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Directions for Economic Recovery in Greece

Introductory note

We are witnessing the longest recession in modern western history. The Greek economy suffers from an inefficient and unproductive public sector and a distorted financial model which was based on consumption funded by the public sector. The country's exit from the Eurozone may have been prevented but the government debt remains high. The markets are now anticipating the recovery of the Greek economy, realising, at the same time, that the instability of the institutional framework, the lack of will to proceed with the necessary reforms as well as the delay in changes pose significant obstacles and risks to the economic growth. Changing the economic model and attracting new capital in the market will only be achieved through a strategic shift from "Debt Containment" to "Growth" and from "Public Consumption" to "Private Investments".

Until now, most approaches were either focused on describing the problem or have addressed the problem at a general strategic level. Based on the knowledge of its professionals and accumulated experience from a broad corporate clientele coming from different industries of the Greek economy and the public sector, PwC presents practical guidelines and simple actions that can help Greece overcome this crisis and put the economy in a path for stable and sustainable growth.

Our proposal is structured on four pillars:

- Economic recovery requires investments
- Investment is dependent on trust by the markets
- The limited capital which Greece can attract must be directed to strategic sectors that will support the new economic model, leading to a virtuous circle of growth for the rest of the economic sectors as well.
- Rebuilding trust requires significant institutional reforms

Our proposal may be simple, yet it is brave. We hope that it can contribute to the formulation of an effective national strategy.

Marios Psaltis
CEO
PwC Greece

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Summary

Greece has overcome the risk of exiting Eurozone but the recovery remains fragile. We are witnessing the longest recession of modern history, longer than the American one in 1929. GDP has decreased by 25 p.p. compared to 2008 and unemployment rate has reached a high of 27%.

While government debt is 157% of GDP, Greece, is not over indebted compared to the countries that are under Troika's supervision. Total private and government debt does not exceed 286% of GDP, while Ireland's is 423%, Cyprus's 386% and Portugal's 348%. It is clearly the Greek public sector, that holds the country back and prevents growth.

Currently, the indications are positive. The primary deficit has been reduced to zero. The total deficit is falling rapidly and GDP has been decreasing at a slower rate compared to 2010-2012. Even the government debt is not as discouraging as it seems. 71% is in the hands of our institutional creditors (IMF, Eurozone member states, EFSF, ECB) with the average annual borrowing cost amounting to approximately 2%. The current value of the total Greek government debt, discounted by the interest rate at which Italy and Spain borrow from the markets, is €167 bn. compared to €340 bn. which is its nominal value. Greek bonds' yields, with Greek bonds representing 18% of the government debt, have fallen under 10% following the successful implementation of PSI and the Mario Draghi's pledge in July 2012. Nonetheless, this level is approximately 6 p.p. higher than the yields earned by Italy/Spain/Ireland and 3 p.p. lower than Portugal.

In practical terms, this difference reflects markets' lack of confidence in Greece. The deficit becomes more clear if one compares the interest rates of bonds issued by Greek companies established in Greece (e.g. Titan, Hellenic Petroleum, OTE) and the ones issued by Greek companies established in other European countries (e.g. Coca-Cola HBC). The corporate bonds of the former are negotiated at prices returning an average yield of 6%, while corporate bonds of Coca-Cola HBC have a yield of 2,4%. It is worth noting that markets have more confidence in Greek companies rather than the state itself. The lack of confidence reflects the views of foreign investors regarding the country's failure to implement essential reforms and the political system's inability to comprehend and address the real problems. The lack of confidence in Greece does not only result in more expensive capital for Greek companies, compared to their foreign competitors. It also means that in order to obtain funds for a new investment in Greece, the new business venture must promise an expected return of 5 points higher than that of an investment in any other European country.

The lack of confidence in Greece creates the obstacle of 5% that prevents investments and growth. The investments needed so that the Greek economy gets back on track and flourishes are estimated at 20% of GDP annually, while today they are 13.5%. The difference of 6-7 p.p. equals to €12 bn more investments per year and fills the gap between recession and growth.

In order to obtain the necessary capital we must earn the long-term trust of markets and investors. This requires substantial structural reforms. The institutional environment regulating people's lives and behaviours, and consequently the economic dynamics of the country, has been totally eroded. We need a new reference framework that can provide the necessary incentives and disincentives for a different approach to life, in order to encourage:

- **Investors** to invest their capital in Greece
- **Entrepreneurs** to expand their businesses and become more competitive
- **Civil servants** to have their work driven by outcomes
- **Citizens** to respect and abide by the law
- **Politicians** to think and act for the good of the nation

We also need a systematic effort to reorganise the wilted state that stifles economy. First of all, we must separate the state from production. It must cease operating as a producer and apprentice entrepreneur and engage in providing actual social goods, regulating markets not functioning properly and facilitating citizens. Within this framework, markets will undertake the allocation of resources and provide citizens with alternatives.

The substantial change of the Greek state's mechanisms can be achieved through the following four elements:

- **Total reform of legislation** through codification, simplification and correlation with reality as well as full implementation and rapid administration of justice

- **Stable taxation system** providing motives that can increase the funds inflow, attract foreign capital and control the cost required for markets' function and especially real estate market

- **Improved public administration**, free from political party interventions and with knowhow from the private sector

- **Privatisations, Public and Private Partnerships and trusts** for the transformation of public sector's transactional activities. All the organisations that will remain under public control must constitute independent institutions with permanent administrations.

If we create a comprehensive and internally consistent agenda for the transformation of the state and start to implement it systematically, the lack of confidence from the markets will start to diminish and the country will become more attractive to investments.

The strategy is simple: attract investments.

Private capital will first flow to a small number of large **infrastructure projects** and **tourism**. The competitive advantages we can utilise are Greece's geographical position, which is suitable for trade activities and energy distribution, and its unique beauty. For the time being, foreign capital will not take interest in SMEs or companies active only in the local market. However, SMEs, as all other economic sectors, will benefit from the multipliers created by these investments.

The flow of private capital towards large infrastructure projects will be amplified if it is combined with funding from **NSRF** and if banks release assets trapped in their balance sheets. Nevertheless, in order for tourism, a traditionally extrovert sector, to attract funds, it must improve both in terms of real estate and hotel management.

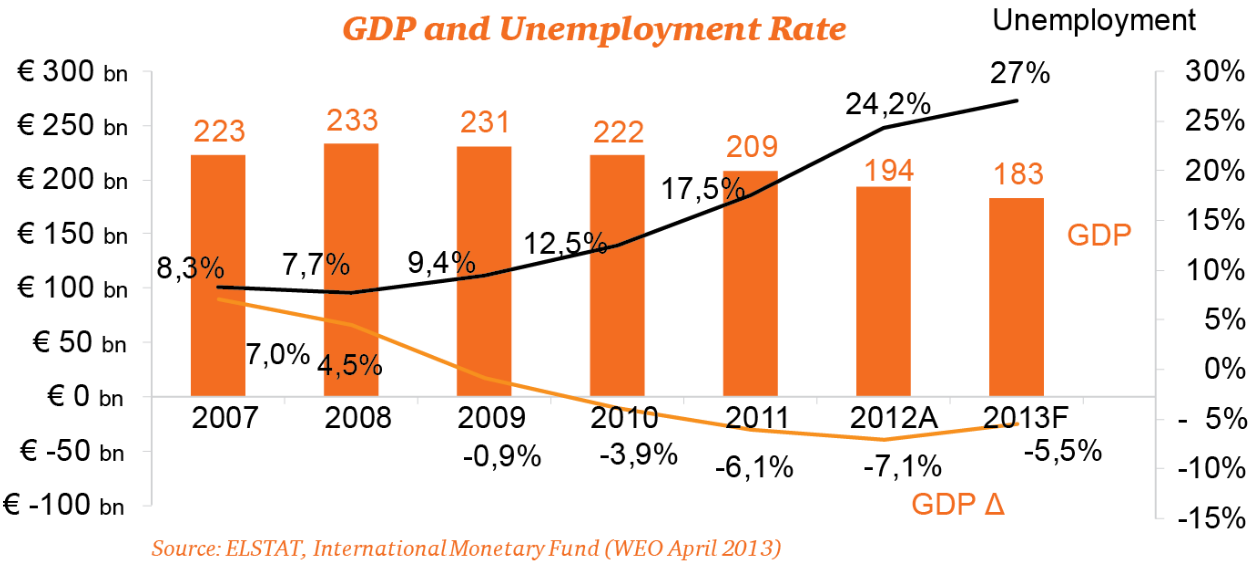
This post-Keynesian funding of growth, with mainly private capital, will create a virtuous circle of investments and consumption which will mobilise all economic sectors.

It is clear that the lack of confidence which we ourselves created has a great cost. We have to eliminate this cost through the implementation of substantial changes to the state and the economy. It will obviously take time. But even so, the effort must begin immediately in order to produce results.

1. Greece today

The worst recession in modern history

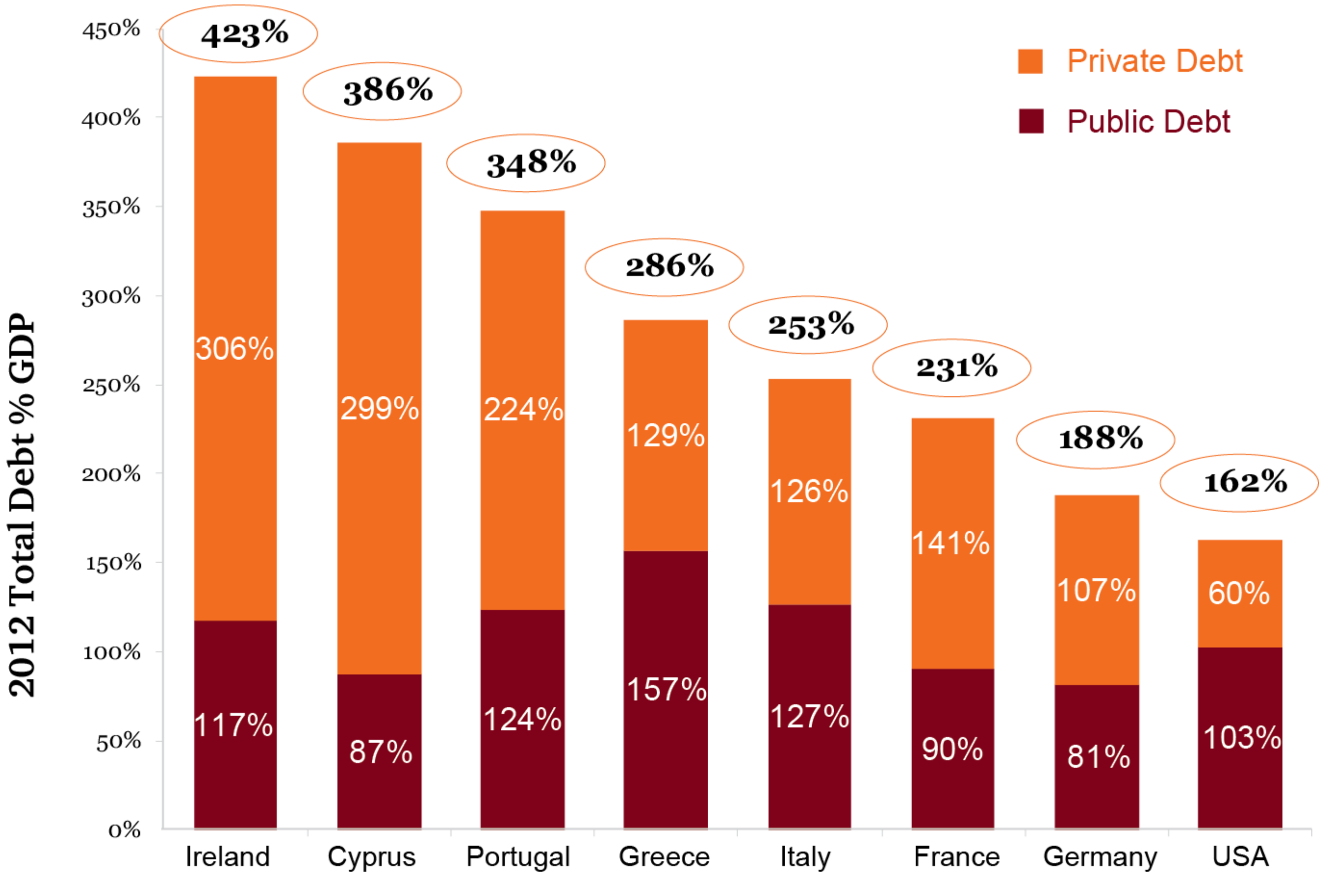
Greece has overcome the risk of exiting eurozone. It is now widely accepted that Greece's exit from the eurozone would have disastrous consequences for the country itself as well as severe impact on the eurozone. Even though Greece remains in the eurozone, its financial condition remains critical. From 2008, Greece remains for the 6th year in a deep and prolonged recession. The cumulative decrease in GDP for the period 2009-2013 has reached 25%, while unemployment rate rose to 27%.



