September 24, 2021
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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 19/92-1

11:55 a.m., November 13, 2019

1. Greece—2019 Article IV Consultation

Documents: SM/19/247 and Correction 1; and Supplement 1; and Supplement 2; SM/19/248; and Correction 1

Staff: Dohlman, EUR; Zettelmeyer, SPR

Length: 53 minutes

Executive Board Attendance

T. Zhang, Acting Chair

Executive Directors	Alternate Executive Directors
	B. Jappah (AE), Temporary
	F. Sylla (AF)
G. Lopetegui (AG)	
	A. Park (AP), Temporary
	P. Fachada (BR)
Z. Jin (CC)	
	P. Moreno (CE)
L. Levonian (CO)	
	S. Benk (EC)
	P. Rozan (FF)
R. von Kleist (GR)	
S. Bhalla (IN)	
	M. Psalidopoulos (IT)
	K. Chikada (JA)
	M. El Qorchi (MD)
H. Beblawi (MI)	
	D. Cools (NE), Temporary
T. Ostros (NO)	
	L. Palei (RU)
	R. Alkhareif (SA)
	S. Chea (ST), Temporary
	P. Trabinski (SZ)
	D. Ronicle (UK)
	P. Pollard (US), Temporary

S. Bhatia, Acting Secretary
J. Morco, Summing Up Officer
D. Alcantara, Board Operations Officer
M. McKenzie, Verbatim Reporting Officer

Also Present
Communications Department: A. Adriano. European Central Bank: D. Rakitzis. European Department: V. Bezerra de Menezes, P. Dohlman, P. Gerson, D. Kim, N. Novikova, F. Parodi, M. Song. Finance Department: J. Okwuokei. Legal Department: C. Claver, C. DeLong. Monetary and Capital Markets Department: T. Bayle. Strategy, Policy, and Review Department: X. Li, J. Zettelmeyer. Alternate Executive Director: J. Di Tata (AG).

Senior Advisors to Executive Directors: W. Abdelati (MI), M.Gilliot (FF), R. Goyal (IN), P. Harvan (EC). Advisors to Executive Directors: D. Andreicut (UK), L. Cerami (IT), D. Crane (US), J. Damgaard (NO), I. Fragin (GR), Z. Huang (CC), A. Korinthios (IT), K. Kuretani (JA), R. Lopes Varela (AF), P. Mooney (CO), M. Mulas (CE), G. Nadali (MD), B. Parkanyi (NE), A. Ribeiro Mateus (IT), D. Shestakov (RU), D. Vogel (AG), A. Tola (SZ).

1. GREECE—2019 ARTICLE IV CONSULTATION

Mr. Psalidopoulos submitted the following statement:

My Greek authorities welcome the Staff Report and the accompanying Selected Issues papers and thank staff for the extensive and constructive discussions and their strong engagement during their last visit to Greece. The authorities, however, feel that despite its merits, the Report focuses excessively on past legacies and challenges and understates recent positive developments that improve significantly the short- and medium-term prospects of the Greek economy. Overall, my authorities assess, and indeed market developments concur, that the Greek economic outlook is much more favorable than the one depicted in the Report.

Historical context

Greece has received extensive financial assistance from its European partners and the IMF from 2010 to 2018, in the context of three consecutive programs (two of which with IMF participation). Greece has exited in August 2018 the third program and is currently under Enhanced Surveillance status. Over the past decade, Greece achieved unprecedented fiscal adjustment; recorded substantial competitiveness gains reflected in equally substantial current account improvements; and implemented a wide range of reforms covering product, services and labor markets; the tax, pension and healthcare systems; governance; and institutional performance. This progress was achieved under the most extreme recession a Western economy has experienced over the past seven decades, resulting at the peak of the crisis in a 25 percent drop of GDP and very extensive social costs. Admittedly, policy mistakes occurred, and the speed of progress was not uniform across programs. Nevertheless, given the facts described above, and in view of acknowledged policy-design mistakes on behalf of institutions' representatives co-determining Greek programs, stating that the Greek recovery "has fallen far short of expectations" (p.1) and that " the authorities largely failed in efforts to achieve a much-needed deep structural transformation of the economy" (p. 22, box 2) is inaccurate and does not constitute a balanced assessment of economic developments in Greece over the program era.

State of play

A key feature of the Report is the projection of modest/declining growth rates in the short- and medium-term (Table 1, p. 33) and the existence of fiscal sustainability risks (p.1). The main themes underpinning this assessment are succinctly summarized in par. 1, page 4. The authorities acknowledge the existence of important legacy issues at the start of their time in office. Nevertheless, and as the experience of other program countries suggests, legacy issues do not constitute an insurmountable obstacle to economic recovery. Two key prerequisites for the latter are the ownership of the reforms necessary for recovery and a critical mass of social support for their implementation. The Greek authorities have ownership of their reform agenda and have been elected with a mandate to implement it, hence strong social consensus is now in place. As a result, a very significant part of the basis underpinning the Report's pessimistic projections has now been removed. The Greek economy has entered a new era and the Report's projections, based on assumptions/parameters characterizing the past, are highly questionable.

The authorities' growth and fiscal projections, as reported in the 2020 Draft Budgetary Plan (DBP), are much more optimistic than staff's. Developments in financial markets and leading economic indicators strongly (and not "cautiously", as mentioned in p.5) support this optimism. Some highlights include: yields and spreads of government bonds, at all maturities, have dropped to all-time historic lows, including negative interest rates in recent TB-issues; Greek Enterprises, like OTE, Hellenic Petroleum and Wind Hellas, have issued new bonds, at favorable terms; and the Economic Sentiment Indicator has been recording the highest confidence levels since 2008. Clearly, markets signal agreement with the authorities' economic plan; and disagreement with the Report's pessimistic projections.

Fiscal policy

Greece has achieved the primary balance targets set by the third adjustment program and Enhanced Surveillance. The authorities assess that the 2019 target will also be met, as strongly indicated by the 10-month budget execution. The authorities endorse recommendations by staff and have taken decisive action to address them. This is reflected in the DBP 2020, which includes significant reductions in corporate/personal/other taxes; reduction in social security contributions (for full-time employees only); and a host of business-friendly tax clauses. To broaden the tax base, the DBP 2020 increases the level of electronic transactions necessary for claiming the tax credit. The authorities have also initiated a full recalculation of objective property values, as a result of which new regions will enter the zone system and the property tax. Work has also started towards introducing electronic books, electronic invoices and direct link of the cash machines to the tax office. In the area of public financial management (PFM) the General Accounting Office has reduced the budget ceilings of the 2020 ordinary budget by approximately 0.5 billion EUR; and implements significant reforms including the Unified Chart of Accounts, Spending Reviews, Performance Budgeting and the Treasury Single Account. Finally, the Independent Authority of Tax Revenues currently implements HR and IT reforms. Overall, the authorities are committed to growth-oriented, inclusive fiscal policies and tax reductions whilst safeguarding agreed fiscal targets. In this context, they welcome the view of the Report that primary balance targets should be lowered and that a smoothing mechanism to allow temporary deviations from fiscal targets in the event of adverse shocks be set in place.

Public debt sustainability

The authorities find staff's assessment of public debt sustainability to be extremely pessimistic, not least because it does not consider the aggressive reduction of Greek bond yields and credit spreads observed over the past eighteen months, and in particular the past three months. The Report's annual projections are far higher than PDMA's projections, which are very conservative both on an accrual and on a cash basis. According to the initial methodology of the Institutions, the 5-year new funding cost of the Hellenic Republic (HR) had to be close to 3.4 percent instead of the current 0.4 percent. This factor has a strong impact regarding the future debt- to- GDP levels and the annual GFN vs GDP, i.e. on both indexes used to assess Greek debt sustainability. Staff adopts extremely conservative assumptions about future interest rates related to the funding cost of the HR and the European Institutions. Regarding the latter, and taking into account that the Greek debt portfolio is 95 percent at fixed rate, having also time to net re-fixing close to 18 years, and that the EFSF's liability portfolio is about 90 percent at fixed rate, it is difficult to explain an increase by 0.8 billion euros of the annual interest payments (on an accrual basis) for the year 2019 compared to 2018, or an increase by 0.4 billion euros for the year 2022 compared to 2021 and an increase by 0.3 billion euros for the year 2023 compared to 2022 (as depicted at page 37, Table 3, line "interest"). Overall, it is difficult to explain why the Greek debt is "less sustainable in the long term", when the previous Report reached a conclusion of a "more sustainable" Greek public debt, when a massive reduction in Greek credit spreads has taken place, projecting a far lower debt servicing cost and a far better investors' perception regarding the Greek debt sustainability and economic growth. The market reaction following the recent approval by European Institutions of the Greek request for a partial early repayment of its IMF loan is a credible signal of Greece's improved debt sustainability outlook. This will be further enhanced by reforms authorities plan to introduce to the pension system, as per their recent announcements.

Banking developments

The Report acknowledges improvements that have been brought so far to the Greek banking system and highlights some legacy issues, which are reflected in a high proportion of NPEs, limited liquidity and low profitability rates. The authorities acknowledge these challenges, but expect the pace of ongoing banking recovery, to whose achievement they assign top priority, to accelerate sharply in the near future. All capital controls have been abolished (as from September 1st, 2019); Greek banks have eliminated their ELA exposure; and private deposits are making a steady recovery. Over the last four quarters, the NPL stock has declined by 13.5 billion EUR, 15 percent on an annual basis, with reduction in 2019Q2 being the highest since 2017. On the back of this progress, in October 2019, the Greek authorities received approval from the European Commission for the "Hercules" Asset Protection Scheme (APS), a fiscal-neutral scheme aiming at a systemic reduction of around 40 percent of the current NPE stock at a lower cost for bank capital ratios. Hercules securitization will offer the investors a yield bearing asset at a period of negative interest rates and booming markets. Investors have positively reacted, and all Greek systemic banks are expected to join this scheme. The draft legislation relating to Hercules will soon be submitted to the Parliament, paving the way for a more liquid, transparent and institutionalised secondary NPEs market that will attract a broader pool of global capital.

Hercules is a bold step of the government's strategy to reboot the Greek financial system including far reaching reforms of its capital markets. To the same end, the authorities are working on other reform initiatives, including revising the personal insolvency and bankruptcy law and simplifying the current out-of-court settlement process for commercial loans. The new single insolvency framework will utilize an electronic platform with digital processes for debt restructuring, pre-agreed debt settlement proposals between creditors, a Credit Bureau for data collection and scoring, Early Warning as well as certified property valuators, financial experts and mediators alleviating courts. Finally, bank balance sheets are supported by the accelerating recovery of the real estate market. Based on the above, the authorities expect a significant increase in the capacity of the banking system to finance the real economy, supporting growth in the short-term through increased liquidity and in the medium-term through increased levels of investment.

Labor market reform

The Report acknowledges that labor market conditions are improving but assesses the quality of recovery to be weak. The authorities share the view that the reforms introduced in 2011-13 led to a significant restoration of the Greek economy's competitiveness and have been a key factor underpinning increasing employment rates observed since 2014. They also agree on the benefits of labor market flexibility within the single currency area and have initiated decisive action towards that direction. Over the past three months, they have repealed three labor law provisions legislated earlier in 2019 restricting labor market flexibility, introduced conditional opt-outs from sectoral collective agreements and legislated a public registry for worker and employer organizations allowing for online voting for critical decisions. This will attest capacity and representativeness when deciding about a strike or about collective labor agreements. The authorities are also working towards modernising legislation with respect to labour force termination, in harmony with the Revised European Social Chapter, and rationalising/simplifying the procedures for overtime reporting, paid leave and others. Furthermore, the DBP 2020 includes provisions relating to childcare aiming to increase female labour market participation. Finally, authorities aim to further codify, simplify and modernise Labour Law, aiming to create stability and flexibility in labour law arrangements that will increase competitiveness and foster jobs' creation and preservation.

Growth enhancing measures

The authorities endorse the necessity of growth enhancing reforms and are determined to push ahead with their implementation. During the programs' era, Greece implemented reforms covering labor, products and services markets, which the Report somewhat underplays. These contributed to improvement in Greece's performance in international business and regulation-quality rankings, as well as to substantial gains in unit labor cost-based competitiveness gains (app. 20 percent over 2010-2018). However, the CPI-based counterpart figure improved only by 8 percent, with no further progress since 2015. Authorities acknowledge this and are determined to reinvigorate the reforms' pace. Indeed, developments over the past three months confirm this determination. Large investment projects like Hellenikon and the Piraeus Port extension have been unblocked, privatisations, like the Athens International Airport, have been resumed, and a credible plan to restore the viability of the country's largest corporation, the Public Power Corporation has been put in place. Last month, the Parliament voted an

Omnibus Development Law including provisions for further liberalisation of product markets and a host of growth-friendly provisions, whose implementation is expected to result into medium-term growth gains estimated by the Bank of Greece in the region of 0.5 percent of GDP. The authorities plan, soon, to bring to Parliament legislation postulating further privatisations (e.g. reginal ports), profitable use of publicly owned real estate (through HCAP) and increasing competition in the energy sector. Last, but not least, they have committed to decarbonisation and moving toward renewable energy sources, which reflects the authorities' strong commitment to combating climate change, including a pledge to stop using lignite for electricity production by 2028. Overall, the authorities believe that their reform agenda will bring about a regime change in the Greek economy, resulting into medium-term growth rates significantly higher than those envisaged by staff.

Transparency and governance

The authorities share staff's assessment that Greece has strengthened its AML/CFT regime in line with international standards and on the importance of upgrading public-sector governance, transparency and institutional performance as key drivers of sustainable growth. The authorities believe in the Rule of Law, meritocracy, predictability, transparency and stability. One of their first legislative initiatives was the introduction of a single Independent Transparency Authority unifying all the disparate entities auditing and overseeing the government. The same legislation introduced a new institution, the Presidency of the Government, responsible for overseeing the implementation of the Government program; a provision for assessing the performance of Government officials and entities based on established KPIs and metrics, in line with international best practices; the introduction of newly created administrative General Secretaries, empowering institutional memory in the public sector and an ambitious and comprehensive project of digitization. The authorities believe that this important legislative initiative will make a significant contribution towards improving transparency and institutional performance, which is not recognised sufficiently by staff's analysis. The authorities plan to actively pursue further their institutional agenda, by focusing in areas including the justice system.

Concluding remarks

The thorough and detailed exposition of current trends and realities in the Greek economy lead my authorities to the conclusion that the country is fully on track to accelerate economic recovery and regain its former position in the world economy on a sound basis. The authorities are adamantly committed to fulfill their obligations and to deliver enhanced and inclusive growth while preserving social cohesion. They are looking forward to the support of their partners in the EU and consider the cooperation and advice of the IMF as having great importance for them going forward, as in the past. Based on the analysis presented above, they are looking forward to future IMF staff reports, involving a more balanced assessment of past events and a higher emphasis on forward looking analysis.

Mr. Ray and Ms. Park submitted the following statement:

We thank staff for a comprehensive set of papers, and Mr. Psalidopoulos for his informative buff statement. While staff and the authorities appear to have different views on what has been achieved to date and the outlook for Greece, we welcome their broad agreement on key policy priorities, and note Mr. Psalidopoulos' view that key ingredients for the implementation of a strong reform agenda are in place. We agree that policy priorities include repairing bank balance sheets, improving the fiscal policy mix and progressing labor market and structural reforms.

We note the difference in view between staff and the authorities on the outlook for Greece. There will always be some uncertainty about economic forecasts and valid differences of view. We encourage staff and the authorities to maintain a constructive engagement to make sure that the widest possible information is incorporated in forecasts underpinning these assessments. Nonetheless, we support staff maintaining conservative estimates—including of future interest rates and funding costs—for the use in debt sustainability analysis. As we have noted previously on Greece, where forecasts are prepared to assess the ability of Greece to repay the Fund and to achieve debt sustainability, it is better to be conservative than risk overestimating what can realistically be achieved.

We tend to agree with the authorities that the 2019 Article IV report takes a different view on Greece's progress during the program period. Where the 2018 Article IV staff report characterized macroeconomic imbalances as "largely eliminated," the 2019 Article IV staff report states that "Greece's external imbalances are significant" and the outlook for the current account deficit has shifted from "expected to remain close to balance" to "expected to widen over the medium-term." Could staff expand on the extent to which this change in assessment is due to revisions in current account data, a shift in view about the extent to which the current account adjustment was structural or cyclical (as described in the Selected Issues Paper) and assumptions about competitiveness-enhancing reforms?

Further progress in addressing bank balance sheet weaknesses remains critical to restoring the financial sector's capacity to support the economy and reducing fiscal risks. We welcome the priority placed on this issue by the new government and the agreement between staff and the authorities that a holistic strategy to address high legacy non-performing exposures (NPEs) is needed. We note positively the initiatives under consideration to achieve a faster reduction on non-performing exposures, including the creation of the Hercules Asset Protection Scheme and reforms to insolvency laws that would promote debt restructuring and payment discipline. To the extent that a faster reduction in NPEs will require additional capital, we agree with staff that efforts to strengthen the loss-absorbing capacity of banking capital should be considered, with priority given to private initiatives but public support provided if needed.

Rebalancing the fiscal policy mix to be more growth-friendly and socially inclusive remains a priority. We welcome the authorities' commitment to growth-oriented, inclusive fiscal policy and tax reductions that safeguard agreed fiscal targets, and their plans to cut direct tax rates and strengthen compliance. As staff's analysis highlights, there would also be material potential gains from broadening the tax base through tax policy changes and enforcement—including through its effect on the payments culture. We agree that there could be a case to consider lower fiscal targets given that would leave room to allow automatic stabilizers to operate to stabilize output in the event of economic shocks.

