



BLACK SEA TRADE AND DEVELOPMENT BANK

GREECE

Country Strategy

2011-2014

DRAFT for BoD
THESSALONIKI
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GREECE COUNTRY STRATEGY

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Table 1: Basic Macroeconomic Indicators at a GlanceCountry Long Term Foreign Currency Sovereign Risk Rating at 1 February 2011: **S&P: B** | **Moody's: Caa1** | **Fitch: B+**

No.	INDICATOR	2007	2008	2009	2010	2011	2012	2013	2014
1	Population (mid-year; million)	11.11	11.14	11.16	10.99	11.00	11.00	11.00	11.00
2	Average exchange rate (Euro/USD)	0.73	0.68	0.72	0.75	0.80	0.83	0.85	0.86
3	Inflation rate (CPI Avg.; %)	2.9%	4.2%	1.2%	4.7%	2.9%	n.a.	n.a.	n.a.
4	Average monthly earnings (USD)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
5	GDP at current prices (EUR bn)	225.54	235.68	233.05	223.09	226.11	230.36	234.96	242.35
6	GDP at current prices (USD bn)	308.69	345.23	323.75	295.88	282.63	276.43	277.25	281.12
7	GDP / capita (in crt. prices; USD)	27,779.74	30,998.34	29,006.87	26,922.27	25,693.86	25,130.29	25,204.26	25,556.59
8	Real GDP growth (%)	4.3%	1.3%	-2.3%	-4.5%	-3.5%	0.8%	1.2%	1.6%
9	Unemployment rate (ILO definition; eop; %)	8.3%	7.6%	9.5%	11.5%	14.5%	15.0%	14.2%	13.9%
10	Industrial output growth (%)	2.3%	-4.0%	-9.4%	-1.6%	1.3%	1.7%	1.8%	1.8%
11	Agricultural output growth (%)	-10.8%	1.5%	2.4%	0.4%	0.4%	0.4%	0.4%	0.4%
12	Remittances - Current transfers, net (USD m)	2,121.63	4,179.56	1,657.26	2,529.00	2,133.00	1,810.00	1,538.00	1,278.00
13	Direct foreign investment (USD m)	1,958.71	5,303.57	2,419.30	2,299.00	2,253.00	2,230.00	2,297.00	2,412.00
14	Consolidated budget balance / GDP (%)	-6.7%	-9.6%	-15.4%	-10.5%	-7.4%	-6.0%	-2.9%	-2.3%
15	Gross external debt (EUR m)	308,539.11	362,587.00	407,859.00	n.a.	n.a.	n.a.	n.a.	n.a.
16	Gross external debt / GDP (%)	136.8%	153.8%	175.0%	n.a.	n.a.	n.a.	n.a.	n.a.
17	Goods: Exports (f.o.b.; USD m)	23,991.40	29,162.70	21,361.40	20,979.00	22,861.00	25,143.00	24,858.00	25,573.00
18	Goods: Imports (f.o.b.; USD m)	-81,041.20	-94,209.00	-64,197.30	-47,458.00	-34,548.00	-27,122.00	-22,453.00	-21,587.00
19	Trade balance (exp. f.o.b. - imp.f.o.b.; USD m)	-57,049.80	-65,046.30	-42,835.90	-26,479.00	-11,687.00	-1,979.00	2,405.00	3,986.00
20	Trade balance / GDP (%)	-18.5%	-18.8%	-13.2%	-8.9%	-4.1%	-0.7%	0.9%	1.4%
21	Current account balance (USD m)	-44,587.30	-51,312.80	-35,912.60	-18,287.00	-3,820.00	12,134.00	15,442.00	16,119.00
22	Current account / GDP (%)	-14.4%	-14.9%	-11.1%	-6.2%	-1.4%	4.4%	5.6%	5.7%
23	Forex reserves (excluding gold; eop; USD m)	631.10	343.79	1,554.81	n.a.	n.a.	n.a.	n.a.	n.a.
17	Goods: Exports (f.o.b.; USD m)	23,991.40	29,162.70	21,361.40	20,979.00	22,861.00	25,143.00	24,858.00	25,573.00
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Sources:

Data for items 1-2, 12-13, 17-18, 21, 23 from IFS, IMF, January 2011

Data for items 3, 5, 8-9 from National Statistical Service of Greece

Data for items 10, 15 from Bank of Greece

Data for item 11 from EIU Country Reports

Data for item 14 from Eurostat

Data for items 12-21 for 1998 from IMF Country Report No. 01/57

I. Recent Economic Developments and Outlook

a. Real Sector Developments and GDP Dynamics

From 2000 to 2008 Greece has continued its run of sustained economic growth, whose acceleration dates back to 1994. Even after the 2004 Olympics held in Athens, despite a contraction of public investment, the Greek economy continued to grow robustly during 2005 -2007 with real GDP growth averaging 4%. These rates were among the highest among Eurozone member countries of the European Union (EU), well above the average growth in the Eurozone.

However, in the post Olympics period such rapid growth appears in retrospect to have been driven mainly by unsustainable foreign financed domestic consumption. Investment dropped starting with 2005, as did industrial and agriculture output, while gross external debt approached the 100% of GDP line as early as 2004. At the same time, the government sought to finalize projects co-financed by the EU under the Structural Funds of the Community Support Framework and Grants provided through the Cohesion Fund. Over the period 2004-2008, the changes that took place in the EU and national economy combined to reduce potential GDP growth from 4% to just 1%, according to estimates by the European Commission, and the sustained rapid growth above potential contributed to higher inflation than EU average, which in turn over time eroded the competitiveness of the economy.

Greece has an open economy in which the state plays a major role, with a small, rigidly structured and conservative private sector dominated by family owned firms. About 50% of the labor force is employed in the public sector, either directly or in state owned enterprises. In terms of sectors, services continued to drive growth and increased as a share of the economy, while agriculture has largely remained marginal and industrial output has been stagnant. Up to 2008 agriculture's contribution to GDP has declined over the years to account for roughly 5% of GDP, while industry remained relatively limited in size contributing approximately 20% of GDP, one of the smaller shares in the EU. Construction has been buoyant up to 2008, contributing about 9 to 10% of GDP formation. Services (including construction) account for nearly 75% of GDP formation and have increased steadily over time.

Following the near collapse of global financial markets in 2008 and the subsequent freezing of financial markets throughout the world, the Black Sea region fell into economic recession which deepened through 2009. While the situation stabilized in the second half of 2009 in most countries of the EU, and of the Black Sea region, the Greek economy continued to contract. The country was effectively cut off from the credit market, while simultaneously suffering successive rounds of credit risk downgrades. Industrial output suffered a severe contraction, while the construction sector suffered an outright collapse. GDP declined by 2.3% in 2009 and 4.5% in 2010. It is expected to fall further by 3.5% in 2011, due to aggressive implementation of structural adjustment measures and further fiscal consolidation, and to stagnate in 2012 before starting to accelerate from 2013 onwards.

b. Public Sector Policy and Fiscal Position

Greece has suffered for an extended period from pervasive public sector inefficiencies and budget overruns, and in spite of significant revenues of about 40% of GDP, large budget deficits added to weak foreign trade outcomes to result in significant foreign borrowing required to fill such financing needs. Although in the period following the adoption of the Euro excessively low interest rates, abundant liquidity and high rates of GDP growth helped finance deficits with ease, Greece has also attempted in the past to reign in its deficits but such efforts proved to have been time bound and had limited results. The Government's fiscal audit during 2004 triggered a review of Government

expenditures by the Eurostat, and finally resulted in revisions to fiscal figures going back to 1997. As a result of these revisions, the general Government budget deficit was re-calculated at a higher level relative to the original figures peaking at 7.7% of GDP for 2004.

The Government embarked upon a stabilization program, with curtailment of general public spending growth and rationalization of off balance sheet accounting. On the revenue side, efforts to combat widespread tax evasion and improve revenue collection were accompanied by value added tax increases, including for new construction, and by the introduction of presumptive taxation for sectors of the economy in which evasion was rampant (particularly for the self-employed). However, notwithstanding above mentioned measures, the informal economy remained sizeable, at an OECD estimated 30% of GDP, and therefore there is additional scope for revenue enhancement via anti-tax evasion measures.