We are witnessing the longest recession in modern history, longer than the great depression of 1930's. The US economy recovered after 5 years of GDP decrease. The Greek economy continues to shrink for the sixth consecutive year. The total decrease in GDP (25%) reflects how the crisis afflicting Greek society and economy today.

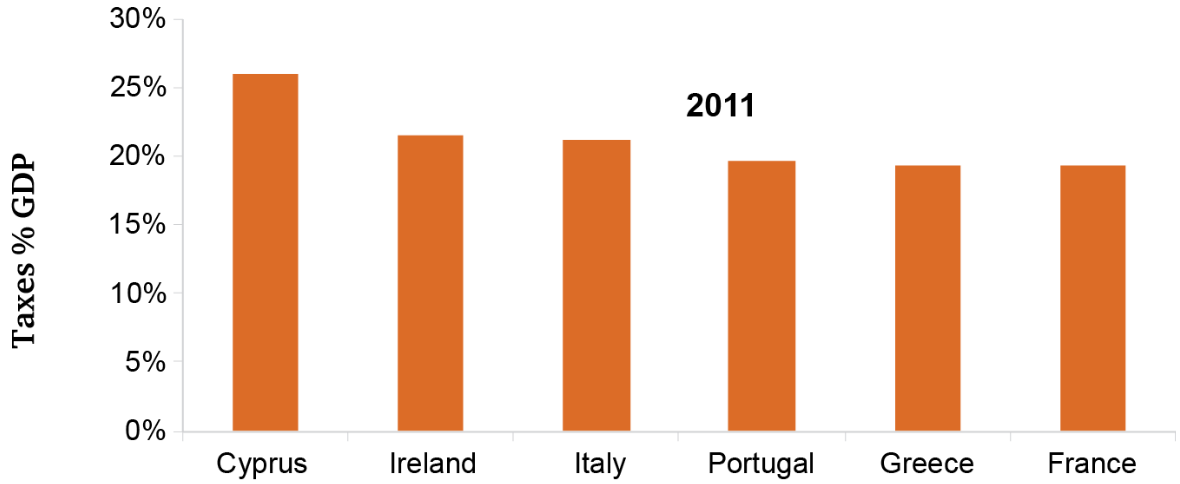
Is Greece actually over-indebted?

While government debt is at 157% of GDP, Greece, compared to the countries that are under Troika's supervision, is not over-indebted. The total private and public debt equals to 286% of GDP, lower than that of Ireland (423%), Cyprus (386%) and Portugal (348%) and similar to that of Italy (253%). The fact that differentiates Greece from all other countries is that the Greek government debt as percentage of GDP compared to the respective private debt percentage is the highest of all, affecting private sector's financing. If, by magic, the government debt decreased by 30 p.p., the private sector could borrow the same amount and finance growth, without affecting the total debt of the country.



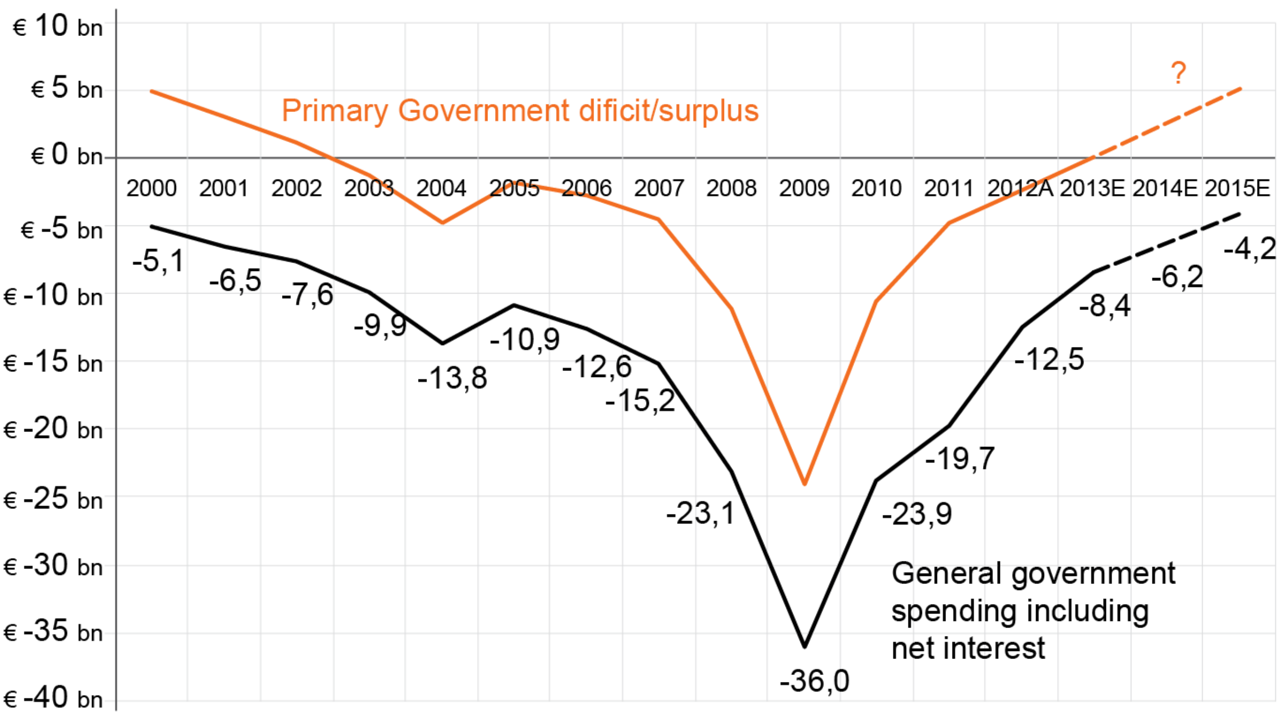
Source: Eurostat

With Greek economy's current structure, the inflated public sector absorbs resources that are disproportionate to its size and stifles all other economic sectors, discouraging investment activities. In practice, Greek state's tax income, which amounts to EUR 48 billion, must service a government debt amounting to EUR 304 billion. Due to the Greek State's inefficiencies the tax income does not suffice to service the government debt, even though, as percentage of GDP, it is similar to that of other countries.



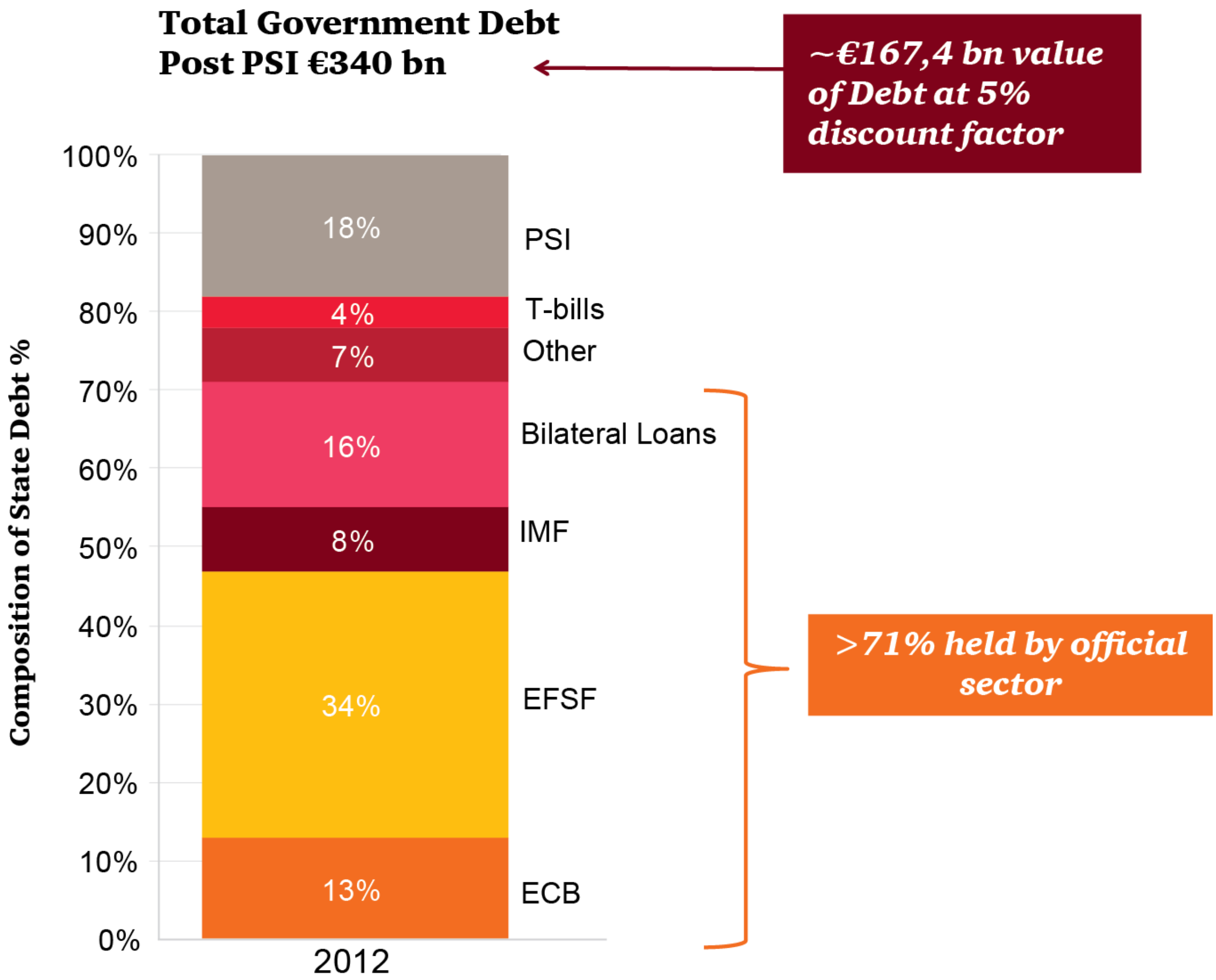
Source: http://data.worldbank.org/indicator/

The Greek government deficit has been improving consistently in the last years and the country is expected to achieve a primary surplus after 2013. GDP has been decreasing at slower rates compared to 2010-2012. The structure of the government debt has improved greatly since 71% is in the hands of our institutional creditors[1] with an average annual cost of 2%, while, in terms of net present value discounted with the interest rate at which Italy and Spain borrow from the markets, the government debt amounts to EUR 167 billion compared to EUR 340 billion, which is its nominal value.



Source: International Monetary Fund (WEO April 2013)

[1] IMF, Eurozone member states, EFSF, ECB

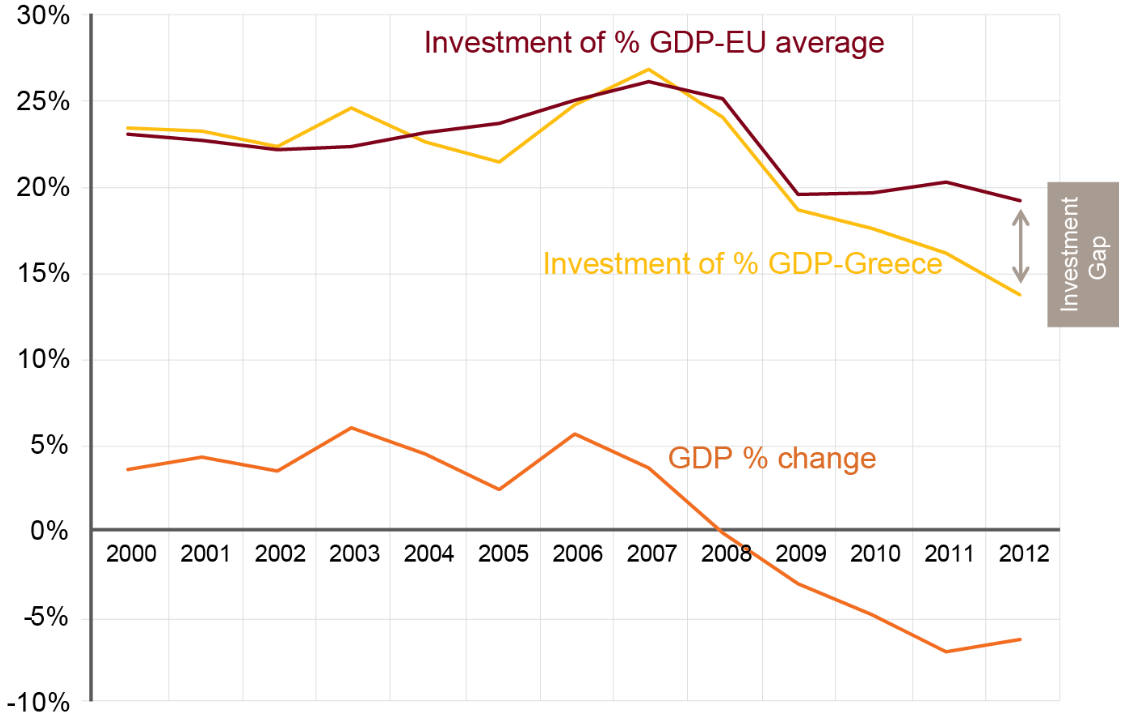


Source: GS Global ECS Research

Greek bonds' yields, with Greek bonds representing 18% of the government debt, have fallen under 10% following the successful implementation of PSI and Mario Draghi's pledge in July 2012. Nonetheless, this level is approximately 6 p.p. higher than the yields earned by Italy, Spain and Ireland and 3 p.p. lower than that of Portugal.