Finally, building on the important progress made during the program era, continued structural reform efforts are needed to enhance competitiveness and support growth. The authorities' determination to reinvigorate the pace of reform is welcome, and we note positively recent initiatives including accelerated efforts to move major privatization projects forward. The staff report also highlights the value of further product liberalization—to what extent are the priorities identified in the staff report addressed by the recently passed Omnibus Development Law? Decisive action to enhance labor market flexibility is also welcome and as staff note, could also be supported by greater use of active labor market policies and measures to enhance female labor force participation.

Mr. de Villeroché submitted the following statement:

We thank staff for their insightful report and selected issues paper in the context of the Greek Article IV consultation. We also thank Mr. Psalidopoulos for his buff statement that provides additional useful details.

We acknowledge the significant improvements achieved over the last decade. Nevertheless, the sizable challenge facing the Greek government is to support growth and facilitate a broad structural adjustment of the economy, while safeguarding fiscal sustainability and preserving social cohesion. Maintaining and further augmenting the wide-ranging reforms that were agreed under the financial assistance program and under the Enhanced Surveillance of the EU are paramount in this regard. We are encouraged by the new government's initiatives that focus on enhancing the investment climate and shifting fiscal policy to be more growth-friendly. At the same time, we would caution the authorities against rolling back previously adopted reforms or measures that would narrow rather than broaden the tax base.

Macroeconomic developments

The above-potential GDP growth in Greece is expected to continue, albeit it will gradually slow down, and remains predicated on continued structural reforms. Against the backdrop of weakening export demand, GDP growth has decelerated in the first quarter of 2019 before picking up again in the second quarter. Most forecasts of the Greek economy, including that of staff, are pointing to this pickup in pace to continue into 2020 based on a strengthening in investments and improving labor market conditions. These expectations are conditional on the swift implementation of the reforms that were agreed with the European partners. External risks point to the downside (a synchronized global slowdown and Brexit).

Fiscal policies

We share staff's view that while achieving the fiscal targets is important for underpinning the credibility of the government's program, holding back capital expenditure cannot be sustainable in the long run. Fiscal overperformance has helped investor confidence to return, as evidenced by the numerous bond issuances this year at favorable yields. We agree with staff that the measures adopted in May that ran counter to reforms adopted under the ESM program in terms of targeting social spending and eliminating tax exemptions and welcome their partial reversal. We welcome the expansionary measures announced for 2020 as steps in the right direction to make public finances more growth friendly. However, we share staff's concern regarding the narrowing of the tax base from the PIT reform and the negative effect of the extended temporary instalment scheme on tax compliance that can offset some of the broadening impact from increasing the prevalence of electronic transactions. Furthermore, expenditures need to be reoriented towards quality investment and more targeted social programs to strengthen growth and social inclusion. At the same time, we note that, contrary to staff, both the European Institutions and the authorities project that the primary surplus target for the 2020-2022 period will be met. The difference seems to stem from the different assessments of counter measures and thus staff's explanation would be welcome.

Staff call for a lower primary balance target or a smoothing mechanism to take into account cyclical or one-off shocks. We recall that the primary balance target was agreed with the Eurogroup, while taking into account the European fiscal rules and considering the implications for the debt sustainability analysis.

Financial sector policies

We welcome the progress made in reducing NPLs. At the same time, we agree with staff that significant further efforts on the side of banks and authorities are still needed. Despite sizable public support to banks, Greece remains an outlier in the EU for the stock of non-performing loans and for the low (zero) RoE on bank assets. Therefore, the momentum on sales and securitization of loans needs to be maintained and further reinforced, while banks also need to step up their efforts for 'organic' NPL reductions. Banks recently announced NPL reduction targets and the Prime Minister's call for even more ambitious reductions are necessary and encouraging in this regard. We welcome the government's new initiatives, including the Hercules securitization guarantee scheme, and note that promoting meaningful debt restructuring and payment discipline are key objectives going forward. These should include establishing a credible threat of foreclosure and the swift elimination of primary residence protection as a financial policy objective. We also strongly agree with staff that a more effective judiciary would be essential.

Improving bank profitability is key for reducing NPLs, raising fresh capital and, ultimately, for financial stability. We agree with staff that Greek banks must enhance their business strategies, improve their governance and risk management to increase their internal capital generation capacity which, along with continued NPL reduction, would help raise fresh MREL-eligible capital and increase the resilience of banks. This being said, we would be less categorical than staff regarding the need for additional capital buffers within the context of the current NPL reduction targets submitted to the SSM; especially when the loss-absorbing capacity of deferred tax credits is also considered.

Structural policies

The prolonged and deep recession in Greece has set back the needed structural adjustment of the economy. We share staff's assessment that with gross fixed capital formation at only half of its level in 2000, the structural adjustment needs facing the Greek economy are sizable. We thus welcome the authorities' overall policy objective to enhance the investment climate, proceed with key privatization transactions and transition to the new energy market model. We agree with staff's recommendation to establish a real-time assessment capacity of current barriers to product markets and competition. We take positive note of the progress achieved so far in this area, such as in the business areas of pharmacies and lawyers and encourage the authorities to continue these reforms. We note that the full implementation of several structural reforms has experienced delays, in part due to the snap elections that took place in July and urge the authorities to implement the agreed reforms without delay. At the same time, there has been some progress on a number of policy areas such as on the implementation of the investment licensing reform, forest mapping, the reduction of the time needed to register a new business and ongoing efforts to improve SOE governance. We believe that the newly adopted labor market reforms are a step in the right direction. We also agree with staff that efforts need to be sustained so as to complete the privatization program, for which delays remain large; but note the program's positive impact on FDI inflows to Greece. Finally, we welcome the authorities' commitment to combating climate change.

Mr. Ostros and Mr. Damgaard submitted the following statement:

We thank staff for the comprehensive set of papers and Mr. Psalidopoulos for his informative buff statement. Greece is still recovering from the crisis. Despite commendable actions, public debt and unemployment are highly elevated, and more needs to be done to bring the country fully back on track. To that end, we welcome the new Greek government's reaffirmation in September to meet the fiscal and structural policy commitments to the Euro Area member states under the Enhanced Surveillance framework. We associate ourselves with Mr. de Villeroche's gray, while adding the following for emphasis.

We strongly encourage the authorities to continue their efforts to bring public debt on a downward path. The 2019 primary surplus is expected to exceed the 3.5 percent of GDP commitment given to Greece's European partners but is projected to fall below the threshold in 2020-2024 in the baseline scenario. We do not agree with staff's recommendation to reduce fiscal targets to create more policy space in the short term. On the contrary, we urge the authorities to implement measures to comply with the 3.5 percent threshold in the coming years to enhance long-term debt sustainability. We stress that changes can only be done in agreement with the Eurogroup, while respecting the European fiscal rules and considering the implications for debt sustainability. Having said that, we do agree with staff that there is scope to rebalance the fiscal policy mix to strengthen growth and social inclusion, e.g., by adjusting pensions and the public wage bill and increasing social spending and investment. We also encourage the authorities to focus on tax enforcement to increase revenues and improve fairness. In this context, we appreciate the SIP on installment schemes, arrears, and payment culture, and note that there are various estimates of the size of the informal economy. In staff's assessment, what would be the revenue effect of bringing informal activities in line with the EU average?

The process of restoring bank health should be accelerated. We welcome the authorities' holistic strategy to address high legacy non-performing exposures (NPEs), including the Hercules scheme. At the same time, we strongly agree with staff that an overhaul of the personal insolvency framework is necessary and particularly a swift elimination of primary residence protection as described in the useful SIP on this topic. A credible foreclosure threat must be in place to address the high NPEs. We welcome the new government's decision to create a new Deputy Minister position to oversee bank reform and encourage the authorities to take every possible step to promote a well-capitalized, profitable, and efficient banking sector.

Comprehensive structural reforms are necessary to boost potential growth. Weak competition and a rigid business climate are obstacles to productivity gains. Hence, we welcome the new government's accelerated efforts to unblock signature privatization projects and push through business licensing deregulation. We also welcome the improvements to the AML/CFT framework and encourage the authorities to keep this issue as a high priority. Finally, it is important that the newly established National Transparency Authority (NTA) receives the necessary political backing and resources to effectively fulfill its mandate to tackle corruption.

Mr. Jin and Mr. Huang submitted the following statement:

We thank staff for the informative reports and Mr. Psalidopoulos for the helpful buff statement. The Greek economy continues to recover after recently completing its program. The authorities have made great progress in fiscal adjustments and competitiveness gains over the program era. However, challenges remain. Going forward, more should be done to improve the fiscal policy mix, repair bank balance sheets and accelerate the much-needed structural reforms. We broadly agree with staff's appraisal and limit ourselves to the following comments for emphasis.

A more growth-friendly and social inclusive fiscal policy mix is needed to safeguard sustainable growth. We commend the authorities' continuous efforts in pursuing fiscal consolidation, with primary surplus exceeding their commitments to European partners in recent years. The fiscal overperformance helped to put public debt on a downward path and restore market confidence but could also dampen economic growth. We note that the authorities committed to a primary surplus of 3.5 percent of GDP for 2020, but also welcomed staff's support for a lower primary balance target. Can staff elaborate more on the feasibility of this primary balance target? The weak tax collection and compliance continues to be a major source of concern. As staff indicated in the selected issue paper, the poorly-targeted installment schemes have encouraged a weak payment culture. We join staff in urging an end to these installment schemes, while increasing well-targeted social spending to protect the most vulnerable. We take note of the divergent views between staff and the authorities on public debt sustainability. Can staff comment on the authorities' debt projections mentioned in the buff statement?

A comprehensive and coordinated strategy should be in place to repair bank balance sheets. The Greek banking sector is still facing system-wide high Non-Performing Exposures (NPEs). We join staff in suggesting a faster reduction of NPEs through a comprehensive and coordinated strategy with appropriate sequencing, which should include an overhaul of the personal insolvency framework and end the temporary primary residence protection. The Greek banking sector has received substantial support from public finance over the past decade. We welcome the cost effectiveness analysis of this kind of support in the selected issues paper and concur with staff that market-based private investors rather than public finance should play a major role in the future. The authorities' recent removal of remaining capital flow management measures (CFMs) is welcome. Can staff elaborate more on the market reaction and primary impacts of the CFMs removal?

Steadfast implementation of reforms in product market is essential to safeguard hard-earned progress in labor market reforms. The authorities have made significant progress in improving labor cost competitiveness during the past years. However, the lower wage only partly passed through to price declines, due to product market rigidities. The imbalance in labor and product market reforms indicated that the labor had borne most of the adjustment burden, making the reform vulnerable to reversals. In this regard, we encourage the authorities to accelerate reforms in product market, including liberalizing the professional service sector, facilitating the firm entry/exit and streamlining the business licensing. We noticed that recent wage hike in some other European countries also only partly pass through to the retail prices. Can staff shed a light on why firms are reluctant to adjust their pricing no matter whether the wage cost increases or decreases?

With these remarks, we wish the authorities every success in their future endeavors.

Mr. Beblawi and Ms. Abdelati submitted the following statement:

We thank staff for a well-prepared report and Mr. Psalidopoulos for his informative buff statement that confirms that the key ingredients are in place for the implementation of a strong reform program. Greece's growth recovery continues, but at a slower pace than the stronger rebound that had been expected following a 25 percent drop in GDP. Key challenges need to be addressed for Greece to resume convergence toward Euro Area (EA) per capita income, including lagging productivity, a persistent competitiveness gap, incomplete cleanup of bank balance sheets, and a more credible path to debt sustainability.

Some positive signs are worth noting. Growth picked up in 2018-19 and is projected to pick up further in 2020-21. Unemployment declined markedly compared to 2017, although it remains high. Exports, especially tourism receipts, continue to grow at a good pace. And public debt continues on a steadily declining trend, although it will remain over 200 percent of GDP for the next three years. Greece's credibility was boosted, as it continues to overperform on its fiscal targets, delivering a primary surplus above the 3.5 percent of GDP commitment to European institutions (EI). The government's existing liquidity buffers can accommodate financing needs through 2022, and Greek spreads have declined to the lowest level in a decade.

We welcome the authorities' recently announced fiscal measures and support staff's call for improvement in the fiscal policy mix, especially since continuous overshooting of the primary balance has been damaging to growth. In particular, we support staff's call for lowering the PIT's tax-free threshold, as it is among the highest in EA. More also needs to be done to improve tax collection and compliance. We welcome plans to enhance the design of the installment scheme for tax arrears. Reorienting expenditure is also important with a shift toward high quality social spending and active labor market policies. We underscore the importance of addressing remaining weaknesses in the consistency and comprehensiveness of official fiscal source data and reporting, while noting recent improvements. We also join staff in urging the authorities to seek consensus with European partners that would allow for justified deviations from the agreed primary surplus, while maintaining market credibility. Has staff discussed the possibility of a smoothing mechanism with European Institutions?

We join staff and the authorities in underscoring the need to accelerate measures to restore banking sector health, as a top priority. Bank balance sheets remain a concern which continues to hold back growth, in spite of substantial injections of funds. The NPE ratio is very high at 44 percent, while provisioning coverage ratio is less than 50 percent, and therefore credit growth remains negative. We encourage the authorities to move toward a more comprehensive and ambitious strategy, supported by further improvements in the legal framework and the insolvency regime.

Staff attributes the less dynamic employment recovery to structural rigidities and, in particular, to weak implementation of non-labor reforms. We welcome the new government's signaling of a preference for greater labor market flexibility to achieve fuller employment, as reflected in its swift action to lift new restrictions on dismissals. We would welcome further information on the AMP pilot to support employability and skill-matching. We welcome the authorities' agreement with staff that labor policies need to be complimented with product market deregulation and strengthening competition. The intentions to take more steps toward attracting investment and reviving privatization are encouraging. We look forward to the authorities' new growth strategy to be articulated by the end of this year. Staff provides charts that show, except in a few areas, Greece remains at or near the bottom among EA members in many cross-country perception surveys. Given our reservations on the use of perception-based indicators, which are sometimes slow to adjust to realities, we would like to see evidence from other EAs who witnessed significant shift in their rankings following recent reforms.

We welcome the new government's stated policy plans and, in particular, the intention to improve the business environment, make the labor market more flexible, and attract investment by reviving privatization. We trust that the authorities will move swiftly to gain the necessary social consensus to deliver on their policy commitments. We note that the authorities have a more favorable view of growth prospects and of external competitiveness than the views of staff. To achieve these goals, it will be important to fully deliver on their planned growth-friendly reforms, including tax cuts, revive privatizations, promote business deregulation, improve bank balance sheets, and improve labor market flexibility.

Mr. Fachada and Mr. Fuentes submitted the following statement:

We thank staff for the reports and Mr. Psalidopoulos for his candid statement. At the outset, we tend to agree with Mr. Psalidopoulos and the authorities that the Article IV report understates recent positive developments in Greece. This year's bond issuances and yield spreads seem to corroborate the authorities' views that the Greek economic outlook is more favorable than the one depicted by staff. That said, and notwithstanding the recent growth, coupled with progress on fiscal consolidation and social outcomes, we believe that long-term conditions for higher and more inclusive growth in Greece remain challenging. Underwhelming private investment and some delayed reforms have tempered business expectations and lowered potential growth. Moreover, risks emanating from the weaker global outlook and rising protectionism could weaken Greece's external position further.

Favorable fiscal performance has supported consolidation. Greece continues to overperform against its budget targets, improving policy credibility. For 2020, we agree with the focus on slightly alleviating tax rates to better promote growth. Fiscal discipline has buttressed the public debt-to-GDP downward trend, while public debt management has contributed to lower sovereign borrowing costs and improve debt composition. Still, staff assesses public debt sustainability as "not assured under a realistic set of macro-fiscal assumptions", including if the risks from weaker growth materialize. Against this background, could staff expand on the nature of the differences between the authorities and their assumptions regarding the long-term fiscal and growth projections?

Protracted weaknesses in the banking system warrant renewed commitment to restore financial sector health. Although Greece has exited its financial assistance programs, most financial institutions remain mired by high non-performing exposures (NPEs), with some systemic banks still in need of additional capital injections. Thus far, efforts to clean up the banking system have had limited success, hindered by poor banking practices, weak sector policies, and a protracted economic slowdown. All in all, we are encouraged by the authorities' intention to address the weaknesses in the banking sector and by the launch of the 'Hercules' securitization scheme. The plan, nonetheless, has been deemed by some observers as too timid to make a difference considering the state of the Greek banking system. Staff comments would be welcome.

Labor market indicators are improving gradually, but structural rigidities continue to limit productivity growth and skills matching. Unemployment continues to decline from very high levels, and youth unemployment is slowly responding to the gradual recovery. We commend the new authorities' intention to support this trend by fostering greater labor market flexibility. Yet, we agree with staff that the steady implementation of active labor market policies is warranted to tackle high long-term unemployment and address the high skill mismatch and low productivity growth.

Pro-growth policy actions undertaken by the new administration are a welcome addition to the structural reform agenda, which must be continued to enhance long-term growth perspectives. Potential output in Greece has been significantly limited by unfavorable demographics, migration and the depletion of capital stock. Therefore, reducing accumulated imbalances to support growth will require years of sustained implementation of institutional and structural reforms for their impact to fully unfold. In addition, decisive measures towards implementation of the privatization plan, the correction of inefficiencies in public administration and the justice system, and the revision of the regulatory burden are necessary steps to improve the business climate and boost investors' confidence.

