the 2020 fiscal target (primary surplus of 3,5% of GDP under the Enhanced Surveillance definition) is attainable under certain preconditions:

a) There will be no negative deviation in the outcome of the additional measures that have been planned in order to improve fiscal performance. More specifically, measures that refer to “combating tax evasion and broading the tax base by promoting electronic means of payments” are highly uncertain as to their outcome while it remains unclear how tax base will be broaden.
b) The optimistic Growth prospects will be materialized.
c) The increase in the nominal GDP by 959 million euros according to estimations by the Ministry of Finance (MoF) (as a result of the additional growth and social measures) will yield additional tax revenues of about 330 million euros and social security contributions of 140 million euros.
d) Any unforeseen expenditures stemming from courts decisions will be fiscally manageable.

The Hellenic Fiscal Council reasserts the MoF’s projection for a 2019 structural balance[1] of 2,7% of potential GDP as well as for a structural balance of 1,8% in 2020. In any case, overshooting the Medium Term Objective (0,25% of potential GDP) for both 2019 and 2020 is highly likely.

In terms of macroeconomic developments, the observed acceleration in growth is undoubtedly positive, however growth rates at least for the immediate future should be much higher.

The 2,0% MoF’s growth projection for 2019 is slightly more optimistic compared to the Hellenic Fiscal Council’s central growth scenario (1,8%), but in any case is considered to be feasible.

Regarding the macroeconomic developments of the first semester of 2019, public consumption had the greatest contribution in the real GDP growth. A source of concern is related to the recent shrinking in private consumption (during the first semester) as well as to the quasi stagnation of investments in fixed capital.

[1] The structural budget balance is a nominal budget balance adjusted by the cyclical component (difference between actual and potential GDP) excluding one-off and temporary policy measures such as receipts coming from privatizations.

The aforementioned negative development in relation to the private consumption gets even more glooming if it is assessed against a 4,9% increase in the household's disposable income. This trend could be partly explained by the ongoing deleveraging that may take the form of reducing past obligations that are due to financial institutions, to the Tax Collection Independent Authority and to the Social Security Funds in the fear of enforced collection measures by the authorities such as bank account garnishment and auctions. New schemes for settling overdue debt in several installments are already in place while the recent election cycle during May and June may have suspended households' expenditure.

Despite these and in terms of leading indicators, the Economic Sentiment Indicator as well as the Consumer's Confidence Indicator showed considerable improvement which will positively affect to a certain extent the "real" economy in the second semester of 2019. In an also positive development, the deficit in the current account compared to previous year was reduced by about 1 billion euros between January and August 2019 mostly thanks to the travel balance.

The unemployment rate remains on a declining path (17% in Q2 2019 compared to 19,2% in Q2 2018) but the number of unemployed is still 430.000 short of the 2008 number. At the same time, employment keeps rising but a huge gap remains (-678.000 people) compared to pre-crisis levels. The evolution of paid employment is relatively unstable showing that the labour market lacks positive dynamics. The reduction – even marginal – of the labour force is also a negative development which makes the condition in the labour market far from being "normal".

Inflation[2] remained low under a trend for a slowing rate from May onwards due to the re-classification of several goods and services in "food and alcoholic beverages", "foodservice" and "energy" sectors to a lower VAT rate. This VAT reduction had a price lowering impact in the "food and alcoholic beverages" and "energy" sectors but not in the foodservice sector where VAT benefits seem to have been "internalized" by the industry (restaurants etc.).

The Hellenic Fiscal Council expresses the opinion that the projected by the MoF 2,8% of GDP growth for 2020 is optimistic but within acceptable limits. International institutions are also more restrained, projecting a growth rate for 2020 between 2% and 2,5% of GDP.

[2] Harmonized CPI

Significant domestic and external downside risks exist that are difficult to be ex-ante assessed and quantified. More specifically:

- The expansionary effects of the 2020 fiscal measures are uncertain to the extent that the fiscal multipliers used (above one for the expansionary tax measures) prove to be overestimated.
- The increase in the private consumption is also uncertain due to the alleged households' propensity for deleveraging which was mentioned above.
- Deterioration in the external balance is likely due to an increase in imports of goods and services for both consumption and production.
- On top of the external balance deterioration scenario, domestic exporters face challenges related to the international competition under conditions of impaired funding recovery by the domestic banking system.
- Further risks can emerge from a possible European economic slowdown, the large stock of Non Performing Loans that inhibit credit growth and possible adverse effects from Brexit.
- Geopolitical tensions and uncertainties in the international environment which are mainly related to the modalities between EU and Turkey regarding the handling of the refugees flows as well as the drilling activities in the Cypriot exclusive economic zone.

Athens, November 18, 2019

The President of the Board of Directors

Prof. Panagiotis Korliras