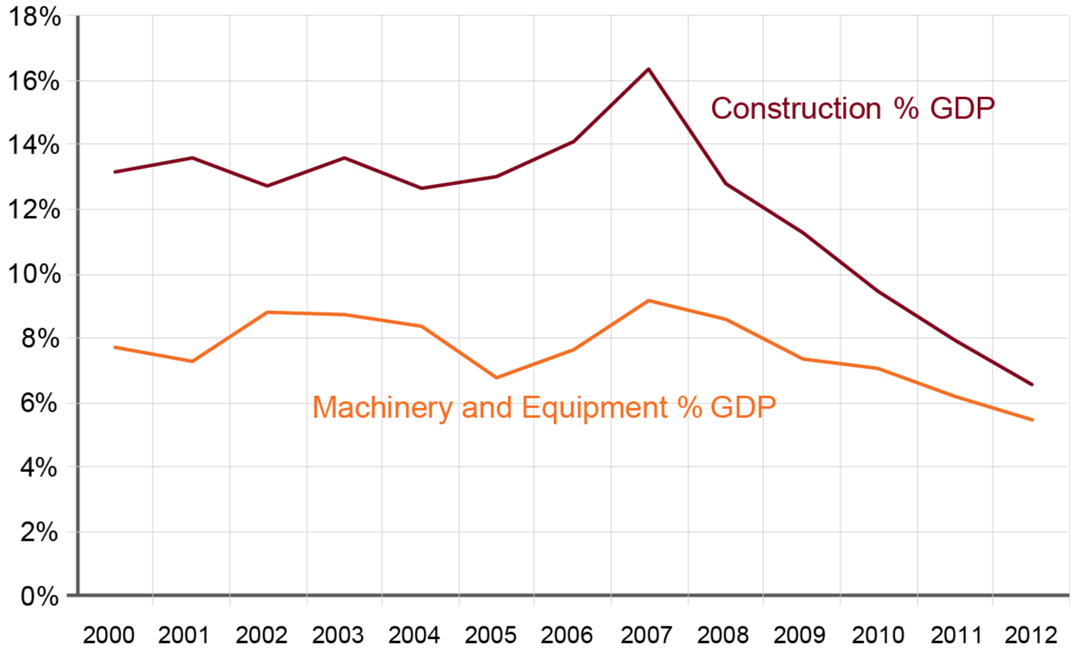
Investment gap: Greece's main problem

Budgetary improvements will not bring the desired growth unless annual investments within the economy increase. Historically, investments in Greece approximated the European average, but from 2008 onwards, their value has been increasingly deviating, following the downward trend of GDP. Total investments in 2012 were at 13.6% of GDP, compared to the average of 24% during 2000-2008, when growth was at 3.1%. The respective European investment average is 19% of GDP.



Source: ELSTAT, International Monetary Fund

The construction sector's collapse by 50% and the decline of the industrial investment rate are two of the main reasons for this investment gap.



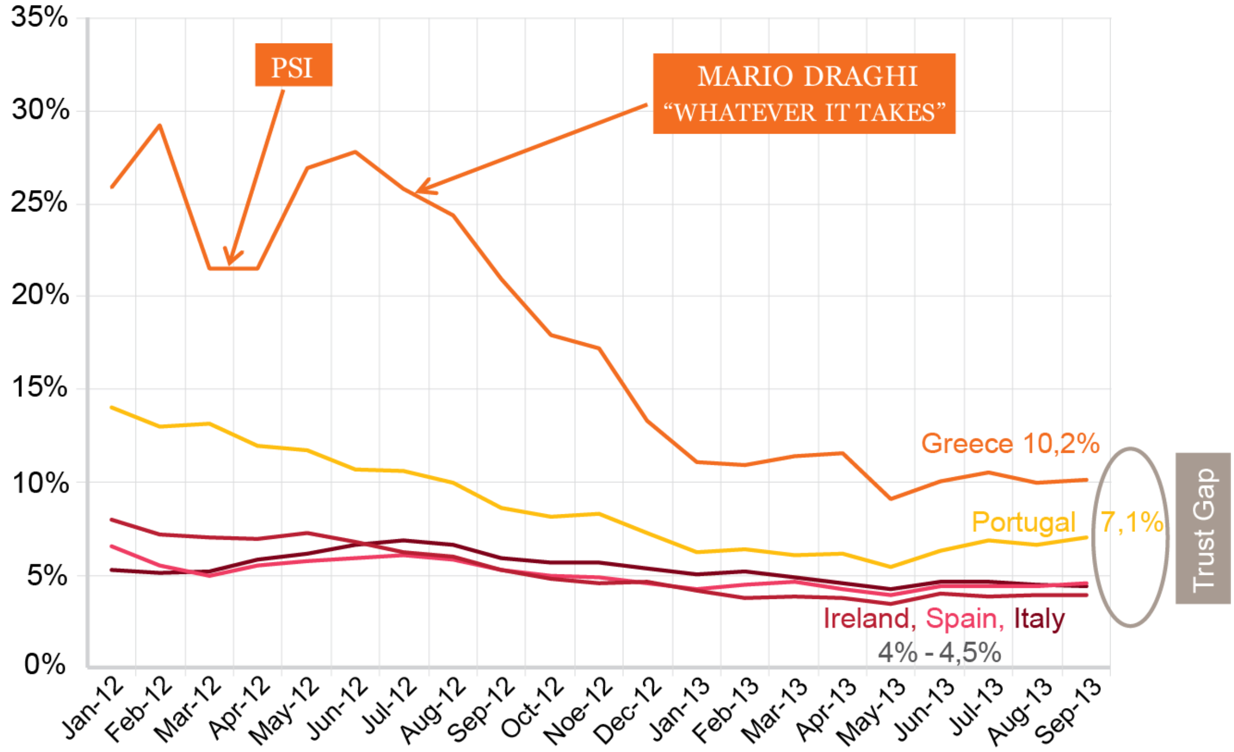
Source: ELSTAT

Mistrust = Lack of investments

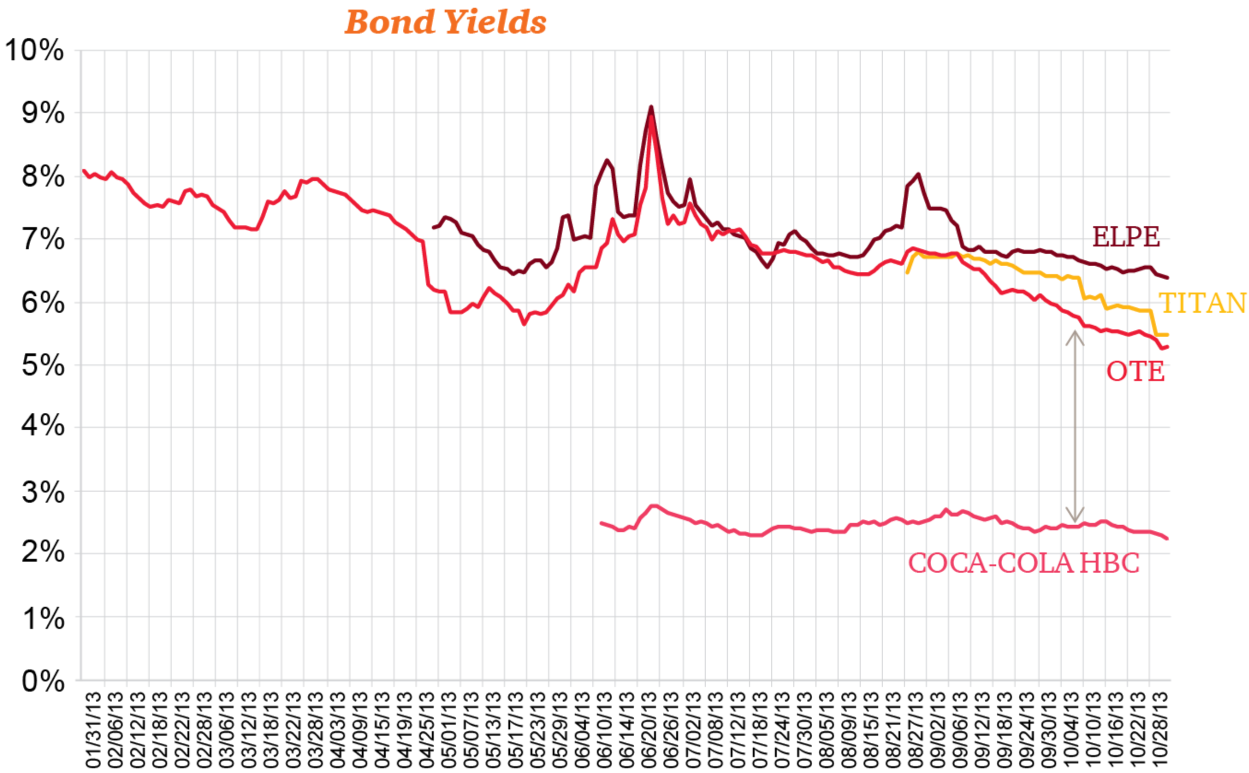
The yield of the 10-year Greek government bond is on a downward path since 2012, reaching 10.2% in September 2013. Compared to September 2012, the yield has fallen to 51% and has been aligned with similar bonds of other European countries such as Portugal, Spain, Italy and Ireland. The milestones of this adjustment were the successful implementation of PSI in March 2013, the statement made by the chairman of European Central Bank, Mario Draghi, in July 2012 “to do whatever it takes" to protect Euro and the formation of a stable coalition government after the double election process in summer 2012. The improvement of the Greek budgetary condition has contributed to the further decrease of the index to current levels, where it meets resistance.

The trust of international markets has not been regained yet, a fact that reflects the difference between Greek bonds and the yield of government bonds issued by countries that are currently subject to Troika's supervision (Ireland, Portugal) or have received great pressure from the markets (Italy, Spain).

10 year Government bonds yield



The deficit becomes more clear if one compares the interest rates of bonds issued by Greek companies established in Greece (e.g. Titan, Hellenic Petroleum, OTE) and the ones issued by Greek companies established in other European countries (e.g. Coca-Cola HBC). The former have an average yield of 6%, while Coca Cola HBC's are at 2.4%, resulting in a consistence difference equal to 4 p.p.



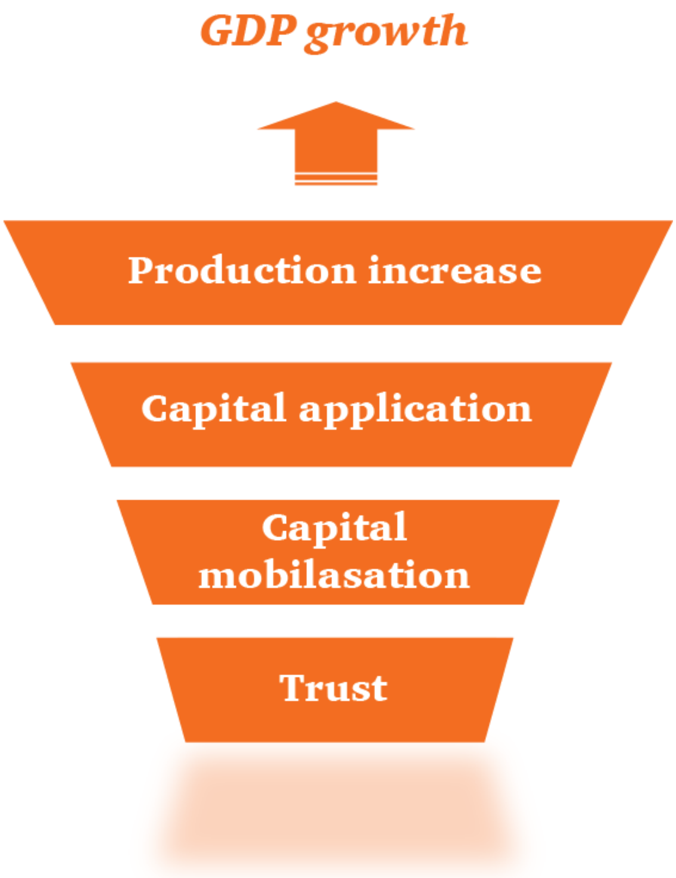
It is impressive and unprecedented that Greek companies borrow at a lower cost than the country itself. International markets have more confidence in Greek companies than the Greek state, sending a powerful message for the anticipated state's reform.