Mr. Benk, Mr. Harvan and Mr. Bukovina submitted the following statement:

We thank staff for their informative set of reports and Mr. Psalidopoulos for his informative buff statement. While Greece has achieved substantial progress in recent years and the new government has presented ambitious plans, going forward, implementing critical reforms agreed under the financial assistance program will be necessary. We associate ourselves with the statement by Mr. de Villeroché and offer a few remarks for emphasis.

We concur with staff on the need to rebalance the fiscal mix in order to meet the fiscal targets and safeguard debt sustainability. We note that the budgetary overperformance in 2018 has relied on under-execution of capital expenditure. We consider the announced reduction in direct taxes in 2020 a step in the right direction to recalibrate the fiscal adjustment. We also welcome continued efforts to strengthen tax compliance and payment culture and the partial reversals of the measures adopted in May 2019 that ran counter to reforms adopted under the ESM. We concur with staff on the downside risks for the budgetary outcome and stress the need to tightly monitor developments including the high number of ongoing court cases. Progress in implementation of growth-oriented structural reforms would put Greece on a stronger footing when dealing with budgetary risks from reversals of the business cycle and external macroeconomic shocks. We note that contrary to the Fund staff's forecast, the European institutions and the authorities project that the primary surplus target for the 2019-2022 period will be met. Could staff comment on the differences in the assumed impact of measures announced in the 2020 draft budget?

Despite a more adverse debt sustainability analysis, staff calls for a lower primary balance target already before 2022. We recall that the primary balance target was agreed within the Eurogroup and any revisions should consider implications for debt sustainability.

Further efforts to strengthen the stability and resilience of the banking sector are needed. To that end, we welcome the ambitious plans by the authorities to clean up banks and to bring the NPE ratio to single digits by mid-2022. We agree with staff that efforts should also include the elimination of potentially wrong incentives for banks and consumers as well as removing constraints in the resolution framework. The "primary residence protection" and "deferred tax credits" should thus be tackled in particular. While current capital buffers appear sufficient within the context of the NPE reduction targets, banks' ability to provide lending support for investment and growth would be improved by raising capital – not necessarily the CCyB as recommended by staff - and reducing reliance on deferred tax credits as capital.

The much-needed structural transformation of the Greek economy will require strong commitment to implement reforms to support growth and protect vulnerable groups. The still rigid business environment poses a major hurdle to attract more foreign investment and risks stalling privatization efforts. Benefits of lower direct taxes for potential growth might not bear fruit in the context of some reversal of labor market reforms and as highlighted by staff, a more dynamic recovery of the labor market has been prevented by weak implementation of product markets or business climate reforms. Could staff comment on whether the estimates of reform payoffs of lower direct taxes and higher investment are conditional on product and labor market reforms? Could staff provide more details on the downward revision of long-term potential growth estimates compared to last year's assessment?

Mr. Tan and Mr. Chea submitted the following statement:

We thank staff for the comprehensive set of reports and Mr. Psalidopoulos for the insightful buff statement.

While economic growth is projected to pick up in 2020, supported by expansionary fiscal policy and foreign direct investments, the Greek economy remains vulnerable to internal and external shocks, particularly in the near term. In this context, we regret to learn of significant policy reversals in the period leading up to the 2019 elections, which have complicated Greece's growth prospects that are already weighed down by significant crisis legacies. Strong country ownership and steadfast implementation of the reform agenda will be critical to foster macroeconomic stability and support higher sustainable and more equitable growth. In this regard, we are heartened by the buff statement that the Greek authorities have been elected with a mandate to implement their reform agenda and strong social consensus is now in place. We agree with the broad thrust of staff's appraisal and would like to offer the following comments for emphasis.

Rebalancing the fiscal policy mix and making tangible progress on fiscal structural reforms are essential to promote stronger growth and social outcomes. While we welcome the authorities' track record in meeting its fiscal commitments to European partners, it should not come at the expense of growth-friendly public investment and critical social spending. In this respect, we take positive note of the authorities' commitment to growth-oriented, inclusive fiscal policies and that primary balance targets should be lowered and a smoothing mechanism to allow temporary deviations from fiscal targets in the event of adverse shocks be set in place. We encourage the authorities to continue efforts to complete the independent revenue administration (IAPR) HR reforms consistent with the Fund TA, and further mobilize the AML/CFT framework to combat tax evasion. Accelerating fiscal structural reforms to strengthen revenue administration and public financial management should also remain as a priority. Could staff comment on the difference in views regarding pension cuts and lowering of personal income tax-free thresholds?

Breaking the ongoing cycle of high NPEs, low profitability and weak capital and liquidity buffers requires urgent and multi-pronged actions. We welcome the recent elimination of capital flow management measures and the ongoing resolution of non-performing exposures (NPEs). But faced with legacy challenges such as poor repayment culture, weak banking governance and practices, and inadequate financial sector policies, Greece's NPEs remain high and quality of capital remains weak while bank profitability is amongst the lowest in the region. Therefore, we agree with staff on the need for a more holistic strategy that is ideally more market-based, with appropriate sequencing of measures and coordination of key stakeholders. Could staff elaborate further on the details, particularly the prioritization of the reform agenda, and whether the authorities have the capacity to develop and implement such a strategy? And how likely would the authorities succeed in garnering market-based private efforts?

Complementary efforts to implement needed structural reforms both in the labor and non-labor markets will help support higher employment, boost productivity and competitiveness. We welcome the authorities' commitment to strengthen public-sector governance, transparency and institutional performance as stated in their buff statement. This will help foster better public sector efficiency and accountability. We also welcome the authorities' ongoing efforts in promoting business deregulation and labor market flexibility. Nevertheless, we agree with staff that further efforts are needed to address the structural labor market bottlenecks and accelerate the implementation of non-labor reforms. We encourage the authorities to prudently implement the new minimum wage framework, and further promote business deregulation to encourage product market liberalization in order to help foster inclusive work force participation and promote a more business-friendly environment for foreign direct investments.

With these remarks, we wish the authorities success in their future endeavors.

Mr. El Qorchi and Mr. Nadali submitted the following statement:

We thank staff for a well-written set of papers, and Mr. Psalidopoulos for his helpful buff statement.

Aided by debt relief from European partners and booming tourism, Greece has experienced a modest economic recovery over the past three years. In 2019, growth remains modest; inflation is low, with a large negative output gap; and unemployment has declined further but remains high. The fiscal position is in surplus, the external current account deficit has narrowed, and the elevated public debt is trending downwards, though debt sustainability is not yet assured. Despite improvements, bank balance sheets remain significantly impaired, contributing to continued credit contraction, and posing substantial fiscal and financial stability risks. The structural reform agenda also remains largely unfinished. The new government deserves credit for deciding to prepay part of the Fund credit subject to surcharges as well as pledging to follow pro-growth policies, which have been met with initial positive market reaction. The downside risks to the outlook, however, place a premium on further efforts to rebalance the fiscal policy mix, restore bank health, and advance structural reforms. We concur with the thrust of staff appraisal.

A more growth-friendly fiscal policy is necessary to support growth while remaining consistent with long-term fiscal and debt sustainability. Given damaging effects of priority expenditure compression on growth, we see merit in a somewhat lower primary surplus target over the medium term and a smoothing mechanism to allow temporary deviations from the fiscal targets in the event of shocks. Could staff indicate how likely it is for Europe to amend Greece's fiscal commitments under the enhanced surveillance framework and agree to a primary surplus target lower than the 3.5 percent of GDP in 2020-22? Cutting PIT and CIT rates, broadening the tax base, and modernizing revenue administration should be complemented by containing pensions and the wage bill, reorienting expenditure toward high quality investment and social outlays, and enhancing spending efficiency. We welcome measures to contain fiscal risks, including by strengthening public financial and investment management, and integrating risk management into the budget cycle.

The banking system has recently experienced some positive developments, including rising private deposits and renewed investor appetite. However, capital quality remains weak; system-wide nonperforming exposures (NPEs) are particularly high at 44 percent; some systemic banks are in breach of liquidity coverage ratios; and profitability is low. We welcome the authorities' Hercules asset protection scheme aimed at creating a more liquid and transparent secondary NPEs market, but agree that a more comprehensive, ambitious, market-based, and well-coordinated strategy is needed to bring NPE ratios to single digits by mid-2022 and restore banks' ability to finance growth. This requires promoting meaningful debt restructuring, including by an overhaul of the personal insolvency framework, streamlining judicial processes, and strengthening banks' internal governance.

Deeper and broader structural transformation to increase labor market flexibility, liberalize product and service markets, and accelerate privatization is needed to raise productivity, employment, and growth in the face of adverse demographics. The authorities' determination to push ahead with reform implementation, as indicated by Mr. Psalidopoulos, is praiseworthy. We welcome the government's recent labor market actions and its intention to link future minimum wage adjustments to productivity gains, address skill mismatches through vocational training, and boost female participation, including by improved access to dependent care. Could staff, however, indicate if the authorities are ready to go further and fully restore the 2011-13 landmark labor reforms? Work should continue to improve the business climate by streamlining regulations, opening closed professions, and reforming SOEs as well as network industries. Unblocking signature privatization projects and pushing through business deregulation and digitalization bode well for increased FDI. We welcome recent measures to combat corruption and encourage further progress in promoting good governance and the rule of law.

We wish the authorities success in their endeavors.

Mr. von Kleist and Mr. Fragin submitted the following statement:

We thank staff for its candid set of reports and Mr. Psalidopoulos for his informative buff statement.

We concur with staff's view that Greece's economic recovery continues, but remains sluggish, reflecting not least a wide range of persisting structural impediments and incomplete reforms. Greece's prospects for economic convergence are clouded: Productivity remains low, weak bank balance sheets weigh on growth and on fiscal as well as financial stability and investment remains muted. We appreciate the new government's commitment to pro-growth reforms. As staff rightly notes, one key challenge will be to overcome the influence of vested interests and to aim at a broader burden sharing of the economic adjustment within society and among reform areas. We associate ourselves with Mr. de Villeroché's statement and would like to provide the following additional remarks.

We do not concur with staff's support for lower primary balance targets. Given the projected gradual closing of the output gap, a fiscal expansion (in cyclically adjusted terms) is possible while keeping the 3.5 percent GDP aim for the primary budget unchanged until 2022. The authorities should meet their fiscal commitments to EA member states under the ‘Enhanced Surveillance’ framework. Moreover, for the years from 2023 onwards caution is warranted with a view to compliance with the SGP. Currently a primary surplus of around 2 percent is projected. But it should be noted that the associated overall structural balance might be substantially worse than allowed under the SGP (overall structural deficit higher than 0.5 percent of GDP).

We agree with staff that the authorities should improve the fiscal policy mix in order to boost socially inclusive, higher growth. As outlined by staff, the Greek tax policy falls behind EA averages when it comes to growth-friendliness and inclusiveness. The public wage bill has been crowding out social spending and investment. Therefore, we agree with staff that the authorities should seek to enhance their spending efficiency and reorient public expenditures towards high quality investment and targeted social spending. Moreover, the authorities should address the causes of the systematic under-execution of investment spending in order to improve budgetary practices and to fully utilize the resources available for public investment to support growth. In this context, we take note that the authorities intend to improve their fiscal policy mix by allocating two thirds of any additional fiscal space to tax reductions and the rest to targeted social and investment spending. How does staff assess these plans?

We recognize staff’s renewed call for broadening the tax base by lowering the PIT tax-free threshold. We take note that the PIT tax-free threshold is relatively high, compared to the EA average. We further note that lowering the PIT tax-free threshold could increase the authorities’ scope for growth-enhancing measures. However, the comparison of the thresholds among EA countries could be enhanced by including the mean annual earnings. Furthermore, we would have appreciated a more detailed discussion on measures aiming at broadening the tax base for the high income bracket and increasing efforts to reduce tax evasion and improve tax compliance.

We support the government’s focus on cleaning up banks’ balance sheets, while appreciating staff’s candid, if sobering, assessment of the urgent challenges facing the Greek banking system. We note with some concern that system-wide NPEs remain the highest in Europe while profitability is the lowest. We also take note of staff’s assertion that any major bank failure would be highly destabilizing. Therefore, we share staff’s recommendations to accelerate financial sector reforms and restore bank viability. This would imply inter alia promoting meaningful debt restructuring and payment discipline, fast and resolutely reducing NPEs, building and improving the quality of capital, and containing the bank-sovereign nexus. Regarding the latter, we concur with staff's recommendation against relaxing ECB-mandated sovereign exposure ceilings. However, the above objectives may be mutually conflicting: With regard to the asset protection scheme ("Hercules") the government would assume risks by granting a guarantee on securitized non-performing loans. In addition, the securitization of NPEs would lead to a transfer of risks into less supervised secondary markets. Therefore, we echo staff's call to improve the legal framework such that any public support is subject to a dynamic cost-benefit analysis and in line with the EU framework.

We take note that Greece's current account deficit has widened. With all due caution about the methodological uncertainties, staff's high estimates of Greece's cyclically-adjusted current account deficit and of the negative residual testify to the critical need to boost competitiveness and reduce product and labor market rigidities. Interestingly, staff's fiscal policy advice would contribute to a further weakening of Greece's external position, thereby – all else equal – causing the current account gap to increase further. Against this background, could staff elaborate on the outlook for the external position and the respective roles of structural reforms and fiscal policy in this context?

Against this backdrop and given the shortfalls in reform implementation diagnosed by staff, we welcome the authorities' intention to address structural labor market bottlenecks as well as rigidities in product markets. As also noted by staff, structural unemployment is among the highest in the EU. Reforms aimed at labor reactivation and inclusion as well as aligning labor provisions with ILO best practices are thus welcome steps towards a recovery of employment. Furthermore, narrowing the structural competitiveness gap vis-à-vis the EA remains a challenge. Reforming SOEs and network industries is therefore key to create a more competitive and dynamic economy with a welcoming business climate in order to boost employment, innovation and productivity.

Finally, we appreciate that Greece has strengthened its AML/CFT regime in line with international standards, even though gaps remain. We echo staff's call to improve the rule of law and to speed up the reform of the Criminal and Criminal Procedures Codes to align with the OECD's Anti-Bribery Convention. In addition, we concur with staff on the importance of enhancing the quality and efficiency of the judicial system as well as safeguarding the achieved improvements in the quality and credibility of official statistics.

Mr. Bhalla and Mr. Goyal submitted the following statement:

We thank the staff for Article IV Consultation Report on Greece, and Mr. Psalidopoulos for his informative buff statement. Greece continues to make recovery but falls short of expectations. Slower progress on structural reforms vulnerabilities continue to pose fiscal and financial stability risks. We acknowledge the policy stance of the newly elected government towards growth and commitments made to the Euro Area on fiscal and structural policies, but it may be challenging. Notwithstanding these vulnerabilities, Greece with official debt relief and market issuances has been able to create significant liquidity buffer and is seeking to prepay Euro 2.7 billion of its Euro 8.4 billion IMF loan.

We note that Greece continues to overperform against its fiscal target commitment to European partners, but it is largely with under execution of public investments. Fiscal consolidation efforts essentially need to focus on improving tax compliance and reorienting of expenditure on investment and quality social spending. Key hindrances to improvement in fiscal outcomes include narrow tax base, tax evasion, weakening of payment culture by installment schemes and burden of pension spending. In the runup to the elections, authorities diluted the efforts to bring in fiscal reforms. We support staff recommendations to authorities to cut pensions, lower the personal income tax-free thresholds, to implement stronger tax collection measures and to end 'temporary' ad hoc installment schemes.

As per staff assessment, Real Effective Exchange Rate (REER) is overvalued by 10 percent given the gap between cyclically adjusted current account balance and that consistent with fundamentals and desirable policies. This would necessitate authorities to complete the unfinished reform agenda, particularly with respect to labor and product market reforms, to unleash productivity and strengthen competitiveness. Given the recent labor market policy reversals and difficulties with implementing labor reforms in the backdrop of social perception that workers have borne the brunt of adjustment, productivity-enhancing measures would be needed to maintain/ improve competitiveness. Whether authorities are contemplating some specific steps in this regard - staff may like to comment.

The nonperforming exposure (NPE) at 44 percent, which is the highest in Europe, weighing on banks' profitability and capital adequacy, remains a significant impediment to future growth. Despite significant injection of capital both by government and by private sources, banking system has continued to be vulnerable and source of fiscal and financial instability risks.

We note steps being envisaged by the authorities to clean up the banking sector - creation of a new Deputy Minister position to oversee bank reforms, proposal to set up a separate asset management company involving government support and intentions to bring NPE ratio to single digit by mid-2022. We believe that restoration of banking health would essentially require an effective insolvency framework and support staff suggestions relating to elimination of Primary Residence Protection (PRP), creation of credible foreclosure threats and limit on the length of debt installment schemes. Staff may like to elaborate on the fiscal impact of proposed asset management company involving government support.

Mr. Moreno and Ms. Mulas submitted the following statement:

We thank staff for its comprehensive set of papers and Mr. Psalidopoulos for his informative buff statement. We associate ourselves to Mr. de Villeroché's statement and would like to add the following remarks.

Greece progress and reform track needs to be recognized. As highlighted in the acting chair's summing up on the first post-program monitoring, Executive Directors welcomed the commendable progress in implementing reforms which have helped restore stability and growth, reduce unemployment, improve debt sustainability and regain market access. Against this backdrop, we share the authorities' view that the staff report could be more balanced in recognizing these efforts. It is important to acknowledge the sacrifices of the Greek people and the authorities' efforts to implement reforms, including a significant fiscal adjustment.

We welcome the authorities' commitment to reform. As stressed by staff, the new government has made a promising start in unblocking structural reforms and privatizations and in advancing the clean-up of bank's balance sheets. It is reassuring from Mr. Psalidopoulos' buff that the authorities have a strong ownership of their reform agenda and have the electoral mandate to implement it. We encourage authorities to use the current positive economic juncture and their majority in Parliament to maintain and deepen the current reform momentum.

We share staff's view on the need of fiscal policies to boost socially inclusive growth. We find very interesting the analysis of the inclusive growth indicator in Annex V, which highlights its deterioration, particularly during the crisis. We agree with staff that expenditure needs to be reoriented to social spending. The current draft budgetary plan 2020 already includes several discretionary measures to foster social protection. Staff's views are welcome.

Which measures should be prioritized or included to foster a more inclusive growth? Staff supports a lower primary balance path to provide additional fiscal space for social inclusion and growth policies. At the same time, the Debt Sustainable Analysis notes that the debt-to-GDP path for 2019–25 is projected at a higher level due to lower GDP nominal growth and lower primary surpluses over the projection period. Could staff advice on the DSA's impact of a lower primary balance path? We recall that the primary balance target was agreed with the Eurogroup, consistent with the European fiscal rules and considering the implications for the debt sustainability analysis.

Authorities should address the bottlenecks of arrears management. The Greek authorities have committed to clear the stock of arrears, avoid the accumulation of new arrears, and complete the implementation of reforms identified by the Hellenic Court of Auditors. Despite the fact that the net stock of arrears has decreased since the end of the program, the pace of reduction has significantly slowed, and new arrears continue to be created in some sectors. Therefore, we encourage authorities to foster the implementation of the structural measures to address the bottlenecks of arrears management.

We welcome the "Hercules Plan" as an important step to resolve the reduction of non-performing loans (NPLs) of Greek banks. The recent assessment of the Commission that the "Hercules Plan" is free of any State-aid will facilitate attracting a wide range of investors and support banks in their ongoing efforts to reduce the amount of NPLs on their balance sheets. Over the last two years, NPLs were reduced by a quarter, which is significant, and the banks have also set up relatively ambitious strategies for the next three years. Still, the ratio of NPLs to total loans will remain relatively high; therefore, it is important to ensure effective legal framework and judiciary processes to foster the resolution of NPLs.

In the labor market, challenges include both labor reactivation and inclusion. We concur with staff on the need for fostering labor reforms, particularly more effective labor activation policies to support employability and skills-matching. On the minimum wage increase and the abolition of the sub-minimum wage, we consider appropriate the authorities' decision to give enough time to assess its impact on the pace of recovery in the labor market, as staff itself recognizes that the research on Greece is inconclusive. We welcome the recent provisions relating to childcare aiming to increase female labor market participation, as it remains low by regional standards.

We agree on the need for further measures to improve the investment climate and foster competition. While significant and wide-ranging reforms have been delivered in recent years to improve the business environment, much remains to be done in this area to support the shift towards a more export- and investment-led growth model. Overall, it will be crucial to focus reform efforts on product markets to improve product choice, quality, and competition. The interesting SIP finds out that the more competitive wage structure has only partly translated into price adjustment due to product market rigidities and rising non-wage costs factors. Therefore, a renewed reform push in the product market front has the scope of fostering higher employment and growth. We welcome the accelerated efforts to unblock signature privatization projects and the lifting of remaining capital flow management measures (CFMs) on outflows. Finally, we would encourage staff to analyze measures to address climate change in Greece in future Art. IV consultations.

Mr. Rosen, Ms. Pollard and Ms. Crane submitted the following statement:

We thank staff for the informative papers and Mr. Psalidopoulos for the helpful buff statement. We welcome that Greece's economy continues to recover, with an uptick in growth and decline in unemployment in 2018, albeit slower growth so far in 2019. We appreciate that the new government has made important initial policy steps in the right direction and we believe the authorities' plans for reform merit support. We are heartened by Mr. Psalidopoulos' reference to a strong social consensus in favor of reform, in the buff statement. We recognize Greece's relatively strong liquidity position, and we welcome the recent removal of the remaining capital flow management measures. Nonetheless, the lack of durable progress over many years on improving Greece's competitiveness and long-term growth potential is discouraging, and the new authorities' ability to overcome vested interests remains to be seen. We concur with the thrust of the staff appraisal and would like to highlight several points.

Fiscal Policy. We are concerned by the low quality of Greece's ongoing fiscal adjustment. Greece continues to "over-perform" on its fiscal targets at the expense of growth, while slipping on measures aimed to improve the quality of the fiscal policy mix. We urge the authorities to consider base-broadening tax measures, in addition to planned tax cuts, and to vigorously implement stronger compliance. On the spending side, we encourage the authorities to explore how to better control pensions and public wages to make room for priority social and capital investment spending. We are concerned that under current policies, authorities may be forced to resort once again to compression of much-needed, growth-enhancing capital spending. We encourage the authorities to consider seeking agreement with

European partners on a lower fiscal surplus path to better support growth, and a fiscal smoothing mechanism to provide more room for counter cyclical policies, as recommended by IMF staff.

External Competitiveness. With efforts at internal devaluation incomplete and subject to backtracking in recent years, Greece needs to address high labor and non-wage costs relative to peers. We welcome the new government's initial intentions on collective bargaining, arbitration and the minimum wage, along with privatization plans. The Selected Issues Paper on Reforms, Labor Market Dynamics and Competitiveness points to the importance of increasing the dynamism of firms so that labor cost reductions translate into reduced prices and improved competitiveness rather than higher margins for firms. We encourage the authorities to prioritize improvements in product markets and the business environment, as an essential complement to policies to increase labor market flexibility. Active labor market policies and targeted social support can also cushion the burden borne by labor.

Banking Sector. Another key concern is that banking sector weaknesses continue to weigh on growth. We urge the authorities to build on the planned Hercules scheme and push forward with comprehensive measures to decisively address non-performing exposures. Consideration should be given to the creation of a public bad asset resolution entity in order to cleanse banks' balance sheets and allow a resumption of effective intermediation. We would also note that staff makes an excellent case in the Selected Issues Papers for limiting residential mortgage protection and ad hoc social security installment schemes to help strengthen payment discipline.

Data. We welcome the establishment of the Hellenic Statistical Authority and the recent elimination of discrepancies in fiscal reports of the Bank of Greece. We echo staff in urging the authorities to support the independence and professionalism of ELSTAT.

Mr. Palei and Mr. Shestakov submitted the following statement:

We thank staff for the well-written report and Mr. Psalidopoulos for his insightful buff statement. We welcome the progress achieved by the Greek authorities in reducing macroeconomic imbalances and implementing structural reforms. Over the past decade, Greece has achieved fiscal adjustment and recorded competitiveness gains under the conditions of the extreme depression. However, large productivity gaps persisted. High public debt and unemployment, and the fragile financial system continue to constitute vulnerabilities. The lack of a broad public support for continuing the reform agenda was indicated by the policy retreat in August 2018. We welcome the renewed commitment of the new administration to the reforms. The new Greek authorities should consider using their political mandate to improve the business climate and ensure inclusive and broad-based economic growth.

We welcome the new authorities' pro-growth efforts and agree with staff that the ability to overcome vested interests and push through the reform agenda will prove critical. The staff's estimates of long-term economic growth remain rather pessimistic, close to 0.9 percent. In this respect, we note that higher growth projected by the Greek authorities could also be feasible under the scenario of comprehensive and well-coordinated reforms.

Current estimates of structural unemployment around 13 percent reflect both adverse headwinds of the aging population and slower export growth due to global trade uncertainty. Policy reversals following the 2011-2013 labor market reforms contributed to lackluster employment growth. Product and labor market liberalization, further privatizations and increased labor market flexibility should ensure the Greek economy resilience against the downside risks of the global economic slowdown and Brexit. Have the Greek authorities presented a timeline for the upcoming reforms? Could staff identify possible political challenges for the new administration in following the reform agenda?

The increased capacity of growth-promoting institutions should relieve structural constraints. In this regard, we welcome the establishment of the National Transparency Authority, modernization of the judicial system to improve the rule of law, and adherence to the AML/CFT framework.

Public debt-to-GDP is projected to trend down over the next decade with low liquidity risks, but staff are not assured of the long-term debt sustainability. We note a divergence between the authorities' view and those of staff on the DSA assumptions regarding the projected effective interest rate on total public debt. Could staff explain why the Greek debt is considered less sustainable in the long term against the background of both lower risk-free rates and lower Greek risk premium?

We call on the Greek authorities to adhere to their fiscal targets without jeopardizing economic growth and social inclusion. We agree with staff's recommendations that direct tax cuts should be combined with tax base broadening, eliminating poorly targeted tax relief, and stronger tax collection efforts. The social spending mix should be made more inclusive by adjusting pensions and a public wage bill and putting more emphasis on the means-tested Social Solidarity Income and public health.

A weak banking sector continues to pose a financial stability risk. Non-performing exposures (NPEs) are reduced, but the pace of reduction slowed, and credit growth remains negative. Further deterioration of bank balance sheets may lead to deposit outflows with potentially costly public interventions. We welcome the "Hercules" asset protection scheme and encourage the fast adoption of the legislation to pave the way for a more liquid secondary NPEs market. Other financial reform initiatives including better insolvency regime should foster a profitable and efficient banking sector.

With these remarks, we wish the Greek authorities success in facing challenges ahead.

Mr. Chikada and Mr. Kuretani submitted the following statement:

We thank staff for a set of comprehensive reports and Mr. Psalidopoulos for his informative statement. We welcome Greece's continued economic recovery, the new government's pledge to follow pro-growth policies, and improved investor sentiment towards Greece. However, vulnerabilities stemming from the crisis legacy, including but not limited to high public debt and weak bank balance sheets remain. Thus, continuous reform efforts and strong political resolve to tackle vested interests are imperative to sustain the recent positive momentum and ultimately realize the benefits from the decade-long adjustments Greece have endured. We broadly concur with the thrust of the staff appraisal, and would like to offer the following comments:

Fiscal Policy

Fiscal policies should focus on more balanced burden sharing and fiscal policy mix to realize socially inclusive growth. We are particularly concerned that the poverty rate for the youth has increased significantly while that for the retired has declined markedly over the last decade. We commend that the 2019 primary surplus is projected to exceed Greece's 3.5 percent of GDP commitment to the European partners due partly to stronger tax revenue collection. We welcome that meeting its fiscal targets has boosted Greece's credibility. However, revenue mobilization needs to be strengthened and overreliance on higher tax rates should be corrected by addressing narrow tax bases, which reflect a weak payment culture and vested interests. We encourage the authorities to broaden the tax base through tax policy changes and enforcement, to strengthen the Independent Authority for Public Revenue (IAPR) and mobilize the AML framework to combat tax evasion.

On the expenditure side, while we welcome that the new government has started to undertake several pro-growth policy actions, we urge the authorities to consider more about striking the right balance between spending on pensions and those on other social spending and investment. In this context, we concur with staff that the authorities should make further improvements in budget planning and implementation, consistent with Fund TA.

We welcome that the coverage and timeliness of data compilation processes have improved by TA from the IMF and others. However, there are discussions focused on additional actions to improve the rule of law and data transparency. We would appreciate if staff could elaborate more on how to improve these areas in addition to the issues in the report.

Financial Sector

The authorities need to address the banking sector weakness expeditiously to restore bank lending and support the economy. It is welcoming that the new government is prioritizing bank clean-up by calling for aggressive Non-Performing Exposures (NPE) reductions aiming to bring NPE ratios to single digits by mid-2022, in addition to the Hercules scheme. To this end, further improvements in the legal frameworks and effective enforcement are imperative, and we concur with staff that an overhaul of the personal insolvency framework is needed by abandoning Primary Residence Protection (PRP) as a financial policy objective, creating a more credible foreclosure procedure, and limiting the length of debt installment schemes.

Mitigating Internal Devaluation Costs

Greece needs to endure internal devaluation to improve its competitiveness in the currency union, however, adjustment costs could be mitigated by well-coordinated reforms. We welcome that the new government has signaled a preference for greater labor market flexibility and achieving full employment through the Development Law. However, the authorities should aim at full restoration of the 2011-13 landmark labor reforms to improve labor market conditions. We encourage the authorities to focus on productivity enhancement through improved labor market flexibility, more effective labor activation policies, stronger institutions, and business deregulation. In this regard, we commend staff's analysis on the relations among wage policies, non-wage cost developments, and competitiveness. We concur with staff that the non-wage reforms such as product market, business climate, and banking reforms should be prioritized to avoid putting further adjustment pressure on wages.

Mr. Ronicle and Ms. Andreicut submitted the following statement:

We thank staff for the set of reports and Mr. Psalidopoulos for his informative buff statement. We broadly agree with the thrust of staff's analysis and welcome the range of topics covered in the selected issues paper. We are encouraged by Greece's continued economic recovery and by the commitment of the newly elected government to pro-growth policies. Greece has come a long way, though much remains to be done to restore incomes to pre-crisis levels. We therefore urge the authorities to redouble their efforts, making the most of the current low financing costs and the window of political opportunity.

Macroeconomic developments

We welcome the solid pace of growth in recent years, the ongoing decline in unemployment and the decline of Greek spreads to their lowest level in a decade. We also take note of the full repayment of Emergency Liquidity Assistance, plans for early repayment of the Fund and of the fact that Greece's primary balance in 2018 was well above the country's original commitment. Despite these positive developments, growth is expected to slow, inflation is weak, and staff note that debt sustainability is not assured. Could staff elaborate on what outcomes might be expected for key macroeconomic variables, especially growth, unemployment, inflation and the debt-to-GDP ratio, if the ECB were to take further action to bring inflation to target at a conventional 18-24 month horizon?

Fiscal policy

While large primary surpluses will help accelerate the reduction in debt vulnerabilities, and appear to have reassured markets, we agree with staff that achieving this through under-execution of investment is detrimental to growth. We welcome the reduction in some headline tax rates, and the base-broadening for some taxes, but think base-broadening could go further and that expenditure needs to focus on investment and well-targeted social spending.

Structural reforms

We welcome recent structural reform measures, including improving labor market flexibility, the re-skilling of the labor force and encouraging female participation, as well as the removal of barriers in outsourcing to private contractors. These measures have markedly improved business sentiment and should in turn stimulate private investment.

We also take note of the challenges ahead, not least of the fact that the new government is inheriting a difficult starting point, including policy reversals across financial, labor and product markets. Given the promising start, we urge the authorities to maintain their level of ambition and the current pace of reform.

Financial sector

A well-functioning and adequately capitalized banking sector is essential for long-term growth and will ensure credit flows to the real economy. We agree with staff's assessment that the banking sector is a top priority and that efforts in reducing the stock of non-performing exposures (NPEs) should continue. We are encouraged by the commitment of the new government to fix bank balance sheets, as well as by their ambition to bring NPE ratios into single digits by mid-2022.We also welcome good progress made by the authorities through the recent 'Hercules' asset protection scheme. Like staff, we also stress the importance of improving the quality of bank capital, which is excessively reliant on deferred tax credits that do not provide adequate loss-absorbing capacity. That will require the sort of comprehensive plan outlined by staff, including: reducing NPEs; equity issuance; reform of the personal insolvency regime; and, strengthened bank profitability.

Mr. Mahlinza and Mr. Jappah submitted the following statement:

We thank staff for the well-written set off reports and Mr. Psalidopoulos for his helpful buff Statement.

We take note that the Greek economy continues to recover, following exit from the Fund-supported program. However, significant challenges remain, including emerging fiscal and financial sector vulnerabilities as well as structural rigidities. Accordingly, we take comfort from the authorities' indication of strong ownership and determination to implement reforms as outlined in the buff Statement. In this respect, we encourage greater focus on rebalancing the fiscal policy mix to support growth, repairing banks' balance sheets, upgrading governance and transparency, and supporting employment and productivity growth. We broadly agree with staff's appraisal and offer the following comments for emphasis.

A prudent fiscal policy remains essential to place public debt on a declining path. We take note, however, that the recent overperformance against fiscal target commitments has boosted credibility while taking a toll on economic growth. We therefore, urge the authorities to adjust the policy mix towards high quality investment and social spending. We also concur with staff that the authorities should engage Euro Area partners on a lower primary balance target as well as consider a smoothing mechanism to allow temporary, symmetric deviations from the primary deficit target. Could staff clarify the chances that this request could be accepted by the Euro area partners? Are there precedents for such? Further, we welcome the administration's commitment to simplify the tax system to create a pro-business environment. In this regard, we commend the authorities for measures articulated in the Draft Budget Plan (DBP 2020) aimed to reduce property tax, corporate tax, value-added tax, as well as personal income tax rates in the lowest bracket. We, however, take note of the disagreement between the authorities and staff on the debt outlook, with the authorities citing recent reduction in the credit spreads as a basis for a more optimistic outlook. According to Mr. Psalidopoulos' statement, staff's last report rated public debt as more sustainable, while the current report flags it as less sustainable in the long term. Can staff elaborate on the change in assessment?

Restoring bank viability and further financial sector reforms should remain a priority. Against this background, we welcome steps taken to facilitate the resolution of non-performing exposures (NPEs), including the appointment of an oversight authority. That said, NPEs remain very high at 44 percent, constraining banks' capacity to lend. On this premise, we concur with staff on the need for a more comprehensive and ambitious bank resolution strategy, supported by strong supervisory incentives. Such an approach would entail a recalibration of the sector's policies to accelerate the pace of balance sheet clean up to resolve liquidity challenges and improve on banks' profitability. Relatedly, we look forward to the enactment of the Hercules Bill which is intended to mitigate the impact of NPE write-offs on investments in the banking sector, through securitization. Lastly, we welcome the removal of capital flow measures.