The lack of confidence reflects non-Greek investors' views regarding Greece's failure to implement essential reforms and the political system's inability to comprehend and address the real problems. The lack of confidence in Greece does not only result in more expensive capital for Greek companies compared to their foreign competitors. It also means that in order to obtain capital for a new investment in Greece, a new business venture must promise an expected return of approximately 5 p.p. higher than that of an investment in any other European country. These 5 p.p. discourage investments and hinder growth.

The investments needed in order for the Greek economy to get back on track and flourish are estimated at 20% of GDP annually instead of 13,5% that are today. The 6-7 p.p. gap equals to €12 bn more investments for the country and fills the space between recession and growth. Regaining trust through a structured economic strategy and substantial restructuring of the public sector is the only way to attract investments.

2. The challenge

Trust in an economy is a fundamental condition for capital inflow. The appropriate utilisation of capital in investments can lead to the increase of production and as a result of GDP, creating positive impact on budgetary management.



Rebuilding trust in the Greek economy requires significant reforms. We need a new reference framework for the economic dynamics of the country which can drive business practices and citizens' behaviours. The new reference framework must provide the necessary incentives/disincentives for:

- **Investors** to invest their capital in Greece
- **Entrepreneurs** to expand their businesses and make them more competitive
- **Civil servants** to have their work driven by outcomes
- **Citizens** to respect and abide by the law
- **Politicians** to think and act for the good of the nation

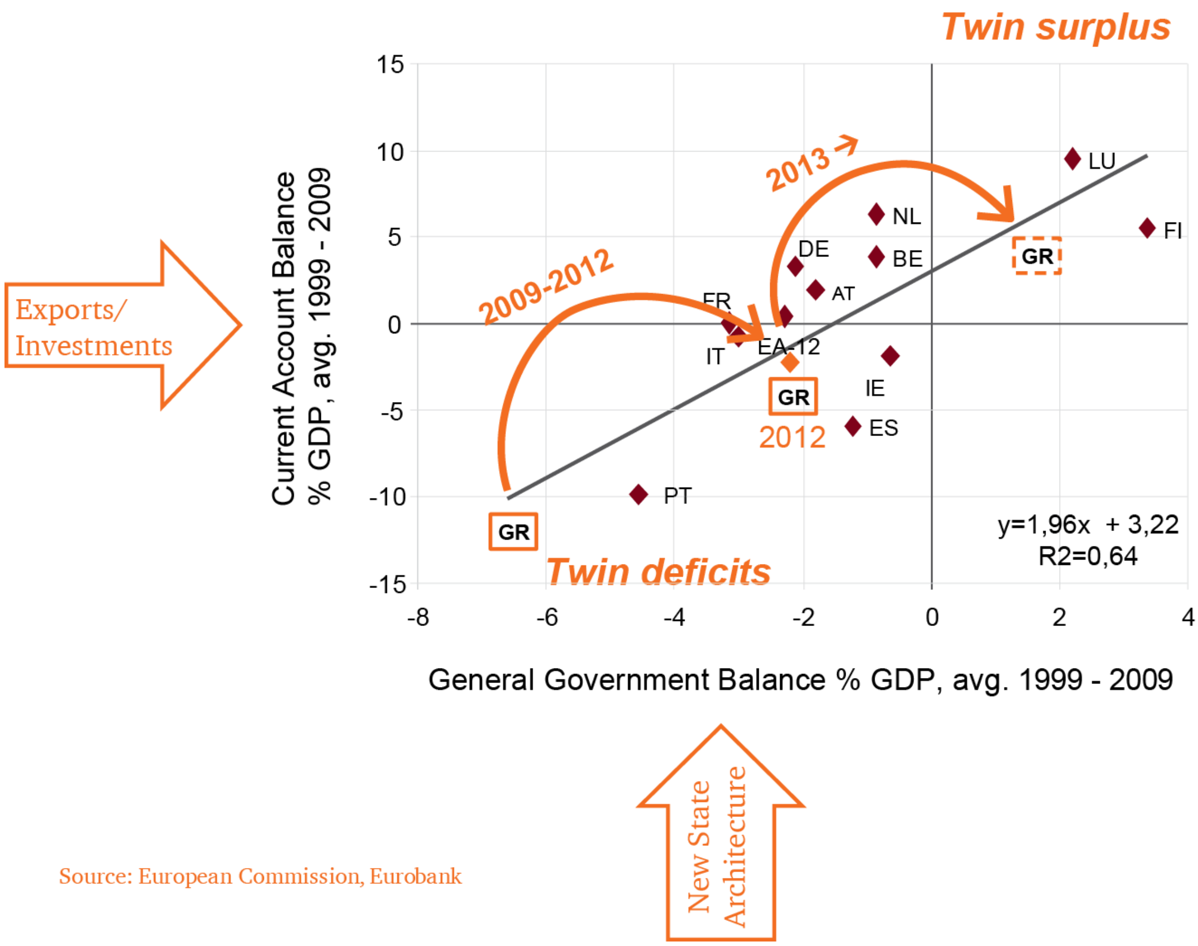
If we create a comprehensive and internally consistent agenda in order to change structures and institutions and start to implement it systematically, the lack of confidence from the markets will start to diminish and the country will become more attractive to investments. In this way we can give economy a real boost, creating an environment of growth and prosperity once again.

3. Investments in Greece's competitive advantages

A clear vision for growth

Economic recovery and growth through investments can serve as clear guidelines for public reforms as well as focus point for the various plans to exit the crisis.

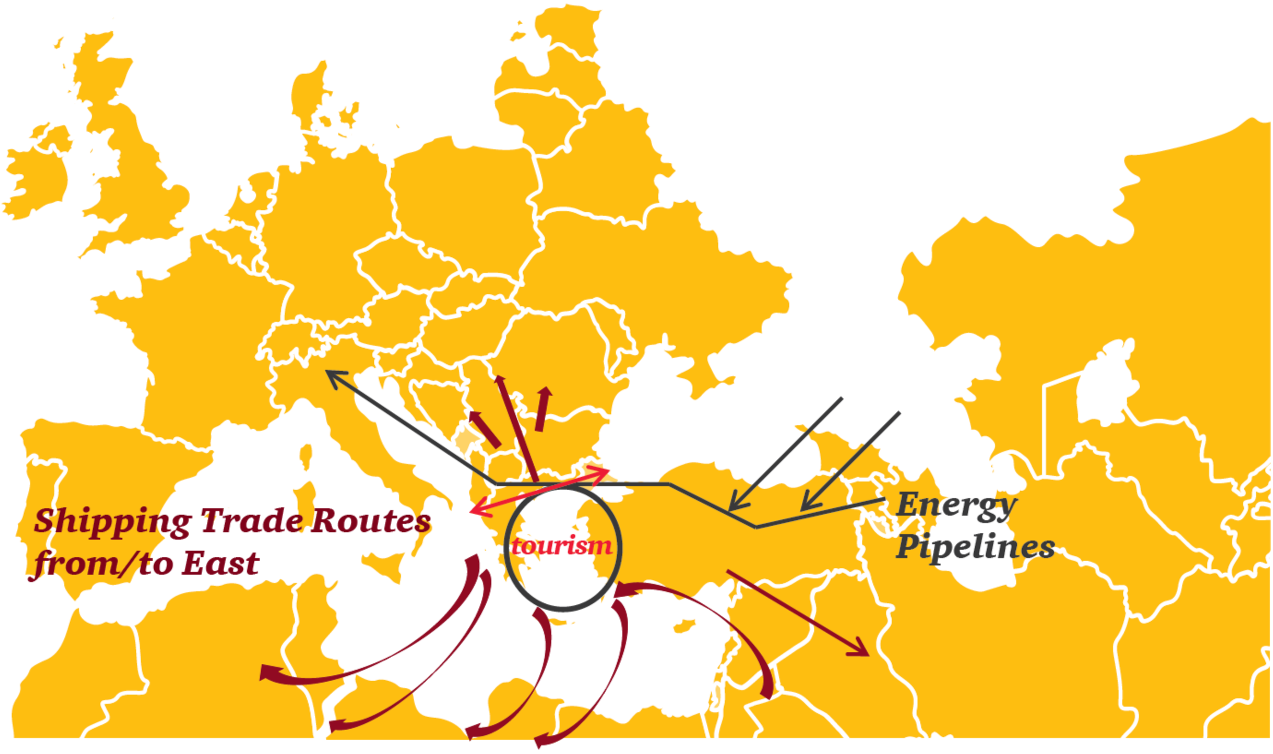
In 2009, the Greek economy showed a "double deficit" that is a state budget deficit combined with a current account deficit and was in the worst position compared to other European countries. This situation was a result of the previous economic model which supported consumption through public over-borrowing. The current situation is much improved but in order for Greece to overturn the double deficit and become substantially more competitive internationally, the public sector's structure must become more efficient and we must support activities that can significantly boost the Greek GDP and trade balance. In this way, the Greek economy will be able to achieve a "double surplus", establishing the country's competitiveness.



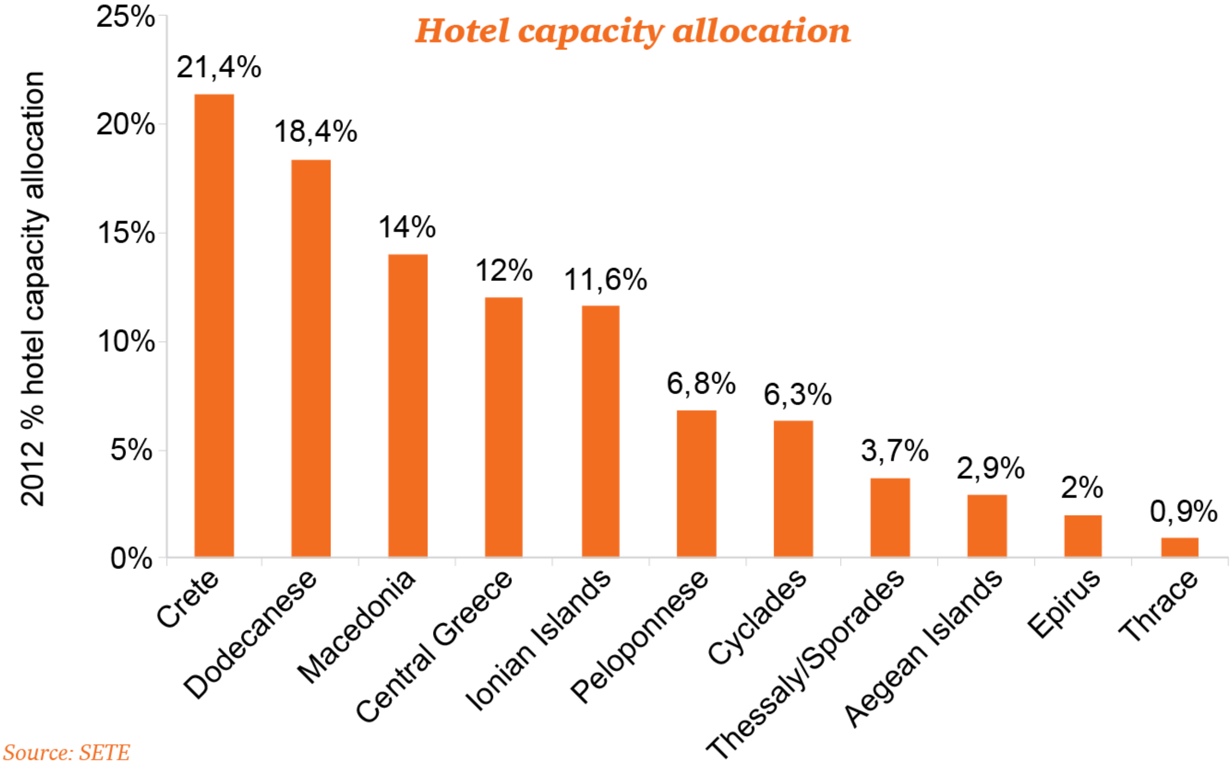
Source: European Commission, Eurobank

The road towards a double surplus and a stronger position in the international markets requires capital for investments and reforms. And capital may flow to Greece mainly because of its competitive advantages.