Reinvigorating structural reform implementation is key to supporting economic growth. In this context, we welcome the new administration's focus on greater labor market flexibility that strikes a balance between employees' rights and competitiveness. At the same time, the full restoration of the 2011-13 labor market reforms, which the authorities acknowledge, led to an increase in employment, should remain a priority. Further, we urge the authorities to scale up post-secondary, vocational and adult education in line with labor market requirements and intensify the reskilling programs. We welcome the drafting of a new Development Bill that aims to attract strategic investments, expand employment opportunities, improve living standards, and create a business-friendly environment through the streamlining of business licensing procedures. In addition, we support the planned review of the status of "closed" professions, which we hope would pave the way for simplification of entry requirements. Can staff comment on the status of the new Development Bill which was expected to be enacted into law at end October?

Mr. Doornbosch and Mr. Cools submitted the following statement:

We thank staff for the very good report and Mr. Psalidopoulos for the informative buff statement. The report points out the risks to the Greek economy and highlights the priorities for the new government. The Greek economy is recovering, but at a slower pace than expected. We welcome the new government's pro-growth agenda and invite the government to undo crisis-era policy reversals. We support the priorities highlighted by the IMF, which are in line with Greece's June 2018 Eurogroup commitments. We associate ourselves with Mr. de Villeroché's statement and would like to make the following points for emphasis:

First, impediments to efficient product markets and to competition should be addressed. According to the interesting Selected Issues Paper, program-era policies have made Greece's wage structure more competitive. However, this has only partially translated into price adjustments, specifically due to product market rigidities. We welcome staff's recommendation regarding the establishment of a real-time assessment capacity of current barriers to product markets and competition as a good starting point. Sustained ambition by the authorities will be needed.

Second, we concur with staff that the fiscal policy mix should be focused on growth and inclusion. In that light, the composition of the social spending budget could be reoriented towards critical issues such as health and education.

Third, on financial sector issues, we commend the significant efforts over the last years by the Greek authorities in reducing NPEs, as described in Mr. Psalidopoulos buff statement. We welcome the authorities' recent increased efforts to address the slowing pace of non-performing exposures reduction. We also commend the government's efforts, as highlighted in Mr. Psalidopoulos' statement to reboot the Greek financial system, including far reaching reforms of its capital markets.

Mr. Lopetegui and Mr. Vogel submitted the following statement:

We thank staff for the reports and Mr. Psalidopoulos for his helpful buff statement.

Growth has returned, albeit at a modest pace. After the huge crisis suffered by the country, it was only in 2017 when Greece started to grow at rates above 1 percent, while remaining below 2 percent. Nonetheless, the staff report projects growth rates below 1 percent from 2022 onwards. Unemployment has been declining substantially, but remains high; non-performing exposures, at 44 percent in 2019Q2, are still at levels that pose critical obstacles to credit and growth. We acknowledge the important efforts and progress made by Greece and its population in terms of fiscal adjustment; however, the public debt-to-GDP ratio is still at a problematic level, exactly as projected for 2019 in the staff report issued in July 2017, at the time of the request for a Stand-By Arrangement. We do want to highlight, however, that the authorities have been able to build a strong liquidity position and that capital flow measures have been removed.

We welcome the Greek authorities' firm commitment and ownership of their reform agenda, which constitute a fresh start for the country. As Mr. Psalidopoulos rightly underlines, legacy issues do not constitute an insurmountable obstacle to economic recovery. Sound policies, appropriate reforms, and an understanding of the circumstances may perfectly reverse the adversity. In this regard, we note important differences between the staff and the Greek authorities on projections and, in this regard, we would like to have further elaboration from staff on these different outlooks.

The country's significant efforts in the fiscal area are clearly reflected in the primary fiscal surplus posted in recent years. For instance, the 2019 primary surplus is projected to be 3.7 percent of GDP, which is only a bit lower than past records above 4 percent. The staff report underscores that market analysts and rating agencies acknowledge that meeting its fiscal targets has boosted Greece's credibility. Nonetheless, if prolonged and sizable fiscal adjustments and the country's consequent credibility do not translate to growth and welfare among the population, as observed in many cases, they will generate reform fatigue, negatively impacting the recovery process.

Moreover, there is a need to improve the quality of the fiscal adjustment. We share the staff's comments that the authorities should seek consensus with European partners on a lower primary balance target, given the large negative output gap and the need to bring down high tax rates and address unmet spending needs. In general, the staff report provides timely recommendations on fiscal measures in order to boost social and inclusive growth.

We are encouraged by the authorities' efforts aimed at addressing the financial system's vulnerabilities that still constitute critical obstacles to investment and growth. In paragraph 25, the staff report underlines some of the same factors that have prevailed for more than a decade, with the result of weak quality of capital and the highest level of NPEs, among others. We welcome the agreement between the authorities and staff that measures to restore the banking system should be accelerated.

Efforts in structural areas need to continue to reinvigorate growth and enhance external competitiveness. We feel reassured by the authorities' determination to push ahead with the implementation of growth enhancing reforms, as stated by Mr. Psalidopoulos in his buff statement, which contains specific initiatives undertaken during the last months, including the passage of the Development Law, and other measures to be considered in the short term.

We welcome the report's conclusion that Greece has strengthened its AML/CFT regime in line with international standards. The authorities' view and initiatives regarding institutions are steps in the right direction in terms of transparency, stability, and rule of law, which unambiguously contribute to investment and growth.

With these remarks, we wish Greece and its people every success in their future endeavors.

Mr. Raghani, Mr. Sylla and Mr. Alle submitted the following statement:

We thank staff for a comprehensive set of papers and Mr. Psalidopoulos for his informative buff statement.

Greece exited a decade-long period of adjustment programs aimed at recovering from deep-rooted economic woes. We welcome the macroeconomic gains of the reform efforts, including returning growth, better fiscal figures and improvements in employment. Going forward, the challenges still facing the economy are commensurate and require a strong reform momentum. In this regard, we welcome the ownership and the commitment of the new government to implement their reform agenda, aided by a strong social consensus as stressed by Mr. Psalidopoulos. In their endeavors, we encourage the authorities to emphasize pro-growth structural reforms, enhancing public debt prospects and gradually improving living standards which suffered years of crisis.

The fiscal policy mix should combine growth-enhancing tax clauses with a set of measures to broaden the tax base. The authorities should be encouraged to fine-tune their reform package to meet the dual objective of reducing a range of taxes to boost growth while broadening the base with others. In this regard, we welcome both policy measures such as bringing new regions to the property tax basket and administrative reforms geared toward digitalizing tax operations. Likewise, we see merit in measures to boost disposable income with an expected positive impact on consumption and growth. Going forward, we encourage the authorities to step up fiscal reforms that could yield higher payoffs, as presented in Box 1, P. 9. We concur with staff that labor tax cuts which increase higher labor force participation together with steps to improve infrastructure and the business environment could deliver stronger GDP growth.

We welcome staff assessment that the public debt-to-GDP is projected to trend down in the next decade. The reduction of Greek bond yields and credit spreads observed over the past eighteen months as pointed out in the buff statement is an encouraging sign in this regard. The authorities should be advised to keep up with their fiscal commitments including with the EU, in order to further improve market sentiment. The planned partial early repayment of Greece's IMF loan should also help in the same vein and contribute to improve the debt sustainability outlook.

We welcome the authorities' commitment to clean up banks as a step to enhance lending for investment and growth. Signs of improvements in the sector are encouraging, including the recent full repayment by banks of the Emergency Liquidity Assistance, rising private deposits, access to secured interbank financing and renewed investor appetite. The appointment of a high official to oversee financial sector reforms and the setting of aggressive non-performing exposure targets by banks are early positive steps for reforms. Efforts in this regard should focus on improving coordination among stakeholders, enhancing the quality of capital and banking practices, and enforcing compliance with key ratios. Furthermore, we encourage the authorities to adopt staff-recommended holistic strategy with appropriate sequencing of measures for a sound and strong financial sector delivering credit to the economy and supporting growth.

Far-reaching structural reforms are needed to support growth and structural transformation. We welcome achievements in labor, products and services markets reforms. From staff analysis, “the 2011-13 collective bargaining and minimum wage framework reforms helped lower labor costs, improve labor market flexibility and employment recovery, and reduce external imbalances”. At the same time, despite the fact that labor market distortions contributed to the country’s imbalances in the 2000s - as analyzed in the Selected Issues -, staff reported that “in a context of social perceptions that workers bore the brunt of the adjustment, the authorities implemented a series of labor market policy reversals following program exit”. Could staff elaborate on the impact of those policy reversals? Furthermore, what lessons can be drawn from such developments in terms of the IMF engagement and policy recommendations to member countries, especially in times of crisis?

Going forward, more effort is needed to address structural bottlenecks to growth and unlock the economy’s potential. In this regard, emphasis should be put on improving the business climate to the level of peers in the European area. Steps already taken, including to finalize some signature privatization projects, deregulate business licensing, attract FDI by lifting constraining spatial planning rules, go in the right direction. Likewise, we see merit in restructuring some SOEs, reviewing the status of closed professions and developing an export promotion strategy to address non-price competitiveness. As the recovery takes holds, we encourage the authorities to take measures to improve living standards for the segments of the population which have been hit hard during years of crisis.

With this, we wish the Greek authorities, every success in their endeavors.

Ms. Levonian, Ms. McKiernan and Mr. Mooney submitted the following statement:

We thank staff for their comprehensive report and Mr. Psalidopoulos for his buff. The Greek people have undertaken considerable sacrifice over the last decade and deserve credit for the progress that has been made during that period. We strongly welcome that economic growth continues in Greece, albeit at a slower pace than anticipated. Risks to the outlook are tilted to the downside in the short term, and we agree with staff that the implementation of more ambitious structural reforms could raise potential growth above current projections in the medium term. We agree with the main thrust of staff’s assessment and offer the following points for emphasis.

We believe that an appropriately sequenced implementation of the reform agenda would contribute positively to an uplift in growth in the medium to long term. In terms of debt sustainability, we note staff's view that this is not assured under a realistic set of macro-fiscal assumptions over the long term, although the buff argues that this is an overly pessimistic assessment. Can staff address the concern raised in the buff that they did not consider the reduction in Greek bond yields and credit spreads over the past eighteen months in their analysis? We agree that fiscal policies should be predicated on boosting socially inclusive growth. In this regard, we support a broadening of the tax base and an increased focus by the authorities on stronger tax collection efforts. In terms of expenditure policy, we encourage further efforts to improve budgetary planning and implementation.

On the financial sector, we note the progress that has been made through concerted efforts by authorities to address the relevant weaknesses. However, NPEs remain at the highest level in Europe and we welcome the "Hercules" state-supported NPE securitization guarantee scheme. We positively note the Prime Minister's ambition to bring NPE ratios to single digits by mid-2022. We support staff's call for an overhaul of the personal insolvency framework and agree that faster reduction of the household insolvency case backlog is key to supporting NPE reduction. To further strengthen the banking sector, the loss-absorbing capacity of bank capital should be strengthened. In this regard, we agree with staff that reducing the share of deferred tax credits (DTCs) to total capital is important. We note that staff have called for a credible, comprehensive, coordinated strategy regarding the implementation of these measures. While we would be supportive of such a strategy, can staff elaborate on who would design and lead such a scheme, and the main stakeholders involved? In terms of the AML/CFT framework, we note the conclusions of the recent FATF assessment report which indicates that the regime is in line with international standards and encourage authorities to address swiftly the remaining weaknesses.

We welcome the new government's policy agenda, which focuses on the enhancement of the investment climate, proceeds with key privatisation transactions and transitions to the new energy market model. As regards the investment climate, addressing constraints to FDI should lead to positive employment benefits both directly and indirectly in the SME sector. Further general reforms to address institutional constraints to firm entry/exit and labour flexibility are required, as outlined in the Selected Issues Paper. We support the authorities ongoing efforts in the area of SoE reform. We are surprised that the report is silent on the issues of climate change and gender equality – can staff clarify whether their analysis touched upon these important issues?

Mr. Mouminah, Mr. Alkhareif and Mr. Rawah submitted the following statement:

We thank staff for the well-focused reports and Mr. Psalidopoulos for his helpful buff statement. Over the past decade, Greece has made important progress in advancing its structural reform agenda amid a very difficult situation. Looking ahead, efforts to continue addressing past legacies and remaining challenges are important to boost growth prospects. We are in broad agreement with staff's analysis and policy recommendations and would limit our remarks to a few issues.

Continued improvement in the fiscal policy mix accompanied by a sustained public debt reduction is critical going forward. We take positive note of staff's assessment that Greece continues to outperform its fiscal target commitments to European partners. Furthermore, sentiments have improved, reflecting the notable reduction in Greek yields and credit spreads, and the successful new bond issuance at favorable terms. That said, fiscal policy mix should be recalibrated towards achieving more inclusive growth, including through meeting the much-needed investment and social spending. In this vein, we take note of the ongoing discussion between Greece and the EIs regarding a possible adjustment of the primary balance path over the medium-term. We also welcome the authorities' plan to cut the existing high direct tax rates while broadening the tax base, supported by further strengthening tax compliance. These reforms should proceed in conjunction with continued efforts to strengthen IAPR and mobilize AML framework to combat tax evasion. On spending efficiency, we join staff in urging the authorities to achieve further improvements in budget planning and implementation as well as address the structural causes of arrears, in line with past Fund TA recommendations.

Restoring the banking system's health should continue in order to improve financial sector resilience and boost its ability to support growth. In this context, we welcome the new government's emphasis on prioritizing the banking system clean up, including through the proposed state-supported scheme "Hercules" aimed at achieving a meaningful reduction in NPE ratio. We also agree on the importance of strengthening banks' loss-absorption capacity and note the need to further enhance profitability, governance and legal framework of the banking sector. At the same time, we look forward to further efforts to promote debt restructuring and payment discipline. On AML/CFT, we take positive note of the progress made on strengthening the framework, and we encourage the authorities to continue their efforts to address the remaining gaps.

Finally, accelerating structural reforms to support economic growth is important. In this context, we welcome the authorities' ongoing efforts toward streamlining business licensing, promoting privatization, strengthening competition, and deepening the labor market reforms. We also take positive note of the establishment of the National Transparency Authority and the ongoing efforts to strengthen the rule of law. We note the divergence of views between staff and the authorities, and therefore, would welcome a more constructive dialogue going forward.

With these remarks, we wish the authorities further success.

Mr. Trabinski and Mr. Tola submitted the following statement:

We thank staff for the comprehensive set of papers and Mr. Psalidopoulos for his informative buff statement. The Greek economy continuous to recover, though growth rates remain moderate. Given the overall favorable economic conditions, we see scope for addressing a number of obstacles to the medium and long-term growth prospects. This could include tackling unfavorable demographics, a high stock of NPLs and public debt as well as an impaired productive capacity of the economy, which is a legacy from the multi-year recession. Moreover, it is important that the accomplishments achieved during the program era are underpinned by further measures to bolster the investment and business climate. Against this background, we encourage the new government to maintain its firm commitment to pursue the structural reform agenda.

Fiscal policy needs to be recalibrated to support inclusive growth. On the revenue side, we welcome the authorities' plans to cut PIT and CIT rates. These measures should be accompanied by a broadening of the CIT tax base, which goes beyond the lowering of the tax-free threshold. At the same time, we are concerned that efforts to strengthen tax compliance are undermined by the systematic use of installment schemes that perpetuate the weak tax payment discipline. In this context, going back to a single "basic" installment scheme with strict eligibility criteria for viable debtors seems to be warranted. On the expenditure side, the subdued public investment is regrettable as it further limits the economic recovery. Also, it is key to address bottlenecks in budget execution and improve the coordination between the public investment framework and the ordinary budget. We would be interested in staff's view on whether the creation of an infrastructure fund integrated in the public investment framework could circumvent the coordination issues?

In addition, we agree with the measures proposed by staff to support higher and more inclusive growth, targeting population groups that are more likely to fall in poverty. In particular, we agree with staff that bringing the pension benefits of existing retirees in line with the new benefit formula would help create the necessary resources to finance social spending.

Restoring financial sector resilience and its ability to finance growth should remain a key priority. We welcome the authorities' efforts to restore the health of the banking system. At the same time, we take note that the process of reducing NPLs is taking place largely through write-offs and sales. While some progress has been achieved, we are concerned that the level of NPLs remains high and limits the ability of Greek banks to provide credit to the real economy. Thus, institutional, legal, and other structural bottlenecks, which are preventing a faster resolution of insolvency cases, should be addressed. In this context, we wonder how staff assesses the impact of the state's asset protection plan "Hercules" on NPL reduction?

The deterioration of the external sector position calls for additional measures to address the competitiveness and productivity gaps. Staff's external sector analysis shows that imbalances have primarily a structural nature and can be traced back to product and labor market rigidities, which had led to competitiveness and productivity gaps. Hence, structural reforms allowing for a fairer burden sharing of the structural transformation between labor and capital remain key. Also, there is a risk that the objective of greater labor market flexibility and full employment could remain out of reach without meaningful progress with product market reforms. Finally, more efforts should be dedicated to improving business climate, which is essential to attracting additional foreign financing.

The representative from the European Central Bank submitted the following statement:

We would like to thank Mr. Psalidopoulos for his informative buff statement, and Staff for their report, which we view as balanced. We broadly agree with Staff and share many of the main findings, in particular those related to risks facing the Greek economy and policy priorities ahead, and would like to highlight a few items.