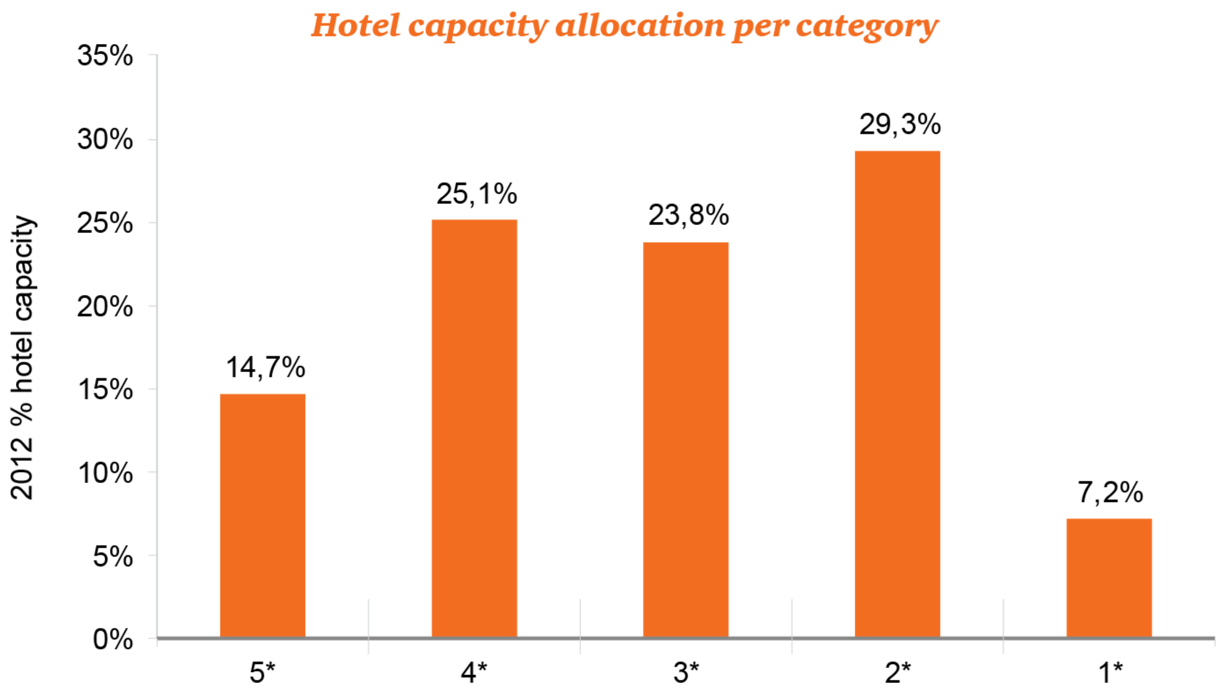
The first competitive advantage is the country's geographical position which from the ancient times has been a **commercial-cultural-economic crossroad** and a physical passage connecting Near and Far East with Central and South Europe. The trade flow from East to Europe passes through Greece, as shown by COSCO's investment in the port of Piraeus and the resulting change of its role in the Mediterranean transit trade. The energy and trade flow from Middle East and Central Asia to Europe passes through Greece, as indicated by the investment plans of TAP pipeline and the traffic of Egnatia motorway.



The second competitive advantage is that Greece is undoubtedly an international **tourist destination**, attracting more than 15 million visitors annually. Greece is the 17th largest tourist destination and counts more than 20 international airports and numerous ports and marinas. Today, Greek tourism infrastructure includes 9,670 hotels with 770,000 beds, demonstrating the importance of the Greek tourism industry not only in the South-East Mediterranean but in entire Europe as well

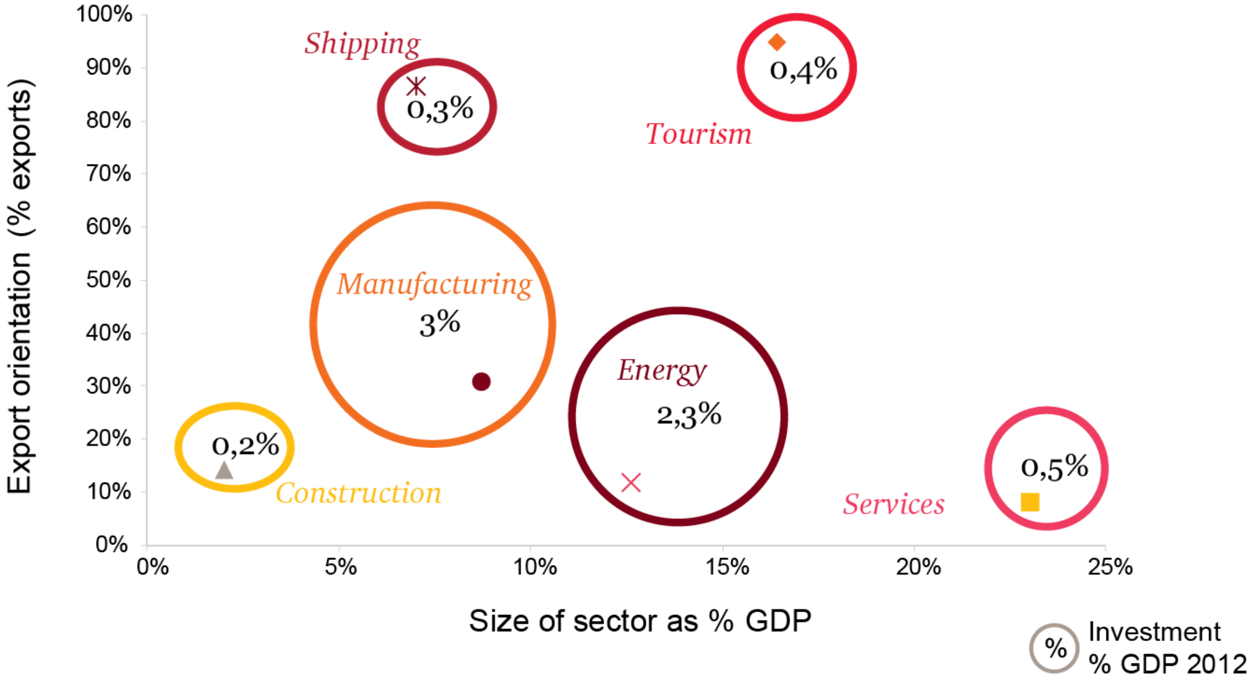


Source: SETE



Source: SETE

In order to achieve maximum effect from the investments made during the recovery period, these investments must be directed towards big scale sectorswith direct export potential and significant multipliers. Tourism is an obvious choice. The infrastructure industry also has the necessary scale to receive investments, in order to support horizontally related sectors such as trade (services), construction and energy.



Source: ELSTAT, BCG research, World Travel and Tourism Council

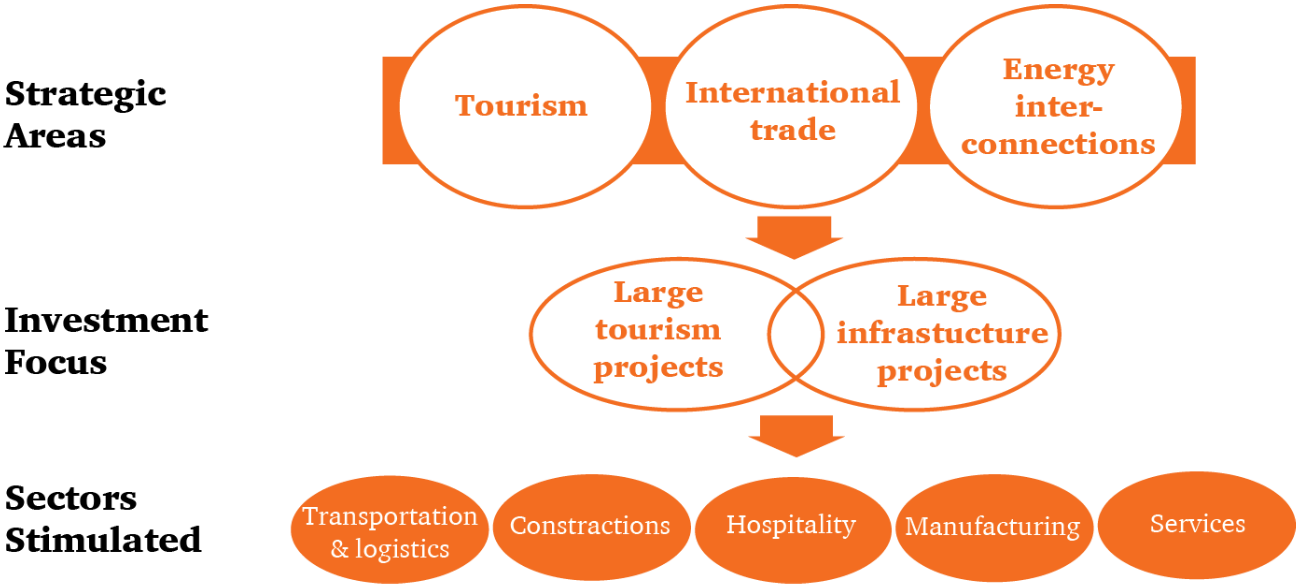
The Greek owned **maritime industry** is an odd example as it is internationally competitive and operates globally free of the limitations and the restrictions the Greek state imposes on domestic economic activities. Greek ship owners control over 16% of the global fleet[2], 20.8% of global tanker fleet, 19.9% of bulk carriers global fleet and 6.8% of container ships in terms of dwt capacity. The Greek flag holds the 6th position internationally (in dwt), while the Greek owned fleet counts 3,321 ships (over 1,000gt) of a total capacity amounting to 224 mil. dwt. Approximately EUR 66 bn are invested in Greek shipping, with 80% of the capital coming from the international markets. In 2012 alone, the Greek shipowners invested EUR 5.4 bn in new vessels, that is approximately 21% of total investments, public and private, in the country. This amount represents the 24.5% of total investment of European shipping companies in new ships, with Greece holding the 2nd position after Norway, as regards investments in new vessels. Moreover, according to Marine Money data, in 2011 and 2012 private equity funds invested approximately USD 6.4 bn in the shipping sector.

The Greek owned shipping industry, operating in an international environment with stable and generally favourable tax regime, mobilises gigantic economic resources even during periods of crisis. In a stable and positive environment international funds can be easily attracted by Greek owned shipping companies.

2. Un Review of Maritime Transport, 2012

Strategy to exit recession

Infrastructures facilitating tourism, trade and energy transfer and tourism industry itself are the strategic areas for investment. The initial investments in these sectors will give a boost to activity, driving growth in other economic sectors as well, such as transports, logistics, constructions, industrial production, hospitality and other services.



These areas have the potential to increase national income through high economic multipliers. Investments in infrastructure projects have a significant economic multiplier of 2x and can pass the increase of demand on to relevant economic activity sectors, initially in the cement and metal industry and, subsequently, in the entire Greek economy. Tourism multiplier is similar, at 2x, and has a high impact on restaurant and catering services, transports and construction industries.

These investments can contribute to GDP and create jobs on a solid basis. The significant boost of the Greek economy, which can be achieved by focusing on tourism and infrastructures, will spur growth in all other sectors of the Greek economy as well. The export-focused sectors will be affected first. Moreover, it will reinforce, with its dynamics, SME's growth all over the country.

Direct investments in infrastructure

Investments in the country's infrastructure, through Public and Private Partnerships (PPPs), will be the driving force for upgrading tourist services, energy interconnections, transit services and international trade. Completing only the already planned projects can result in capital inflow amounting to EUR 17 bn. by 2025.

Tourism Product Upgrade

- Key marinas
- Mega yacht marina in Lavrio
- Regional airports
- Upgrade of island ports
- Cruise ports
- Kastelli airport

€ 3 bn

Energy Interconnection

- Interconnection for electricity transmission in Aegean islands, Rhodes and Crete
- Investment in infrastructure of RES (geothermal/off-shore wind parks) to support the interconnections
- Gas pipeline interconnections to Turkey, Italy and the Balkans
- Construction of gas storage facilities in the north of the country

€ 12 bn

International Trade

- Transshipment services in the ports of Piraeus and Thessaloniki
- Through road networks (Egnatia and other central road networks)
- Development of road networks connecting to neighboring Balkan countries (Bulgaria, FYROM, Albania)

€ 2 bn

Upgrading tourism infrastructures and facilitating access to Greece have fundamental value. Upgrading local airports and island ports, building marinas and a mega-yacht marina (in Lavrio) are necessary for the reinforcement of tourist traffic. Specifically, building the Kastelli airport along with the existing network of airports and in combination with cruise ports will create new entrance points in the country and also diversify and upgrade the Greek tourism industry.