We broadly agree with the assessment of the macroeconomic outlook for Greece and would like to highlight that this is predicated on continued reforms. Like Staff, we expect GDP growth in Greece to continue in 2020 at levels above potential, based on a strengthening in investments and improving labor market conditions. The implementation of the structural reform agenda that has been agreed between Greece and its European partners remains a critical element in sustaining and materializing such expectations. We agree that risks are tilted to the downside, reflecting in particular external factors (e.g. a synchronized global slowdown and Brexit).

We echo Staff's view that achieving the fiscal targets is important to sustain the credibility of the government's program, while also noting downward revisions in fiscal path projections by Staff. The fiscal overperformance recorded by Greece has helped investor confidence to return, as manifested by recent favorable bond issuance events. We agree with Staff that the measures adopted in May 2019 ran counter to reforms adopted under the ESM program in terms of targeting social spending and eliminating tax exemptions and welcome their partial reversal. We see some of the measures announced for 2020 as steps in the right direction to make public finances more growth friendly. However, we share Staff's concern regarding the narrowing of the tax base from the PIT reform and the negative effect of the extended temporary instalment scheme on tax compliance that can offset some of the broadening impact from increasing the prevalence of electronic transactions. At the same time, we note that, contrary to Staff, both the European Institutions and the authorities project that the primary surplus target for the 2020-2022 period will be met. The difference seems to stem from the different assessments of counter-measures and thus Staff's explanations could contribute to enhancing understanding of the underlying considerations, in particular in view of their implications for the debt sustainability analysis.

We note Staff's call for a lower primary balance target or of a smoothing mechanism to take into account cyclical or one-off shocks. We recall that the primary balance target was agreed with the Eurogroup, while taking into account the European fiscal rules and considering the implications for the debt sustainability analysis.

We welcome the progress made in reducing NPL but agree with Staff that significant further efforts on the side of banks and authorities are still needed to reduce stocks and enhance resilience. Despite sizable public support to banks, Greece remains an outlier in the EU in terms of NPL stock and low RoE on bank assets. Therefore, the momentum on sales and securitization of loans needs to be maintained and further reinforced, while banks also need to step up their efforts for ‘organic’ NPL reductions. We support recent encouraging announcements by the banks and the government pointing to a more ambitious stock reduction, and welcome the government’s new initiatives, including the Hercules securitization guarantee scheme, noting that promoting meaningful debt restructuring and payment discipline are key objectives going forward. These should include establishing a credible threat of foreclosure and the swift elimination of primary residence protection as a financial policy objective. We also strongly agree with Staff on the long-standing issue that a more effective judiciary is warranted and essential for the successful implementation of such strategy. Further, we also agree with Staff that Greek banks must enhance their business strategies, improve their governance and risk management to increase their internal capital generation capacity which, along with continued NPL reduction, would help raise fresh MREL-eligible capital and increase banks’ resilience.

We share Staff’s assessment that the structural adjustment needs facing the Greek economy are sizable, but also see some encouraging signs of action and intentions by the new government. With gross fixed capital formation at only half of its level in 2000, we particularly welcome the authorities’ overall policy objective to enhance the investment climate, proceed with key privatization transactions and transition to the new energy market model. While we agree with Staff’s recommendation to establish a real-time assessment capacity of current barriers to product markets and competition, we would also take positive note of the progress achieved so far in this area, such as in the business areas of pharmacies and lawyers. We note that the full implementation of several structural reforms has experienced delays, in part due to the snap elections that took place in July 2019. Renewed efforts are needed an, in that respect, we welcome some progress on a number of policy areas such as on the implementation of the investment licensing reform, forest mapping, the reduction of the time needed to register a new business and ongoing efforts to improve SOE governance. Finally, we also agree with staff that efforts need to be sustained to complete the privatization program – which has suffered considerable delays – and note the program’s positive impact on FDI inflows to Greece.

The Acting Chair (Mr. Zhang) made the following statement

Good morning, everyone. The subject of this session is Greece - 2019 Article IV Consultation. All of you issued gray statements. Thank you for that. The ECB representative also issued a statement.

As you know, the Greek economy continues to recover, although the growth rate is still lower than expected. In this context, the new government is committed to pursuing growth-friendly, inclusive policies and their early actions since they were elected, including implementing a number of measures in the fiscal and structural areas, which is a very good signal to start a new chapter. Nonetheless, as your gray statements highlighted, there are important remaining challenges to achieve more sustained growth through deeper reforms and with a stronger political resolve. I am sure later on we will discuss those issues which were highlighted in the staff report.

Another development I want to report to you is that this morning, we received a formal notification from the Greek authorities that they intend to prepay about one-third of the IMF loan, which is the amount of SDR 2.2 billion. Even with that, the remaining balance still ranks the fifth largest among our membership. That highlights the importance of our continued engagement with the Greek authorities. Of course, as you know, Greece remains in post-program monitoring (PPM).

Finally, I want to highlight that this Article IV consultation mission was successfully conducted together with staff from the European institutions, which conducted their fourth review mission and the European enhanced surveillance framework.

Mr. Rozan made the following statement:

I would like to start by thanking staff for the very interesting set of documents and Mr. Psalidopoulos for his useful buff statement. Allow me to touch upon some of the main issues that have come to light in the report.

First, we share staff's general assessment, that Greece's economic and financial normalization is on track; however, the sustainability of the recovery is not guaranteed, as the country remains vulnerable to shocks and macroeconomic imbalances. As delays in critical policy reforms since the end of the financial assistance program are potentially looming over Greece's recovery, we are really encouraged by the new government's willingness to improve the orientation of fiscal policy, while abiding by the previously agreed fiscal rules.

We note that staff calls for a lower primary balance target or a smoothing mechanism to take into account cyclical or one-off shocks. We recall that the primary balance target was agreed with the Eurogroup, while taking into account the European fiscal rules and considering the implications for the Debt Sustainability Analysis.

Taking into account this objective, the fiscal policy mix could be strengthened and rebalanced. We welcome the measures included in the 2020 draft budgetary plan to foster a more growth-friendly and inclusive tax policy, as referred to in Mr. Psalidopoulos' buff statement. We encourage the authorities to continue in this direction and re-orient spending toward high-quality investment and social spending. The composition of public finances and the design of an ambitious agenda for growth is key to boost socially inclusive growth while complying with the targets agreed with the Eurogroup.

On financial sector policies, we welcome the willingness and action from the new government to prioritize bank cleanup. In this regard, the implementation of the Hercules Asset Protection Scheme is encouraging. We agree with the authorities, that more aggressive reductions aiming to further reduce non-performing loans (NPLs) are warranted. We encourage them to proceed further to promote meaningful debt restructuring and payment discipline. We also believe that a more effective judiciary is essential.

Finally, the structural challenge that Greece faces is quite extensive, and we note that there has been some backtracking since the exit from the program. In this regard, we very much welcome the new government's pledge to enhance the investment climate, proceed with key privatizations, transition to the new energy market model, and remove impediments to product markets and competition. We support the authorities in their endeavors to fuel this momentum and achieve progress in key policy areas; among them, labor market flexibility, business deregulation, and state-owned enterprise (SOE) governance.

Finally, we strongly support the analysis done by staff on product market competition to ensure that the structural reforms can reach their full impact on the country's competitiveness.

Ms. Levonian made the following statement:

Let me begin by thanking staff for their comprehensive report and Mr. Psalidopoulos for his informative buff statement. We have issued a gray statement, so I can be very brief.

We wish to recognize the scale of the adjustment that has been undertaken by the Greek people throughout this very challenging period. We welcome the economic recovery. While vulnerabilities obviously remain, we note the progress made by the authorities, in particular, since the new government took office. The real challenge is to reinvigorate the momentum of reform. We encourage the authorities' endeavors toward a more growth-friendly and socially inclusive fiscal policy mix, and public financial management reforms are critical in this regard. The need for higher quality government spending, focused on investment that will help future growth, will be essential to improve long-term productivity and debt dynamics.

Finally, we welcome the draft budget plan 2020 provisions related to child care, which aim to increase labor force participation by females, as outlined in the buff statement.

With that, we wish the authorities well.

Mr. von Kleist made the following statement:

I would like to thank staff for the set of well-written reports and Mr. Psalidopoulos for his helpful buff statement. We have issued a gray statement, and we also associate ourselves with Mr. de Villeroché's statement. Therefore, I can be brief, with just two points.

We welcome the authorities' commitment to reinvigorate the structural reform agenda. One key challenge remains to improve the composition of the budget and to overcome the recurrent underspending on public investment. In addition, continued labor and product market reforms are critical to foster competitiveness and productivity. More broadly, a persistent momentum for structural reforms will remain essential to sustain growth in the face of downside risks to the outlook going forward.

Taking note of the remaining differences in the assessment of long-term debt sustainability between staff and the European institutions, we would like to reiterate that any long-term fiscal projections need to be underpinned by a compliance with European fiscal rules.

With this, we wish the authorities continued success in their future endeavors.

Ms. Pollard made the following statement:

Let me begin by noting that I am fascinated by the random pairings of chairs and speakers on the display in front of us. I cannot help but notice that the U.S. and China are paired together, which I hope is a sign of improving relations between our chairs.

With that, let me begin by thanking staff for the excellent set of papers and their answers to technical questions and to Mr. Psalidopoulos for his helpful buff statement.

I agree with Ms. Levonian in noting the progress that the Greek authorities have made over the past years. Mr. Psalidopoulos rightly reminds us of the high social and output costs that were incurred by the crisis. Where he is critical of staff is on the challenges. We also focus on the challenges facing the Greek authorities, and I would say that is the case because we see the enormous potential for the economy if these challenges can be addressed. With that said, let me just echo two points from our gray statement.

The first is on fiscal. Here, we underscore the importance of a growth-friendly policy mix and would caution against underspending on capital investments, as other chairs have said. We welcome the plan for business-friendly tax measures and efforts to broaden the tax base by adjusting the threshold for electronic transactions necessary for claiming a tax credit, which is referenced in Mr. Psalidopoulos' buff statement. We encourage the authorities to pursue measures to better control pensions and public wages to create space for high priority spending. We also encourage them to discuss with their European partners a possible lower fiscal surplus path to better support growth, as well as a fiscal smoothing mechanism.

Finally, on the banking sector, we remain concerned that more comprehensive and decisive steps are still needed to restore the banking sector to health. We appreciate the staff's answer to technical question No. 17 on the Hercules securitization scheme, which highlights that this effort moves in the right direction but is not sufficient, leaving banks still weighed down by non-performing exposures (NPEs) of about 30 percent. We encourage the authorities to consider employing a bad asset resolution entity that could more decisively improve bank balance sheets and promote the resumption of lending, which is critical to boost growth. We agree with staff, that the banking sector reform needs to rest on a firm legal foundation that promotes stronger payment discipline and meaningful debt restructuring.

Mr. Trabinski made the following statement:

We welcome the new government's commitment to broaden the tax base, improve the business environment, increase labor market flexibility, and boost investments. At the same time, we encourage the authorities to resume the reform course and to avoid further reversals of the adopted measures, such as the 2020 personal income tax (PIT) reform and the pre-electoral pension measures. Let me focus today on three specific points.

First, on fiscal policy mix, we welcome the overperformance of fiscal targets. However, we see scope for a further improvement of the quality of fiscal adjustment. Solid fiscal performance has helped Greece, among others, to achieve significantly lower borrowing costs; yet, as staff note, the growth-friendliness and inclusiveness of Greek tax policy still lags the euro area average. Getting the right expenditure mix will be important to sustain a strong primary balance in the medium term. In this context, realigning the pension benefit schemes to the new formula will help redirect spending toward growth-enhancing public investment and critical social needs.

Second, the structural nature of external sector imbalances points to the need to address labor and product market rigidities. Despite the improvements during the last decade, the real exchange rate overvaluation persists, pointing to higher production costs, relative to trading partners. The full implementation of developing bill measures should constitute a priority since they will tackle labor market rigidities and remove roadblocks to competition in the product market. The latter would lead to lower non-wage costs, which staff flag in the selected issues paper as the main factors responsible for the blunted impact of the wage cuts on prices.

Third, restoring the financial sector's resilience and enhancing its lending capacity should be a priority. This seems to be particularly important in the context of the slower pace of NPEs' reduction and negative credit growth, emphasized by staff in the report. Moreover, a further deterioration of bank balance sheets could threaten financial stability. We note that a process of reducing NPLs is taking place, largely through write-offs and sales, denting bank balance sheets. The process of NPEs' securitization would further help the financial sector clean up; but, as Mr. von Kleist noted in his gray statement, this could also transfer the risks to government finances in the less regulated secondary market. Hence, there is a need for a more comprehensive solution--in particular, tackling institutional and legal constraints to establish an efficient resolution framework, as was pointed out by Ms. Pollard.

Mr. Palei made the following statement:

I was also impressed by the performance of the electronic system. Somehow, I had a much darker view of what we have here. I was thinking about the Comprehensive Compensation and Benefits Review (CCBR) and the way we rely on the recently introduced new performance evaluation for staff. I hope it will work better than the system we have for the Board's communications here.

On the bright side, I noticed that we also cloned Mr. Ostros here. This is a big plus to our performance, which might increase productivity further and maybe mitigate the cost of some of the deficiencies.

Going back to Greece. First of all, I would like to thank staff for the set of good papers and also for the written responses to Directors' questions. I also found the frank comments by Mr. Psalidopoulos, about the views of his authorities, to be very useful because they highlight some of the remaining differences and views on the outlook and also on the evaluation of the past reforms.

The very low growth path and the very slow recovery of Greece is a huge puzzle, and I do not think it has been explained properly by now. I will make just a few comments on this situation.

First of all, I would like to refer to the chart provided by staff at the very beginning of the report, where we see the evolution of the GDP per capita in various crisis-affected countries. We see that the decline in GDP in Greece was comparable to the Great Depression in the United States and some of the other huge calamities. But many of those other economies, they did return to the pre-crisis peak relatively fast--and "fast" is also a relative term. Over a period of, say, 7, 10 years, most of the countries did return to the pre-crisis peak.

In this picture, we do not have the Baltic States. These are also very stark examples of how the GDP went down. In Latvia, it went down by almost the same amount, about 25 percent, and in other Baltic States; also, about 17 percent in Estonia. Then they came back to the pre-crisis peak.

Here, we have a country that went down by 25 percent, and it never came back in terms of economic recovery. This is puzzling for me. It suggests that before the crisis, for over a decade, the economy was functioning at an actual GDP level of about 30 percent higher than its potential. This is a very sustained and huge deviation from the growth trend. I do not think it has not been explained. I personally think that it bodes well for the views still held by some, that Greece does have much brighter economic prospects ahead of it and maybe the current situation is just a legacy of this very popular story about the country and how its economy functions, and maybe this story will change in the coming years. But, of course, that is speculation. And here, it probably pays off to be on the cautious side and to continue with the reforms and focus on the immediate, immediate tasks.

Another big factor here is the projections for the interest rates for the euro area; whether they normalize over the medium term or not also remains an open question. And maybe Greece is bound to converge to these rates over the medium term. It depends on the views of the quality of the European institutions, the euro area monetary fund that was created after the crisis, and certainly all the other institutional changes in the currency union.

Mr. Alkhareif made the following statement:

We join others in thanking staff for their comprehensive work and answers to Directors' questions. I thank Mr. Psalidopoulos for his extensive buff statement, which clearly highlights the positive, important progress made by the Greek authorities. I encourage the authorities to continue their efforts to improve the reform implementation and safeguard macroeconomic stability.

I noticed the first page of the report did not fully reflect the positive developments of Greece's economy. I would encourage staff to take this into account in future Article IV consultations.

On the fiscal front, like Ms. Levonian, we encourage the authorities to continue their focus on growth-enhancing capital spending to generate jobs and high-quality growth. We echo the points raised by Mr. Rosen, Ms. Pollard, and Ms. Crane in their gray statement on the usefulness to consider a lower fiscal surplus path going forward, in cooperation with other European countries, as well as to consider the fiscal smoothing mechanism to help unlock fiscal space for growth-enhancing measures.

We take note of the reform implementation on the fiscal front. We welcome the authorities' plan to cut the existing high direct taxes and broaden the tax base. We also support their efforts to strengthen tax compliance.

On spending efficiency, we join staff in encouraging the authorities to achieve further improvements in the budget planning.

On the banking sector, we welcome the new government’s emphasis on prioritizing the banking system cleaning up.

On Anti-Money Laundering and Combating the Financing of Terrorism (AML/CFT), we take positive note of the progress made on strengthening the framework.

Finally, we welcome the authorities’ ongoing efforts toward streamlining business licenses, promoting privatization, strengthening competition, and deepening the labor market reforms. We also take positive note of the establishment of the National Transparency Authority and the ongoing efforts to strengthen the rule of law.

With these remarks, we wish the authorities continued success.

Mr. Moreno made the following statement:

I thank staff for the report and Mr. Psalidopoulos for his reassuring buff statement in terms of the reform commitment of the authorities. I also associate myself with the statement made by Mr. de Villeroché. I would just like to make a few comments.

First, like Ms. Pollard and Ms. Levonian, I would also like to acknowledge and stress the efforts made by the Greek society and the Greek authorities in the past. I think we already did it in the first post-program monitoring last March. Like Mr. Psalidopoulos, I think the staff paper could have been more positive in this respect.

Second, on the fiscal adjustment, I would also like to echo that there is an important difference, both in the calculations of the primary surplus but also in the recommendations of the future path of the fiscal adjustment with the European institutions and with the authorities. Like Mr. Rosen and Mr. von Kleist, I would like to highlight that this is an agreement within the Eurogroup, and any changes should be done in accordance with the European fiscal rules.

A brief parenthesis to Mr. Palei. We are happy with the quality of the European institutions. Of course, there is always room for improvement. This is something that is being carried forward. We have a new commission starting in a few days--20 days from now.

Third, like other colleagues, together with growth-friendly policies, I would also highlight the importance of sustaining social expenditure in the budget. Annex V is concerning in terms of the loss of inclusive growth in Greece. By the way, this a very useful annex that I would like to see across the board in different countries. Given the new political cycle, I would ask the authorities to take advantage of the beginning of the new term not only to strengthen the reform agenda, but also to open a broad-based debate on social spending and how it can be better targeted, including the more complicated debates on pension and the public wage bill.

Fourth, I find that the staff approach on the minimum wage and collective bargaining could be enriched further. This is an ongoing debate in many countries, not only in Greece. Of course, we must pursue the objectives of competitiveness and flexibility, but these are not the only objectives. We have the labor market policies, which should also be assessed against--to ensure adequate levels of employment, wages, quality of the euro environment, and degree of adaptability. I think that this is not sufficiently captured in this report. Again, this is not only for the case of Greece, but this is an ongoing debate going forward. There are differences here between the IMF and other institutions and countries and even with the OECD. This is an area where more can be done.

Finally, we missed in the report a clear reference to the climate change strategy. I think that--taking advantage that the Strategy, Policy, and Review Department is here--this is something that should be standard or more taken into account in Article IV reports, in general.

Mr. Ostros made the following statement:

I thank staff for the good set of reports. I associate myself with the gray statement of Mr. de Villeroché and the intervention of Mr. Rozan this morning. I would also like to thank Mr. Psalidopoulos for his buff statement.

Like others, I would like to commend the authorities for reaching their fiscal targets in recent years. It has clearly impacted how actors view debt sustainability. It has gone in a positive direction, evidenced by the rapid reduction of credit spreads in the bond market.

I do think it is important to continue with this relatively tight fiscal policy. The hard-won gains, in terms of increasing investor confidence, should not be jeopardized by considering a short-run fiscal stimulus at this stage.

There is, of course, a need to boost investment and to strengthen social spending. I do think that the staff's answers to the technical questions show that there is substantial revenue potential from broadening the tax base. We especially appreciate the staff response to our technical question on the revenue effect of bringing informal activities in line with the EU average. The estimates of 2.5 percent of GDP from the VAT alone clearly shows that expenses aimed at strengthening growth and social inclusion can be financed, not to mention the need to also broaden the tax base when it comes to personal income taxes. So more important in the long run is to have a stronger revenue mobilization and a modernization of public expenditure. I would prefer that before a short-run fiscal stimulus.

Mr. Jin made the following statement:

I am surprised and excited to see that China and the U.S. and also China and Greece are in the same constituencies. This may be a technical mistake by a human being, but I think this may not be a mistake by God or by the Heaven, in Chinese. It may strongly indicate by God that these countries should work together and for a common goal. I believe this is not a dream; it will become a reality in the future--hopefully not a very remote future.

We thank staff for the well-written report and Mr. Psalidopoulos for the encouraging buff statement. We have issued a gray statement and let me make a few more comments.

The Greek authorities have made great progress in fiscal adjustment. It is true that this fiscal adjustment helped to put public debt on a downward trend and boost credibility; but if the adjustment is largely achieved by cutting much needed pro-growth capital spending, it will dampen economic growth. We noted the divergent views on whether Greece should have a lower fiscal balance target.

I can remember that several years ago, this Board was discussing whether this 3.5 percent surplus target could be achieved. The fact is, for the past two years, the Greek primary surplus actually exceeded this target, but at the expense of growth and social inclusion. In this regard, we encourage staff to do a cost-benefit analysis, providing us some guidance on how to pursue the fiscal adjustment without dampening economic growth.

Nevertheless, no matter what the fiscal target is, we strongly encourage the Greek authorities to improve their fiscal policy mix, to cut the tax rate while improving tax compliance, to shift expenditure from pensions and public wages to high quality investment and social spending to make it more growth-friendly and socially inclusive.

We particularly like the concept of growth friendly. We have joined the international community's efforts to support the Greek economy by making direct investment in infrastructure and promoting employment and trade in this country. We will continue to firmly support the Fund's effort to support the Greek economic recovery and the restructuring.

The staff representative from the European Department (Mr. Dohlman), in response to further questions and comments from Executive Directors, made the following additional statement[1]:

Thank you for the very interesting comments and the discussion here. I did not hear any questions, but I would like to address a couple of the points that were raised.

Several Directors mentioned the growth projections and the pace of the recovery, and the explanation for why it has perhaps been disappointing. We can point to a couple of factors and things that we have mentioned in the past.

One is the political consensus, or lack thereof, that existed during the peak of the crisis. In contrast to other euro area countries, Greece had a very significant turnover, frequent elections, the highest number of finance ministers, prime ministers, and so forth, among the crisis countries. So this issue of political consensus at a very difficult time is one factor.

Second is the demographics. It is well known that there has been a very significant outward emigration of young, well-educated Greeks, in the range of 500,000. This was a very significant decline. The European Commission's own Ageing Reports show a reduction by 2020 -- when you compare the 2012 Ageing Report with the 2018 Ageing Report, there was a reduction of about 20 percent of the projected workforce by 2020. This shows a very significant shift in the demographics for the worse.

[1] Prior to the Board meeting, SEC circulated the staff's additional responses by email. For information, these are included in an annex to these minutes.

I think it is also fair to say, as one of the Directors pointed out, that Greece started at a much worse situation. We have to remember that at the onset of the crisis, the current account deficit was about 15 percent of GDP. The overall fiscal deficit was about 15 percent of GDP as well. These are some of the factors. Also, the evolution of the European institutions was something that was raised by Directors.

Another issue that was raised was about the minimum wage and labor--we take note of those suggestions. There was a suggestion made to do more analyses on climate change. We do think this is a very important issue. It is important for Greece. Greece is taking this very seriously, from what we have seen in their own reports and from brief discussions in this area. That is something that we will look into for the next Article IV cycle. But there is a trade-off to be made in terms of priorities.

Let me just mention one more thing about the tone and the balance in the report. Did we get the balance right? Did we give enough credit to the authorities? Certainly, it is important to give credit where credit is due, and there has been progress. During its first four months, our sense is that, the new government has done some things on legislation andmade some important changes, but we also need to give it some more time. Let's see where we are by the time the second post-program monitoring cycle comes around in the second quarter of next year. We expect to be at the Board sometime in June. At that time, we are hopeful that we will be able to report that things are happening on the ground.

It is also important to remember that Greece is an outlier, a negative outlier in many ways in the euro area. We have mentioned them in the report. I would be happy to elaborate on that here now, if Directors wish to hear that. The main point is that we should be factual, have a fact-based analysis highlighting the main areas of risk and the difficulties and challenges to overcome to achieve higher socially inclusive growth, and then do our best to get traction. Here, we also have to continue working with our partners in the European institutions. We have a good dialogue, both with the institutions and the authorities, including through our technical assistance program, which is heavily focused on revenue generation, revenue compliance.

Mr. Palei made the following statement:

Thank you very much for the responses to some of the issues I have raised and other Directors have raised.

> This notion of the labor force declining by 20 percent, this is the first time I have heard that. Maybe in future reports, it could be explored a little bit more. But even if it is that large--which I am not sure about--we can recall the experience of the Baltic States. They also experienced a huge outflow of the labor force; and still, they came back very fast and exceeded the pre-crisis peak. So there are still some things to address and explore and maybe think about in terms of the speed of recovery and what the reasons are.

The Acting Chair (Mr. Zhang) - Are there any further comments? Mr. Dohlman, if you would like to quickly address the labor force.

The staff representative from the European Department (Mr. Dohlman), in response to further questions and comments from Executive Directors, made the following additional statement:

> On the last point made, what I hear here is that there is more appetite for perhaps another look at the underpinnings of the long-term growth rates and the pace of recovery, the reasons for that recovery. That is something we would suggest that we pursue in the context of the next Article IV cycle, the PPM being more of a risk-based assessment cycle. We will take that onboard. Thank you.

Mr. Psalidopoulos made the following concluding statement:

> Thank you, Chair. On behalf of my authorities, I would like to thank staff for the hard work and for the productive and frank exchange of views since the Article IV mission back in September. I also thank Directors for their gray statements and for their comments this morning. Their messages will all be conveyed in Athens and will receive due consideration.
>
> Fifteen months ago, Greece officially concluded its last financial assistance program by the European Stability Mechanism (ESM). The economic adjustment has eliminated fiscal deficits, reduced the current account imbalance, and increased flexibility in the real economy. Exports continue increasing, and industrial production is in expansionary territory. Unemployment has dropped by 10 percentage points, and the real estate market prices have started recovering. The Economic Sentiment Indicator has reached a 12-year high, and consumer confidence has picked up over the last three months, standing close to a 20-year high.

Financial indicators in the first three-quarters of 2019 improved remarkably. Greek sovereign and corporate bond yields declined after September 2019 to historically low levels. The Greek authorities have committed to complete the key structural reforms initiated under the ESM program, relating not only to fiscal outcomes but also to the areas of social welfare, financial stability, labor and product markets' privatizations, and public administration. Public debt is on track. Risks may arise after 2032, but the Eurogroup has committed to review the situation then with the Greek authorities and will decide whether additional debt relief measures are needed. Governance and transparency have been declared key priorities of the Greek authorities.

So, what are the challenges moving forward? First, to continue to improve market access. Second, to reduce the high stock of nonperforming loans. Third, to step up the pace of the privatization and the reform programs. Fourth, to change the fiscal mix. Five, to accelerate the rebalancing of the economy toward a new growth model.

Looking forward, developments in the global economy and financial markets will set the stage for Greece in the midterm. Against the backdrop of global growth, the Greek economy is expected to continue a growth trajectory, growing by 1.9 percent in 2019. GDP growth is projected for the next couple of years to be about 2 percent.

The Greek authorities understand that this growth rate disappoints some observers. Ideally, a steep recession must, according to many--including Mr. Palei--be followed by a huge rebound in growth. In real life, however, big and extended recessions, like the one Greece has gone through, shape household and business expectations, as well as investment decisions in a very negative way. Rereading John Maynard Keynes will reveal very modern things.

Admittedly, economic policy can reverse negative trends. My authorities undertook continuous efforts to heal the economy from the wounds inflicted by the recession. These efforts are ongoing. We need to understand these changes in economic policy, that they are not conducted in a laboratory, and the subjects of new policy mixes after a crisis are free agents and society.

The recent civil unrest all over the world currently underlines the importance of moving with economic policy reform cautiously in order not to provoke civic unrest that would endanger the longevity of reform outcomes. I plead, therefore, in favor of looking at the glass of Greece currently as half full, rather than as half empty. Looking at it this way would also better honor the joint efforts of all parties involved in the Greek bailout since 2010.

Growth at an accelerated pace will be forthcoming, as ownership of reforms, confidence, and trust continue strengthening. Cautious moves, instead of big uncertain leaps, are key for long-term success. The country is moving forward. It has concrete policies and plans of its own. It counts on the assistance and advice of the European institutions and the Fund, and will be adjusting the policy mix going forward in a way that honors international obligations and the long-term interests of Greek, European, and global economic stability.

The Acting Chair (Mr. Zhang) noted that Greece is an Article VIII member, and no decision is proposed.

The following summing up was issued:

Executive Directors agreed with the thrust of the staff appraisal. They recognized the progress that the authorities had made in implementing reforms during the program period, as well as the Greek economy's continued recovery, but noted that important challenges remain. In this context, they took positive note of the new government's commitment to pursue growth-friendly and inclusive policies and welcomed their early policy actions. They stressed, however, that sustained and deeper reform implementation, deploying a full range of policy tools, and strong political resolve to tackle vested interests will be necessary to meaningfully boost investment, growth, and social inclusion.

Directors supported the authorities' plans to cut direct tax rates and urged more ambitious efforts to broaden tax bases and enhance tax payment compliance. They urged a shift of spending priorities toward more investment and targeted social spending, while strengthening fiscal risk management and contingency planning. A number of Directors considered that the authorities should build a consensus with European partners around a lower primary balance target to support the growth objectives. A number of other Directors, however, stressed keeping the target, which they noted was agreed taking into account European fiscal rules and the implications for Greece's debt sustainability.

Directors emphasized the importance of restoring the financial sector's resilience and ability to support growth. In this regard, they welcomed the government's more ambitious nonperforming exposure (NPE) reduction objectives, noting that the proposed state-supported NPE securitization guarantee scheme could provide important backing. However, Directors stressed the importance of taking a more comprehensive, ambitious, and well-coordinated strategy to clean up bank balance sheets, relying on market-based mechanisms (with any public support subject to cost-effectiveness assessments). These efforts should also include further improvements in the legal financial framework, including, in particular, an overhaul of the personal insolvency law to eliminate primary mortgage protection in order to strengthen payment discipline.

Directors underscored that Greece's success within the currency union will require policies to help boost productivity and narrow its competitiveness gap. In this context, they welcomed the government's efforts to unblock privatization, implement business deregulation, and restore elements of the cornerstone program-era labor market reforms. Directors stressed that realization of benefits from labor market reform would require meaningful parallel progress with other structural reforms, particularly further liberalization of product markets.

Directors noted the importance of continued improvements in public sector efficiency and governance. They welcomed the recent progress in strengthening the AML/CFT regime and anti-corruption institutions but underscored that important remaining shortcomings should be addressed. Specifically, they urged the authorities to strengthen public revenue administration (including strengthening tax enforcement), enhance the efficiency and quality of the judicial system (including enforcement of contracts), and speed up anti-corruption reforms.

It is expected that the next Article IV consultation with Greece will be held on the standard 12-month cycle.

APPROVAL: October 1, 2021

CEDA OGADA
Secretary

Annex

The staff circulated the following written answers, in response to technical and factual questions from Executive Directors, prior to the Executive Board meeting:

Outlook/Risks

1. ***We would like to have further elaboration on differences between the staff and the Greek authorities on economic outlooks.***

- As elaborated in paragraph 12 and Box 1 of Staff Report, the authorities anticipate stronger impacts on productivity growth and labor supply (e.g., immigration of skilled labor) of recently legislated reforms—including tax cuts, unblocking privatizations, business deregulation, and improved labor market flexibility—than staff projections. Staff assess the reforms are a positive step in the right direction, which is reflected in upside risks that could raise potential growth above the currently projected level (0.9 percent), but that much of the needed structural transformation lies ahead (and must overcome vested interests), and crisis legacies will act as a drag on growth until addressed. The staff report points to other factors as well.

2. ***Could staff elaborate on the outlook for the external position, its change from the earlier assessment, and the respective roles of data revisions, structural reforms and fiscal policy in this context?***

- Staff's current assessment is that the external position of Greece (in 2018) was weaker than consistent with medium-term fundamentals and desirable policies (see SR and Annex II), pointing to a competitiveness gap. This changed assessment is a downgrade from the 2018 Article IV assessment, which reflects several developments: a historical current account revision in late 2018 (see the March PPM Report paragraph 4 and Table 2), the impact of developments since 1H2018 (including the broad-based retreat of earlier reforms discussed in the staff report), and staff's further analysis on the drivers of the current account adjustment and Greece's cyclical position. Other indicators (e.g., Figures 4 and 7) and supporting analysis also show that Greece's competitiveness gap vis-à-vis peers is substantial. Figure 7 and the SIP suggest that Greece's external adjustment during 2009-2013 was largely driven by 'cyclical' factors, including import compression that is linked to contraction of consumption and investment. Staff project that import demand will continue recent robust growth as Greece's output gap closes (2023). The projected decline of the primary balance over the medium term also contributes to the weaker medium-term external balance path.

3. ***Could staff elaborate on what outcomes might be expected for key macroeconomic variables, especially growth, unemployment, inflation and the debt-to-GDP ratio, if the ECB were to take further action to bring inflation to target at a conventional 18-24 month horizon?***

- The question appears to point to a lower-for-longer (interest rate) path. While the underlying circumstances would matter, staff can point to some possible implications. It would support lower sovereign borrowing costs for longer, but the immediate benefits to public debt sustainability would not be prominent given the large share of fixed rate public debt in Greece. Financing costs for the private sector would likely be kept at lower levels, which could support investment, but a more binding constraint to a vibrant investment recovery is the weak investment climate (which will require deep and comprehensive structural reforms to address).

Fiscal Policy and Social Welfare

4. ***The difference in the near-term fiscal projections seems to stem from the different assessments of counter measures, and both the European Institutions and the authorities project higher primary balances for the 2020-2022 than staff project. Staff comments are welcome.***

- The 2020 draft budget assumes additional revenue collections via several administrative actions, including notably the electronic transaction (reporting) requirement for personal income tax purposes (to be eligible for tax credit), delayed tax prepayments for corporates, and faster processing of tax cases in administrative courts. While staff acknowledge upside risks from several of these measures, it projects weaker revenue gains than assumptions of the authorities and the European Institutions, given their uncertain nature.
- Staff's medium-term fiscal projections are based on staff's 2020 assessment, the last medium-term fiscal strategy received from the authorities, the revenue effect of GDP composition changes toward investment, the fading-out of the one-off measures introduced in the 2020 budget, and declining EU transfers.