Energy interconnections will mobilise capital due to their strategic importance regarding European Union's energy supply, mainly with natural gas. Interconnection between Italy and Turkey through TAP is the key example. The construction of natural gas storage sites and an LNG terminal in North Greece will support these interconnections and reinforce Greece's role in natural gas trade. Electricity interconnection between the country's mainland, Aegean islands, Crete and Rhodes will reduce national electricity cost, will enable a more effective management of the islands' Renewable Energy Sources (RES) and an essential electricity connection with Turkey. It is of particular importance the fact that this interconnection will attract much greater investments in the development of Aegean's geothermal field and big scale off-shore wind parks.

Transports and transit infrastructures occupy a dominant position, as they are required to offer reliable and competitive services that will support the supply chains of the West, contributing decisively to the overall competitiveness in the national and international economic arena. The port of Piraeus already processes an important role in the provision of trans-shipment services and the same must be achieved for the port of Thessaloniki in relation with the Balkans. Similar must be the role of the Greek national road network and especially Egnatia motorway, connecting Turkey and Middle East with Europe and the Balkan countries.

Direct investments in tourism

In order for tourism to gain the necessary dynamics to attract new investments, the Greek tourism must be upgraded and Greece must become a high-end tourist destination. To this end, the composition of the country's hospitality facilities must change. The current segmentation of the domestic hospitality units in small hotels and apartments or rooms for rent must change significantly and focus on integrated resorts and high quality specialised resorts.

Integrated resorts offer one of the most attractive choices of the tourist market. As Greece evolves in a 5+ star destination, there is the need to create resorts that offer a variety of activities combining: thermal tourism (thermal centres, spa), sports tourism (sea sports, golf courses), maritime tourism (marinas), conference tourism (conference centres) and much more. Today, several integrated resorts are under construction in Greece in cooperation with top brands of the tourism industry. The development of these resorts will contribute to promoting the wider area of their establishment as a tourist destination. For the development of resorts of such scale it is crucial that the licensing procedures required for their operation are regulated and simplified.

Investors can discover exceptional locations in Greece -by the sea or in the mountains- that can offer unique opportunities for the **development of specialised resorts**. The key to the success of specialised resorts is the study and the identification of the tourist activities that can make the most of the unique advantages of each location. For example, thermal baths and medical wellness services as well as religious and cultural sites provide the opportunities for the development of high quality tourist resorts, creating destinations that are considered unique in their category, globally.

Medical tourism could also flourish making Greece a centre for provision of medical services in North Europe, Turkey and Arabic countries. Greece can benefit from offering high quality medical services, aiming mainly to middle classes, compared to the respective services offered by neighbouring states (Balkans, Middle East and Arabia). Moreover, the absence of legal restrictions in establishing private clinics combined with thermal springs and also the wide availability of facilities can transform several Greek locations into specialised medical services provision centres.

The economic need to upgrade the scale of hospitality units requires the restructuring of the hospitality sector by separating the provision of hospitality services from the ownership of property by establishing Real Estate Investment Trusts (REITs). REITs in combination with large hotel management companies will provide the sector with the scale needed in order to become globally competitive. Especially as regards marketing and bed sale internationally, the concentration can help boost prices and also create non high season specialised tourism offerings that can improve occupancy indices and hotels' financials. Hospitality REITs will facilitate capital inflow for hotels' upgrade and expansion, attracting large scale institutional investors with different risk/return requirements compared to traditional investors. Increased transparency and concentration of property under one ownership will mobilise resources and help banks relax the existing stifling relationships.

The creation of an international secondary residence market will also give a boost to the Greek economy. It is estimated that more than one million European citizens consider Greece as one of the destinations to have a secondary/holiday residence. At the same time, baby boomer generation have started to show their interest to buy holiday residences with the prospect of retirement, a fact indicated by the sale of 4 million holiday residences/units in France, Spain, Italy, Portugal, Cyprus and Turkey during the last twelve years.

In Greece, secondary residence market can generate revenue from the extended stay in the country while it can support the construction industry. The prerequisite for the creation of such a market is its initial function in only few destinations, in order to gain the necessary depth and liquidity as well as the formation of a mechanism for financing final buyers of secondary residences. There is a long way ahead, but the function of such a market could yield 30,000 residences in the market by 2025, indicating a steady investment flow around EUR 2.5 bn annually.

It is crucial that changes are supported by an efficient plan for promoting Greece abroad in order to maximise benefits. Greece must be promoted as a cluster of unique destinations, with infrastructures capable to support high quality services, so as to attract high-end tourist market. The marketing plan must also aim to extending the tourist season creating demand for all year round and promoting multiple rather than individual destinations.

Greece will be able to upgrade the tourist product it offers and improve its brand name as a global tourist destination. Growth in the tourism industry is expected to mobilise investments amounting to EUR 20 bn by 2025.

Actions

1. Develop tourism infrastructure
   - Build marinas at central locations of the country
   - Upgrade local airports and island ports
   - Build a mega-yacht marina in Lavrio
   - Build the Kastelli airport in Crete
   - Upgrade regional airports
2. Develop infrastructures for energy transfer and international trade
   - Natural gas pipeline interconnection with Turkey, Italy and the Balkans
   - Build natural gas storage sites in the north region of the country
   - Develop an interconnection for the transmission of electric power to the Aegean islands, Rhodes and Crete
   - Make large scale investments in RES (geothermal/off-shore wind parks) with the support of interconnections
   - Upgrade the road network connecting the country with all the Balkan countries
3. Take the necessary measures to promote growth in the tourism industry
   - Change mentality, simplify and expedite licensing procedures
   - Establish REITs in the hospitality industry
   - Establish large hotel management companies
   - Create a secondary residence market
   - Develop a marketing plan promoting Greece as a 5+ star destination

4. Capital resources

The Greek economy can be reset through investments co-financed by private funds. However, attracting private funds will be successful if supported by European Structural Funds and if banks release assets that are trapped in their balance sheets. This post-Keynesian funding of growth, with mainly private capital, will create a virtuous circle of investments and consumption which will mobilise all economic sectors.

Public and Private Partnerships (PPPs) can boost economy if they are supported by European Structural Funds and obtain the necessary funding from local banks. Given the long period of time that is required in order to complete and more importantly derive benefit from such investments, a stable tax environment and economic growth are the necessary conditions for attracting large scale funds.

Seeking capital from investors

The development of infrastructures is the driving force of economic recovery. **Developing Public and Private Partnerships** is practically the only way to attract capital to infrastructures.

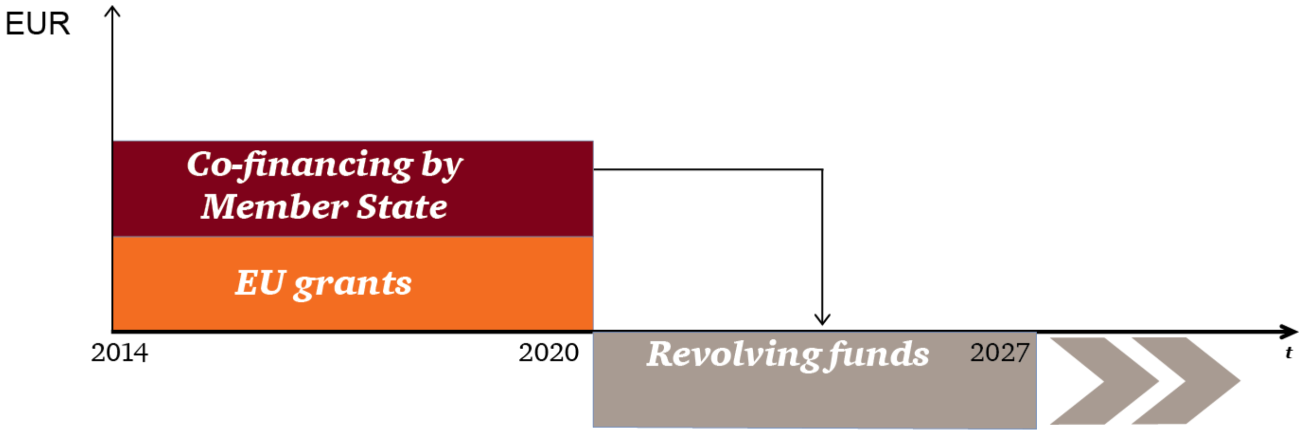
Another crucial factor for the development of infrastructures is **the finalisation of public infrastructure management companies' privatisation** and especially of those that are quoted in the stock market and publish their financial statements at international level. These privatisations could indicate to international markets and investors that the state has commenced a process of reforms and structural changes and that it is now committed to proceed to the actions necessary for achieving sustainable growth and economic stabilisation.

Some examples of public companies the privatisation of which could contribute significantly to the mobilisation of resources towards infrastructures are Piraeus Port Authority S.A. (PPA S.A.), Thessaloniki Port Authority (THPA S.A.), Hellenic Petroleum S.A., Public Power Corporation S.A. (PPC), Athens Water Supply and Sewerage Company (EYDAP S.A.), Athens International Airport S.A. (AIA), Independent Power Transmission Operator S.A. (IPTO or ADMIE) and Thessaloniki Water Supply & Sewerage SA (EYATH). These privatisations are expected to bring EUR 4 bn to the Greek state with secondary investments being the most significant benefit derived in a medium-term horizon.

Seeking capital from European Union's structural funds

Strategic investments in infrastructures which facilitate trade and energy transfer are extremely relevant with wider European politics. The participation of European Union's structural funds in the actions for the recovery of the Greek economy is important for two reasons. Firstly, it provides additional resources for investments in infrastructures and economic reforms. Secondly, it reinforces the sense of trust and stability, creating an environment of mutual support and partnership in the country's effort.

Funding from the European Union, that is traditionally provided through grants, is now shifting to **financial instruments**. These instruments constitute a effective way to develop resources, supporting investments through loans, guarantees, share capital or other risk-bearing mechanisms, possibly in combination with interest or guarantee subsidies.



In the long-term, the use of financial instruments will result in the gradual decrease of European grants due to the leverage of the capital that will be invested from 2020 and onwards. Funding is supported by development or investment banks which will grant loans under more favourable terms.

Actions

1. Provide for the resources necessary for supporting the strategic areas of growth (tourism, infrastructures) in the planning of the new programmatic period
2. Direct available funds towards critical sectors of the economy (tourism, infrastructures)
3. Promote special financial instruments that are suitable for large scale investments and "recycle" capital over time

Capital trapped in banks' balance sheets

Over-indebted companies often are not in position to fund neither their growth nor their operation. There is risk that a part of the country's productive network is formed by zombie companies that utilise resources but are in no position to support growth. Inspired management and anticipated decrease of non-performing loans are the key economic tools for recovery.

Currently, total non-performing loans amount to EUR 65 bn, while this figure is expected to rise in the near future by EUR 10 bn. Out of this amount, EUR 35 bn pertain to business loans, partly secured with collaterals.

The reasons making the management of problematic business loans difficult in practice are the following:

- Lack of liquidity and the necessary capital to support the sustainable restructuring of companies or the sale of assets
- The direct negative effect on regulatory capital resulting from the recognition of (inevitable) losses
- Weaknesses of the Bankruptcy Code which hinder rapid liquidisation of unsustainable assets and flexible restructuring of sustainable companies out of court
- Lack of consensual dispute resolution mentality through arbitration

The aforementioned problems could be addressed by changing the bankruptcy code in a way that would result in rapid and practical solutions and improve the handling of problematic loans by the banks. The active handling of non-performing loans, based on the sustainability of the borrower and in order to support economic activity, would have two important benefits for the economy. Firstly, it would mobilise semi-dormant assets and secondly it would attract "fresh" investment capitals. It is estimated that the new capital that will be invested in the assets that will re-enter the market (e.g. enterprises, hotels, industrial sites) will amount approximately to 20% of the losses expected to be realised by banks. This is translated into EUR 7 bn new capital and acceleration of economic activity.

The losses the banks are expected to realise do not necessarily constitute an impediment in the process of restarting economy. If these losses are recognised as tax credit, as provided by Basel III, their effect on regulatory capital will be immaterial.

Actions

1. Active handling of non-performing loans based on the borrower's sustainability
2. Tax credit of losses resulting from non-performing loans write-off
3. Amendment of Bankruptcy Code
4. Establishment of guidelines for the consensual resolution of problematic business loans

5. Rebuilding trust

The four pillars supporting the effort to regain markets' trust in Greece are:

- The clear definition of a national vision and goal
- The removal of every restriction imposed on entrepreneurship (according to a recent OECD report there are 555 legal obstacles hindering the function of the markets and business decisions)
- The reinforcement of legislative stability (every year the Greek parliament votes for 120 to 150 new laws that alter the way economy and society functions, impeding long-term planning and decision making)
- The increase of the state's efficiency and speed

If we establish a clear and integrated action plan focused on the state's restructuring and economic growth and proceed to its implementation systematically and consistently, we could reinforce trust in Greece and preserve the air of reform with long-term results.

Removing obstacles to entrepreneurship

Overcoming crisis and resuming growth is not feasible without the systematic and continuous effort to remove the impediments that stand in the way of the development of productive activities. Continuing administrative malfunctions and public administration's insularity have become factors of ineffectiveness both for the state and the economy, especially in an environment in which the social framework is becoming more and more complex, innovation is integrated in the technological environment at an extremely rapid pace and the business environment is become all the more globalised.

A structured change of the relationship between the state and enterprises is imperative in order to promote entrepreneurship. The most important point of contact with enterprises, apart from tax and insurance mechanisms, are licensing mechanisms. They are the key for enabling investments and they must feature elements of innovation.

- Shift from the existing system of "processing requests and approvals" to an innovative system based on "declaration of compliance" according to specific requirements
- Undertake the cost of proof of compliance by enterprises, resulting in a significant transfer of administrative cost of the licensing procedure from public administration to the private sector
- Transfer the burden of control from the phase of commencement of activity to the stage of operation
- Provide enterprises with the ability to utilise outsourcing of licensing services to certified bodies
- Establish through legal provisions a targeted system of controls during the enterprise's operation, based on risk analysis
- Establish a certification mechanism for all licensing bodies in public and private sector, based on standard organisational and operational requirements
- Establish a central tracking system in licensing process, in order to reinforce accountability and measure the effectiveness of procedures
- Establish a designated independent central government body to implement the reform and establish the participation of stakeholders in the governance of entrepreneurial environment

Establishing institutional stability

The volatility of the existing institutional environment is proved by the fact that somewhere between 120 and 150 new laws or law amendments are laid down annually. More specifically, during the period 2009-2012 750 laws and presidential decrees were enacted. This number indicates the complexity of the Greek legal framework, a factor that hinders the attraction of investments. The new laws often supersede previous ones and in combination with the large number of non-compliance cases they intensify institutional volatility, discouraging the inflow of capital.

The Greek legal framework must be characterised by more stability, long-term perspective and strategic planning, ensuring in this way the consistency between laws. Promoting overall law enforcement, ensuring consistency and codifying laws and implementation acts are critical parameters that can improve institutional stability.

In order for legal content to be economically relevant to the circumstances prevailing in the regulated sectors, great emphasis must be placed on analysing economic and budgetary impact of new bills (Explanatory Memorandum) prior to their submission to voting, utilising specialised bodies of public administration (e.g. Centre of Planning and Economic research) or private sector.

Establishing a no-amendment 3 year period commencing on the date of enforcement would also contribute towards institutional stability. Furthermore, it would be advisable to set a restriction regarding the number of new laws or amendments on existing laws the ministries are permitted to submit to the Parliament. Every ministry could, for instance, be permitted to introduce only one new law per general secretariat every year. In this way, the institutional framework can be based on a limited number of main laws per ministry, each one of them regulating specific areas of policy, rather than on multiple provisions that do not address issues effectively.

Immediate codification of laws, starting from those concerning activity commencement and business operations, is a necessary condition for institutional stability. The codification must be a prerequisite for laying down new laws. Codification of laws combined with a slower rate of amendments will achieve the desirable level of stability in the country's legal framework. Dialogue for the long-term policy underlying in every new law, can reinforce the relevance of laws to real economy and will enable the effective resolution of issues.

Actions

1. Codify and computerise legislation prioritising first the legislation pertaining to activity commencement and business operation
2. Utilise specialised bodies (public and private) for the analysis of economic and budgetary impact of new bills (Explanatory Memorandum)
3. Restrict the number of new laws submitted to the Parliament by every ministry and implementation of non-amendment period
4. Establish codification as prerequisite for laying down new laws

Creating a tax regime without surprises

The inflow of capital in the Greek economy will depend greatly on the provision of the necessary tax incentives and concessions. By contrast with the current income and property tax policy, attracting investments and growth will be facilitated by providing tax opportunities. The model of attracting investments by implementing particularly low tax rates (e.g. model of Cyprus, Ireland, Arab Emirates etc.) is very difficult to be implemented under the current circumstances, while the success of such a model depends on several factors as well as the overall orientation of the economy (e.g. infrastructures, restrictions imposed by labour law etc.). But also the provision of generous tax exemptions for large investments (tax holidays), which are often considered, are difficult to implement within the overall European legislative framework.

The planning of every new tax strategy must be focused on enabling investors to know in advance the rules and regulations of the market and to be able to accurately assess the tax burden and include it in their business plans. The key for establishing a environment of trust, combined with targeted tax incentives, is:

- State's commitment to restrict the number of tax laws introduced to only one law every three years, especially considering that only just recently two new Income Tax Codes and Codes of Tax Procedure have been enacted, which have been drawn up in a contemporary spirit and incorporate many elements from international tax trends.

- Staffing key and executive posts of the tax mechanism with qualified personnel borrowed from the private sector

- Creation of a fair and unbiased system for resolving tax disputes before reaching court, for, as demonstrated in practice, the existing mechanisms are part of the tax audit mechanism

The inflow of capital will also depend on the provision of the appropriate tax incentives which can be classified in four categories:

- Abolish Tax on the Movement of Capital equal to 1%. Greece is one of the few countries of the European Union still implementing the specific tax

- Sign bilateral tax conventions with counterparties countries that have been investing internationally in the last years such as China, India and Golf countries, favouring Greece by imposing low taxes. Until now, the country's priority in negotiating such conventions was to ensure the highest tax revenue from the tax residents of these countries. This logic must be reversed in order to transform Greece into a preferred trade partner

- Abolish stamp duty in loans, which creates problems to international investors who wish to finance their subsidiaries established in Greece. The abolishment of Stamp Duty Code as a whole would also be recommended, as it was enacted (apart from a few changes) in 1931 (!) and is an entirely anachronistic framework for taxing economic transactions

- Reduce or abolish Property Tax for real estate development companies, such as tourist resorts and hotel facilities. A significant reduction in the Real Estate Transfer Tax, which, today, is by far one of the highest in Europe, combined with a reduction in other taxes and charges (registration and notary fees etc.) will help to attract investments

Actions

1. Commit not to change the tax regime for 3 years
2. Abolish Tax on the Movement of Capital and Stamp Duty Code
3. Sign favourable bilateral tax conventions with key trading partners
4. Reduce Real Estate Transfer Tax and abolish real estate tax on property used in production
5. Renew tax administration personnel through staff loans/secondments and joint actions from both public and private sector
6. Establish an independent and objective procedure for the administrative settlement of tax disputes

Building an effective system for the settlement of disputes

Currently the justice system is malfunctioning and, in principle, this is a result of the accumulation of outstanding legal cases and the delay in their settlement. According to the official statistics published by the Ministry for the first quarter of 2013 **there are approximately 700,000 outstanding legal cases** in the Civil and Administrative Courts of the country (excluding Justices of Peace). Out of these, 26,848 are cases within the jurisdiction of the Council of State and include 4,098 tax cases.

Delayed hearings and postponements, which are part of the ordinary course of case trials, apart from the obvious tribulations they cause to the involved parties, hinder entrepreneurship and economic growth. Apart from the delays in case trials, the accumulation also results from the large number of cases entered into the system, as well as the percentage of cases that continue to appeal proceedings.

The vast number of laws and the intricate legal framework are mainly responsible for bringing about disputes and litigations. The alternative methods for dispute settlement (that is Out-of-Court Settlement, Arbitration and their variants) have already been introduced in Greece but are still in the initial stages of their implementation. The systematic promotion of their implementation, by reinforcing the awareness of enterprises, will relieve the work load of the Greek justice system reducing the standard time of legal proceedings. As a consequence, many cases will be completed, instead of lingering, with apparent positive impact.

A special case of administration of justice with significant impact on the development of entrepreneurial activity and economic recovery is the Bankruptcy Code. Today there are numerous outstanding legal cases of companies with going concern issues which have ceased their operation and are in the process of default. Assets are held captive by the delay in the settlement of these cases and the resulting delay in companies' liquidation. The Bankruptcy Code must be modified in order to facilitate the termination and liquidation of companies dealing with going concern issues, in order to release their assets into the market and alleviate the negative impact from the termination of their operation. At the same time, as regards over-indebted companies which however maintain their sustainability, the Bankruptcy Code must provide the necessary tools in order to enable rapid settlement of disputes with creditors through out-of-court settlement.

Actions

1. Determine a maximum number of postponements and a maximum period of time from the first deposition
2. Enforce all institutional and administrative changes for the implementation of Alternative Methods for Dispute Settlement and raise the awareness of the business community
3. Modify the Bankruptcy Code in order to:
    - facilitate the dissolution and liquidation of non-sustainable companies
    - encourage rapid and consensual out-of-court settlements for sustainable companies

Upgrading the monitoring of budgetary figures

Budgetary reporting management and budgetary figures monitoring, as performed currently, has severe disadvantages:

- Limited data credibility regarding accuracy, completeness, validity and timing
- Inability to monitor budgetary figures on a consolidated basis and compare the figures of different periods
- Lack of information depth resulting in inability to draw conclusions regarding the cause of budgetary problems and different classification of budgetary reports from public bodies
- Absence of an appropriate information system for consolidating budgetary reports

All the above result in limited support of decision making at policy, management, resources allocation and budgetary control level.

The Greek government applies the cash accounting method. This method does not provide accurate and sufficient reporting regarding assets, liabilities and receivables of the public sector resulting in providing the government with a short-term and incomplete view of public finances.

The Greek General Accounting Office must publish information about revenue, expenditure, debt/deficit movement and financial transactions (loans, bonds etc.) for the General Government as a whole, according to the accruals accounting principle. By applying the accruals accounting principle and by adopting International Public Sector Accounting Standards (IPSAS), the Greek government can ensure timely and accurate reporting.

The adoption of modern methods of accounting will indirectly dictate the interconnection of all public information systems and the redesign of the state's procedures. These two steps will lead to higher quality financial information.

Actions

1. Immediate implementation of double entry bookkeeping system in all public administration bodies
2. Implementation of accruals accounting principle through the adoption of International Public Sector Accounting Standards (IPSAS), for the accounting monitoring of budgetary figures
3. Full implementation of IFRS in public companies and organisations and timely publication of audited financial statements
4. Creation of an automated process for collecting financial information and preparing consolidated reports at General Government level
5. Interconnection between public information systems

6. A state that can support growth

Public administration must be restructured and operate differently, like a living organisation which can adapt to changes, create standards and evolve in order to address society's needs. Public administration executives can play an important part in this change. Public administration is required to develop new features which will characterise the new state in the "post-crisis" era:

- ***Flexibility***: readiness to address new circumstances and adapt and respond to unexpected events in a rapid and (economically) efficient way