5. ***In staff's assessment, what would be the revenue effect of bringing informal activities in line with the EU average?***

- Reducing informal activities through strengthening tax compliance would help boost revenue. For example, with respect to the VAT, staff estimates, drawing on the latest EU study on the VAT gap, that bringing the VAT compliance gap in line with the EU average would increase VAT revenues by about 2.5 percent of GDP in 2018.

6. ***While the authorities committed to a primary surplus of 3.5 percent of GDP for 2020, they also welcomed staff's support for a lower primary balance target. Can staff elaborate more on the feasibility of the current primary balance target?***

- Staff's fiscal baseline projections assume the full execution of the budget expenditure and realistic yields from administrative measures set to be introduced for 2020. Staff is of the view that the 3.5 percent of GDP primary surplus target for 2020 is within reach, but this would require materialization of upside risks to revenue and/or growth-dampening under-execution of the budget, notably investment.

7. ***Has staff discussed the possibility of a smoothing mechanism with European Institutions?***

- Yes. Staff suggested a smoothing mechanism with the EIs during the time of the first PPM cycle, both bilaterally and in meetings together with the authorities. During the 2019 Article IV cycle, staff again shared the potential benefits of a smoothing mechanism with both the EIs and new government. Such a mechanism would allow temporary, symmetric deviations from the primary balance target in the event of cyclical or one-off shocks (other than policy slippages), and, importantly, remove strong incentives for overperforming (to provide a cushion, given the 'penalty' for small misses).

8. ***Could staff comment on the difference in views regarding pension cuts and lowering of personal income tax-free thresholds?***

- Staff recommend rebalancing fiscal policies to boost sustained growth and social inclusion. In this regard, eliminating pension bonuses, bringing the benefit of existing retirees in line with the new benefit formula, and lowering the PIT tax-free threshold to broaden the tax base would create fiscal space for high quality investment, social spending, and further tax rate cuts. In contrast, while the authorities agree on the importance of fiscal rebalancing (including tax rate cuts), they expect their fiscal policy objectives to be achieved without pension cuts or lowering the personal income tax-free thresholds.

9. ***Could staff indicate how likely it is for Europe to amend Greece's fiscal commitments under the enhanced surveillance framework and agree to a primary surplus target lower than the 3.5 percent of GDP in 2020-22?***

- This question would be best addressed to Greece's European partners. However, our understanding is that there are no planned changes to the target for 2020, and that any request for future modifications will not be discussed until next year (in part to see how government policies unfold). One issue for discussion is the treatment of

ANFA/SMP profits, and whether its use for investment spending would alter its budget treatment under Enhanced Surveillance (see the June 2018 Eurogroup statement language).

10. ***How does staff assess the authorities' plans to improve their fiscal policy mix by allocating two thirds of any additional fiscal space to tax reductions and the rest to targeted social and investment spending?***

- Contingent on fiscal space, staff support reductions in direct tax rates and reorienting expenditure towards high quality investment and social spending, which would boost Greece's growth potential and social inclusion. As to the exact mix, this would be best assessed in the context of a more complete review of the budget, but staff views higher well-targeted social spending as a high priority.

11. ***The current draft budgetary plan 2020 already includes several discretionary measures to foster social protection. Staff's views are welcome. Which measures should be prioritized or included to foster a more inclusive growth?***

- The 2020 draft budget includes several measures that have implications on social protection, notably the Childbirth benefit, increases in the PIT tax-free threshold for children and the VAT cut for childcare items. In staff's views, social objectives would be better achieved through well-targeted social assistance programs. More resources could be allocated to the Social Solidarity Income, housing benefits, and ALMPs—with areas such as health (and education) also in need of more resources.

12. ***Could staff clarify the chances that the request for a lower PB target and a smoothing mechanism could be accepted by the Euro area partners? Are there precedents for such?***

- In setting fiscal targets, the adjustment of one-off and cyclical shocks is a common practice. Under the preventive arm of the Stability and Growth pact (SGP), all EU countries have medium-term budgetary objectives (MTOs) defined in structural terms. Similar to what the smoothing mechanism would imply, the MTOs also adjust the headline balance for cyclical or one-off shocks (other than policy slippages). As to the likelihood of changes, this question would be best addressed to Greece's European partners.

13. ***We would be interested in staff's view on whether the creation of an infrastructure fund integrated in the public investment framework could circumvent the coordination issues?***

- Staff's view is that improved coordination for public investment could be best achieved with continuing efforts to strengthen public financial management and the budget framework. The authorities have already designed an action plan to this end, which includes capacity development in public investment planning, implementation and monitoring, and enhanced coordination between the Ministry of Development and Ministry of Finance. Staff will continue to offer TA in support of these efforts.

Debt Sustainability Analysis and Debt Relief

14. ***We take note of the divergent views between staff and the authorities on public debt sustainability. Can staff comment on the authorities' debt projections mentioned in the buff statement? Can staff address the concern raised in the buff that they did not consider the reduction in Greek bond yields and credit spreads over the past eighteen months in their analysis? Could staff explain why the Greek debt is considered less sustainable in the long term against the background of both lower risk-free rates and lower Greek risk premium? According to Mr. Psalidopoulos's Statement, staff's last report rated public debt as more sustainable, while the current report flags it as less sustainable in the long term. Can staff elaborate on the change in assessment? Could staff expand on the nature of the differences between the authorities and their assumptions regarding the long-term fiscal and growth projections?***

- There is broad agreement on the starting point (current debt, adjusted for the stock of deferred interest) and the broad assessment of medium-term debt sustainability, as reported in the staff report (para. 12). The difference lies in the characterization of long-term debt sustainability outlook.
- The differences in near- and medium-term interest payment projections can be attributed to different accounting treatments of deferred interest and the assumptions on future interest rates. On the latter, staff has lowered the near to medium-term interest rate assumptions in the current DSA, reflecting recent market developments, and projections for the risk-free rate. However, the immediate benefits of lower interest rates are not prominent because a large share of Greece's public debt currently has fixed rates. Note that the near-term interest payments are inflated somewhat by the upfront costs related to GLF interest rate swaps.
- Staff has incorporated lower borrowing costs in the DSA over the next decade but remains cautious about longer run interest rates given the gradual shift from official sector financing to private sector financing (where borrowing rates are projected to rise due to the expected normalization of the risk free rate, combined with the projected risk premium path). There are also other offsetting medium-term factors, namely lower primary surpluses (on cash basis for 2019-25) and a lower growth path compared to the previous DSA. These factors underpin staff's assessment that long-term public debt sustainability is not assured under a realistic set of macro-fiscal assumptions (see below), despite the more favorable medium-term rate outlook.

- The authorities' baseline long-term macro-fiscal assumptions are more optimistic. The authorities project a higher long-term real growth rate (in the range of 1.5 percent), anchored in higher productivity growth, and assume a higher long-run primary balance (averaging 2.2 percent of GDP) consistent with their European partners under the debt relief agreement. In contrast, staff's long-run real growth projection is just under 1 percent, reflecting adverse demographics and historically weak productivity growth. Staff's long-term primary balance projection of 1.5 percent of GDP is a level assessed as consistent with social and development needs facing Greece. For further details on these assumptions, see the 2018 AIV staff report (Annexes V and VI).

15. ***Could staff advice on the DSA's impact of a lower primary balance path?***

- The net impact depends on how the fiscal space is used. Lower primary surpluses over the projection period would by itself add more to public debt and GFNs. However, if the additional fiscal space from a lower primary balance path is used in a growth-friendly and socially-inclusive manner, it would improve GDP growth and social outcomes. For a technical illustration of the DSA impact of a change in the primary balance path alone, please see paragraph 8 of Annex III.

Financial Sector

16. ***Can staff elaborate more on the market reaction and primary impacts of the CFMs removal?***

- No major reactions have been observed since their removal in early September. The (monthly and weekly) rolling averages of daily cash outflows have remained at normal levels; the cash in circulation continued decreasing; and the level of deposits has remained stable. Nonetheless, the latest data available (as of end-September) points to slight changes in depositors' breakdown, with a decline of corporate deposits (by 6 percent) more than offset by an increase of government deposits (by 26 percent). The removal of CFM measures has contributed to the upgrading by S&P of the sovereign and the major Greek banks, which should help support a return to confidence. The removal took place despite unmet conditions in the 'conditions-based' liberalization roadmap (and removed a safety net in the event of financial instability).

17. ***The 'Hercules' securitization scheme has been deemed by some observers as too timid to make a difference considering the state of the Greek banking system. Staff comments would be welcome. In this context, we wonder how staff assesses the impact of the state's asset protection plan "Hercules" on NPL reduction? Staff may***

like to elaborate on the fiscal impact of proposed asset management company involving government support*?*

- The 'Hercules" securitization scheme is a potentially significant step towards the clean-up of NPEs in the banking system, but its likely uptake is still uncertain. Even with full implementation, it would still leave the average NPE rate in the range of 30 percent, i.e. significantly lagging the EU rate (tenfold higher). Moreover, it will impact future bank profitability (due to the remuneration of the state guarantee at market conditions). Finally, it does not address the legacy of DTCs, which affect the quality of capital.
- As to the fiscal impact, the government has announced that it would provide up to €9 billion in guarantees for the senior (less risky) tranches and will receive market-based fees in return. But additional details are needed to provide a comprehensive fiscal assessment of 'Hercules' fiscal impact that includes expected government revenues, the risk that some of the senior tranches may be called (resulting in fiscal outlays), and a stress test scenario to evaluate tail risks. These details will likely be available once the government proposes legislation to the parliament, and when (i) the risk profile of the assets underlying the securitization tranches, and (ii) the sizing of these tranches is known.

18. ***Could staff elaborate further on the details, particularly the prioritization of the financial sector reform agenda, and whether the authorities have the capacity to develop and implement such a strategy? And how likely would the authorities succeed in garnering market-based private efforts? Can staff elaborate on who would design and lead a comprehensive banking sector strategy, and the main stakeholders involved?***

- The authorities have the capacity to craft and implement such a strategy by bringing together key domestic players (e.g., BoG, HFSF, banks, HBA, Finance Ministry, Justice) and stronger coordination with relevant European counterparts (not least the SSM). The proposed reform agenda for the banking sector can be summarized as focusing on three pillars (supported by the recommendations discussed in the staff report). First, banks should clean up legacies of the crisis by accelerating the reduction of NPEs and by enhancing the quality of capital. In this respect, 'Hercules' is a good step towards accelerating NPE reduction but not enough. Most importantly, the cost effectiveness of the NPE clean-up alternatives needs to be assessed both for banks and the government. Second, supervisors and the authorities should ask banks to enhance their liquidity profiles. Third, banks need to ensure their business viability by enhancing their business models to promote new business with a sustainable risk-adjusted return, and by strengthening their internal governance. The three pillars should lay on a solid legal foundation that promotes meaningful debt restructuring and payment discipline. In this respect, addressing primary mortgage protection is key and issues with the court system will need to be addressed for any reform to be meaningful. Ultimately, banks will be central players in successful implementation of any agenda.

Labor Market and Structural Reforms

19. ***Can staff comment on the status of the new Development Bill? To what extent are the priorities identified in the staff report addressed by the recently passed Omnibus Development Law? Could staff indicate if the authorities are ready to go further and fully restore the 2011-13 landmark labor reforms?***

- The Development Bill was voted on October 24 (effective from October 30^{th}). The legislation includes various structural policy measures to improve labor market flexibility, tackle roadblocks to competition and investment licensing, and unblock privatization. The immediate priority is full implementation of the legislated reforms (which may face vested interests). As to possible further steps in labor market policy, staff understand that the authorities' policy objective is to strike a balance between strengthening competitiveness and protecting employee rights, including by introducing new measures in line with ILO best practices, which does not necessarily require the full restoration of the earlier reforms.

20. ***Given the recent labor market policy reversals and difficulties with implementing labor reforms in the backdrop of social perception that workers have borne the brunt of adjustment, productivity-enhancing measures would be needed to maintain improve competitiveness. Staff may like to comment on whether authorities are contemplating some specific steps in this regard.***

- The authorities indicate that the Development Bill will help improve productivity and competitiveness via higher investment. Other reforms that the authorities plan to support competitiveness include governance reform and privatization of network industries (water, electricity, roads), export promotion and trade facilitation measures that address non-price competitive, and education reforms, particularly of higher education. In addition, the authorities are extending their collaboration with World Bank for the continuation of reforms, including investment licensing, assessment of the methodology and the level of minimum wage increases, ALMP pilots, and the National Cadaster.

21. ***We noticed that recent wage hike in some other European countries also only partly pass through to the retail prices. Can staff shed a light on why firms are reluctant to adjust their pricing no matter whether the wage cost increases or decreases?***

- Recent analytical work by EUR (see Regional Economic Outlook, Chapter 2: Wage Growth and Inflation in Europe: A Puzzle?) finds a general tendency of lower pass-through from labor costs to consumer prices during periods of subdued inflation expectations, greater competitive pressures, and robust corporate profitability.
- The Selected Issues Paper on Greece suggests that the impact of earlier minimum wage cuts on prices in Greece (in 2012) was partly offset by higher taxes (including on labor), higher capital costs, and increased mark-ups (due to lack of sufficient competition).

22. ***We would welcome further information on the ALMP pilot to support employability and skill-matching.***

- Employment services in Greece are provided through the Manpower Employment Organization, which is responsible for ALMPs, vocational training, unemployment and social benefits. About 6 percent of the unemployed are registered in some labor market programs, which include some public works programs, government-subsidized short-term internships, and government-subsidized posts in selected (crisis-affected) sectors. The authorities are planning an improvement of the existing services by ensuring more continuous delivery of the programs, strengthening individual counseling, and better mapping of labor market needs. The pilot of this new ALMP approach started in June 2018 (covering three municipalities), with the first assessment of the pilot expected by end-November 2019. The aim is to expand the new system gradually to the entire country.

23. ***Given our reservations on the use of perception-based indicators, which are sometimes slow to adjust to realities, we would like to see evidence from other EAs who witnessed significant shift in their rankings following recent reforms.***

- The Perception Survey and Ratings chart is to underscore the broad scope of the challenges that Greece faces; and Staff expect successful reforms could potentially help improve investors' perception on Greece.

24. ***Could staff comment on whether the estimates of reform payoffs of lower direct taxes and higher investment are conditional on product and labor market reforms? Could staff provide more details on the downward revision of long-term potential growth estimates compared to last year's assessment?***

- As noted in the staff report, Greece's prospects for sustained high growth and improved social outcome will depend on implementing a critical mass of inter-related fiscal, financial and structural policy reforms. In this regard, the realization of benefits from recent policy actions—including to lower taxes, enhance labor market flexibility, and liberalize business regulations—would require not only some time to produce results, but also meaningful progress in other policy areas (and likely other adjustments along the way).

- Staff revised down Greece's long-run potential growth projections from 1 percent (the 2018 Article IV and the 1st PPM in early 2019) to 0.9 percent, reflecting the broad-based retreat of earlier reforms and other factors. However, staff also noted upside risks that effective implementation of structural reforms that the new government committed to could raise potential growth above the currently projected level.

25. *Have the Greek authorities presented a timeline for the upcoming structural reforms? Could staff identify possible political challenges for the new administration in following the reform agenda?*

- The staff report includes the key elements of plans discussed during the AIV consultation discussions. We understand that the authorities are continuing to refine and adjust their plans (including in the context of their discussions with European partners in the context of the ongoing 4th Enhanced Surveillance review, which includes a number of actions against commitments outlined in the June 2018 Eurogroup statement on Greece) and are aiming to produce an updated growth strategy in the coming months. As to challenges, staff have highlighted risks that vested interests will slow reform efforts.

26. *Could staff elaborate on the impact of the policy reversals? Furthermore, what lessons can be drawn from such developments in terms of the IMF engagement and policy recommendations to member countries, especially in times of crisis?*

- Staff lowered Greece's long-term growth projections by 0.1 percentage point, reflecting broad-based retreat of earlier reform policies ahead of the July 2019 elections. The broad-based policy reversals after the program exit reiterates the importance of policy ownership and social consensus on essential reforms.

27. *We are surprised that the report is silent on the issues of climate change and gender equality – can staff clarify whether their analysis touched upon these important issues?*

- Staff recommended steps to boost female labor participation (paragraph 23 of the staff report). Policy discussions also included the authorities' plans to encourage development of renewable energy, which helps address climate change (paragraph 32). Greece will deliver a National Energy and Climate Plan (NECP) at the end of this year, which will include a strategy for exit from lignite (brown coal) plants and a comprehensive strategy to improve the energy mix by boosting investment in solar and wind sources. The BoG has also been active in studying climate change. Staff is currently considering whether and how to do a deeper assessment in these areas in the context of the 2020 AIV consultation cycle (but will consult further with the authorities, and also weigh this against other priorities).

Public Sector Transparency and Governance

28. ***We would appreciate if staff could elaborate more on how to improve the rule of law and data transparency in addition to the issues in the report.***

- The focus of the discussions was on those aspects of the rule of law that relate to the protection of property and contractual rights, including the predictability and timeliness of the enforcement of those rights. Fund staff found that although the authorities have made progress in this area, challenges related to the efficiency and quality of the judicial system remain. The authorities need to speed up judicial reforms aimed at enhancing overall effectiveness. Despite recent improvements, the time to reach a court decision is often too long and backlogs will require further targeted action. Special attention should be given to producing reliable court statistics based on standardized collection, processing and presentation methods, including the roll-out of integrated electronic case management systems in courts and judicial statistics that the authorities have initiated recently. With respect to the protection of property rights, steady progress towards completion of the national cadaster is needed.