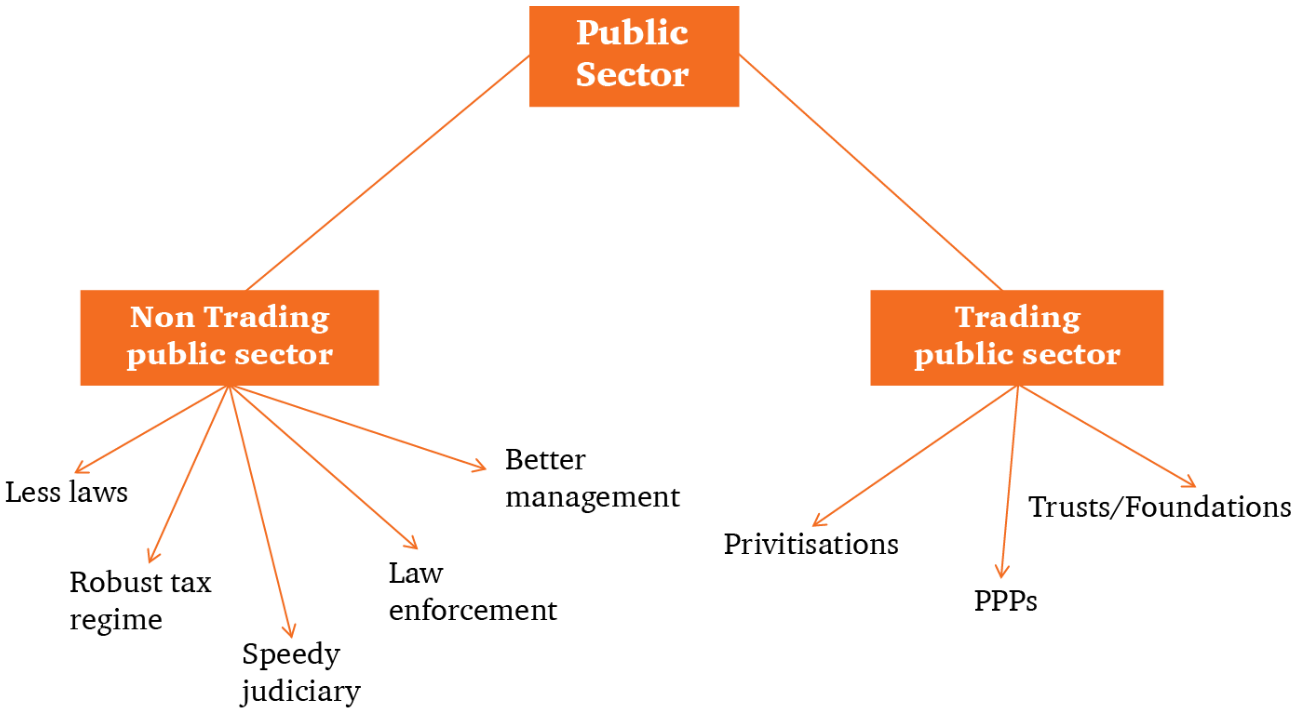
- ***Innovation***: ability to adopt new ideas and operational models, for expediting results

- ***Spirit of collaboration***: pursuit of partnerships with other economic sectors and industries, countries and organisations

- ***Transparency***: responsibility for actions and outcomes, especially now that there is a need to build an environment of trust and reinforce legitimacy

Structural changes regarding mentality and culture as well as reform of structures and procedures are required for Greece to overcome this crisis. State needs a new architecture so as to become more efficient and more simple. For the purposes of this change the state must withdraw from production and no longer participate actively in the markets. It must, however, reinforce its role as regulator of malfunctioning markets and become a facilitator of business activity. Setting markets free to allocate economic resources, providing regulation whenever necessary, can lead to a significantly improved function of the economy, in the long-term.

In this scope, the segregation between **non-trading public sector (administrative activities) and trading public sector (production activities)** is considered necessary. The restructuring of the non-trading sector must be based on elements that reinforce trust: fewer laws, stable taxation, swift administration of justice, law enforcement and more effective public administration. As regards the productive public sector, it must be significantly reduced through privatisations and PPPs and the activities which cannot be undertaken by the private sector must take an organisational form that can ensure the necessary efficiency.



Limiting state's production activities

The state must withdraw as market player and develop its role as market regulator and facilitator, first and foremost, by proceeding to a series of privatisations of public companies. Markets must operate free of government constraints or entrance restrictions and market participants must be able to decide freely on the allocation of resources. The state's role must be restricted to the provision of an appropriate regulatory framework and, thus, it must cease to interfere with markets and professions.

Trusts

The transformation of public organisations into trusts can play an important role in reinforcing transparency, sense of trust, efficiency of management and cohesion and consistency in public sector's roles and activities. Some examples of public organisations that could participate in the administrative reform programme are public hospitals, universities, schools, cultural institutions and museums.

Within this new administrative model, the assets of public bodies will be owned and managed by the trust based on a predetermined framework and specific management policies. The administrators of the trusts as well as the personnel that will be appointed by the administrators will be responsible for managing trusts and their capitals. The regular source of funding of these bodies will be the state in the form of Provision of Services Agreements, while their financial results and their pricing policy will be regulated by the competent Ministry or another regulatory authority.

The establishment of trusts, in the long-term, aims to minimise interference policy and government influence. This goal can be achieved as governments will not have the power to dismiss trusts' administrators and the appointment of the new administrators will take place upon the resignation of the previous administrators.

Actions

1. Public and Private Partnerships
    - Eliminate bureaucracy and expedite the procedures of public tenders and establishment of PPPs
2. Trusts
    - Review the institutional framework regarding public organisations with administrative independence
    - Select cases of initial implementation and specify the method of collaboration with the state

Subsidising demand

Historically, national budget strategies were oriented to subsidising the offer of services and more specifically to subsidising and financing expenditure and public organisations investments. This practice has led to non-efficient use of public resources, which has often reached the verge of wasting public money for the provision of low quality public services compared to the respective services offered by the private sector.

The above practice must change and the state, instead of financing the organisations offering services, to finance the citizens who receive services, providing them at the same time with the opportunity to select their service provider. This model has been applied in Europe and has brought many benefits to the countries adopting it.

At the same time, the state must proceed immediately to the establishment of a regulatory framework which can promote the above structure and facilitate private organisations in the provision of social goods. With these changes, public social policy can focus on providing quality and sufficient services rather than preserving inadequate and financially non-viable organisations, and at the same time the state can reinforce its supervisory role.

Actions

1. Public funding of citizens' expenditure for certain social goods rather than financing the operation of the public organisations providing these goods
2. Develop a regulatory framework to facilitate private sector's activities regarding the provision of social goods

Upgrading state's administrative activity

Using private sector's expertise and practices could contribute greatly to the reorganisation of public bodies. The experience of public sector executives in achieving goals, meeting deadlines, designing efficient procedures and high performance would help change significantly the existing culture and working practices. In the form of an unusual personnel exchange, middle and senior private sector executives could be transferred temporarily to key positions of public organisations, while civil servants could be employed in the private sector. According to this concept, the state should remove restrictions on civil servants' mobility, minimising the possibility of over-staffed or under-staffed public organisations.

The diffusion of the private sector's professional culture into public sector is not restricted only to personnel exchange. The way appraisal and reward of employees is performed in the private sector can create a model for reforming the public sector's employee appraisal system. Linking employee's final reward with the outcome of their work, performing appraisals on a regular basis as well as reinforcing the importance of hierarchy and the sense of responsibility for the outcome are examples of a modern human resources management.

At the same time, public administration executives must acquire the administrative capabilities and behaviours that are necessary for the efficient and effective utilisation of resources for citizens' benefit and the achievement of the country's key strategic objectives. In order to carry the change through, the country will need a strategy for capability management focused on attracting and developing executives who display the required behaviours.

Public administration must establish a strong leadership, which is not determined by election results, as well as hierarchical depth. Some strategic moves for improving public administration are establishing permanent general secretaries in every ministry who will not be appointed by the government and upgrading ministries' general directors' responsibilities.

Outsourcing

The public sector has been using outsourcing in the last years. Such examples are, outsourcing to Chambers the procedures of issuing licenses for establishment and operations for manufacturing units, the provision for the establishment of a register of certified valuators of Environmental Impact Studies, the environmental auditors' register, the use of a certified engineers register for the issue of energy certificates as well as outsourcing tax audit and tax certificates issuing to audit firms.

The advantages of outsourcing derive both from curtailing expenditure as well as adding value to citizens/companies receiving the services. Moreover, outsourcing contributes to economic growth in general as private suppliers/providers can operate free of public sector's restrictions and are able to expand their services and the geographical coverage of their activity beyond the boundaries of their current area of operation (city, region).

Actions

1. Staff secondment, for a limited period of time, from public administration to the private sector and vice versa.
2. Central administration of public administration's human capital and balancing needs and demand
3. Target setting, appraisal and reward of officers occupying responsible positions based on outcome
4. Fixed administrative structure and non-politically based appointment of personnel
5. Outsourcing
    - Predetermining key public sector services that can be outsourced to third parties/providers
    - Determination of a mechanism for singing the relevant agreements and monitoring and auditing the quality of the provided services
    - Developing outsourcing standards (standard contracts, payment methods, partnership conditions etc.)

7. Changing the game

For growth to be fuelled in Greece trust must be rebuilt Without that trust, Greece will have to proceed to the forthcoming economic recovery period without external funds , confronting increased difficulties and losing any competitive advantages it has managed to preserve.

Directing capital to only two areas of activity and to large scale investments rather than allocating it to many smaller opportunities is the first step in order to upgrade connection with markets. Infrastructure and tourism are linked to the country's comparative advantages and, due to their strong multipliers, they can rapidly stimulate growth into the rest of the economy.

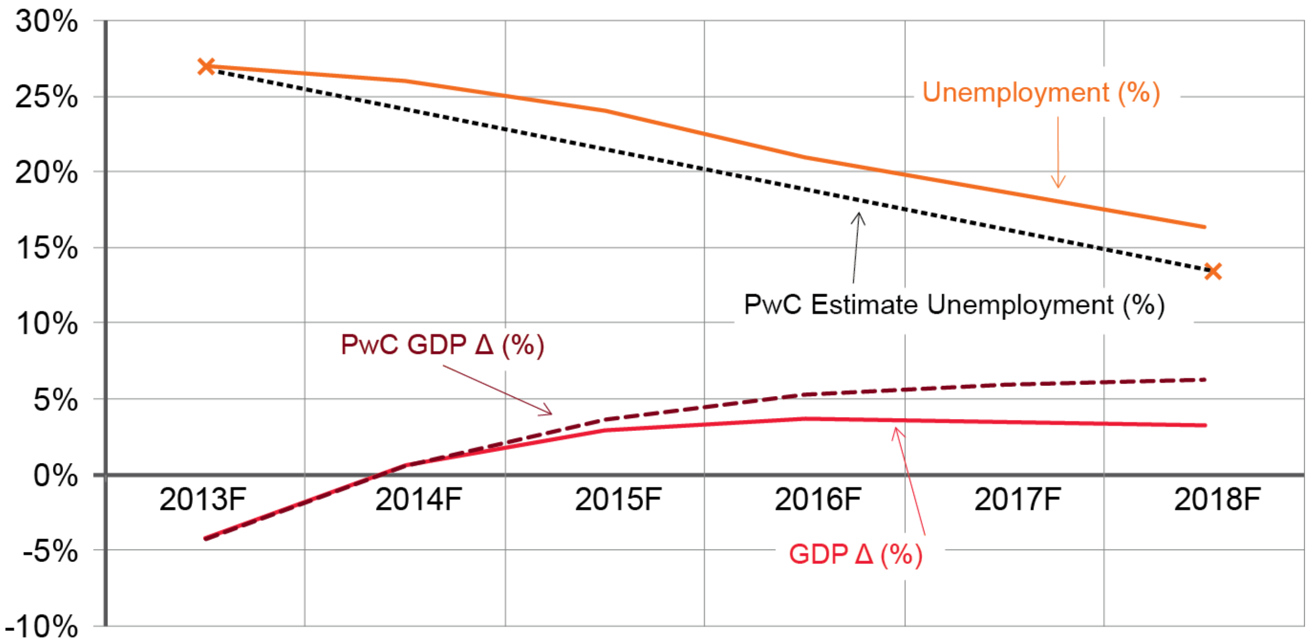
Particularly as far as tourism is concerned, **upgrading activity scale** both in real estate, through special REITs, and in the provision of hospitality services, through the establishment of management companies, is considered as prerequisite for the improvement of their finances and, as a consequence, for attracting capital.

The effective utilisation of the capital originating from European Union's structural funds requires **the fundamental change of their allocation philosophy**, from grants to loans and from public to private management of the investment process. These capitals are crucial for co-funding investments in a way that improves the investors' risk/reward ratio.

Releasing assets from bank balance sheets will attract significant capitals creating a secondary investments cycle, in the economy as a whole. This will send a message to international investors whose presence will build up trust in the country and will provide liquidity.

Lastly, **public sector's** and management philosophy must change fundamentally. The clear segregation of central government and the state's business activities is a prerequisite for building trust. The same goes for upgrading the administration of the narrow public sector and reducing the remaining business activities, after assigning as many as possible to the private sector.

This simple strategy can attract as much as EUR 45 billion of investments in the next ten years. By virtue of infrastructures' and tourism's strong multipliers, GDP will be reinforced with EUR 8 billion annually with a corresponding increase of the taxable amount and taxes by at least EUR 3 billion annually, while 140,000 new stable job positions will be created.



Source: ELSTAT, Bank of Greece, International Monetary Fund, Ministry of Finance

In order to achieve these significant changes and realise this strategy, the political agenda must be shifted :

- from debt containment to development reducing debt to increasing economic activity
- from publicly funded consumption to privately funded investment
- from a slow, investment inhibiting and complex public sector to a relevant and business facilitating State

If we manage to commence the process of change at a political level, then we will be able to regain the lost trust and mobilise a virtuous circle of growth. There is not much time left and as the Ancient Greeks said: **"time waits for no man"**.

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