In spite of such measures, budget deficits continued to widen from 2006 onwards. Successive revisions of public finance statistics during 2009 and 2010 each resulted in larger amounts. On the 15th of November 2010 Eurostat published a final upwards revision of Greece's budget deficit and debt figures for 2006-09. The budget deficit in 2009 was increased from 13.7% of GDP to 15.4% of GDP. The government recorded a primary deficit of an estimated 8.9% of GDP in 2009, but this figure is likely to be also revised upwards following Eurostat's increases of deficit and debt figures for 2006-09.

In 2010 net ordinary budget revenue increased by 5.5%, compared with a target of 6%. Ordinary budget expenditure, however, shrunk more than anticipated, by 9.1%, versus a target of 7.5%. The deficit in the public investment budget shrunk to €5.4bn, a reduction of 28.8%, and the primary deficit to €6.4bn, a decline of 65.5%.

Fiscal indicators (% of GDP)	2006^a	2007	2008	2009	2010	2011^e
General government revenue	39.5	40.4	39.8	37.8 ^b	37.8	37.7
General government expenditure	45.2	46.8	49.2	53.2 ^b	47.6	45.8
General government balance	-5.7	-6.4	-9.4	-15.4 ^b	-9.7	-8.1
Public debt	106.1	105.0	110.3	126.8 ^b	143.5	155.9

e = estimated

As a result of such unsustainable deficits, a public debt in excess of 120% of GDP due to pick at between 145-155% of GDP in late 2012 early 2013, and a sudden and abrupt increase in the cost of borrowing, the Greek government embarked on an unprecedented fiscal consolidation program. The program, supplemented by far reaching structural adjustment actions taken in the product and labor markets, is aimed at bringing the budget back into balance by 2014 through a combination of revenue enhancement and expenditure rationalization measures, stabilization of public debt, and modernization of the economy, which together would create conditions for return to rapid and sustainable economic growth starting with 2013.

In 2010, due to the implementation of strict and far reaching reforms, Greece has recorded extraordinary results, which pave the way to further reforms in the coming years and return to balanced and sustainable growth. Greece implements the Economic Policy Program, the most ambitious fiscal and structural reform agenda in the history of the Eurozone. It is based on unprecedented determination to deliver results, and it includes measures to change and reform structures and institutions through timely implementation of major reforms such as pension reform, labor market reforms and opening-up closed professions. In addition the program is aimed at removing obstacles and providing incentives to release the full potential of the Greek economy.

The measures undertaken include:

- Reduction of ordinary budget expenditures by 9.1% year-on-year (against a targeted reduction of 7.5%). Primary expenditures decreased by 10.9%, against an estimated 9% annual decline.
- Introduction of wage caps, reduction of overtime costs and of short-term contracts, and implementation of a 1:5 hiring replacement ratio.
- Public sector wages were cut by 15% on average in 2009. Further reductions amounting to 7% were adopted in 2010 through elimination of vacation bonuses.
- Restructuring of loss-making public enterprises, including Hellenic Railways, with a 15% wage reduction in all state-owned companies.
- Adoption of the Fiscal Management and Responsibility Act introduced expenditure ceilings and improves budgetary oversight.
- Implementation of local and regional administration reform reduces municipalities from 1000 to 325. The law aims at generating productivity gains and total fiscal savings of the order of €1.5 billion over 3 years.
- Establishment of an independent Hellenic Statistical Authority (in cooperation with Eurostat).
- Overhauling the tax framework to facilitate tax compliance and fight tax evasion.
- Passage of a new anti-corruption law that obliges all public expenditure to be published online.
- Creation of a 'Fast Track' legal framework to attract and expedite large-scale investments. Includes tax incentives, cutting red tape in licensing procedures, a stable tax environment with an 8-10 year horizon, and an investment program worth €4 billion.
- Reduction of corporate tax rate on non-distributed profits from 24% to 20%.
- Adoption of the new Real Estate and Asset Privatization Programme which will generate €7 billion through sales and privatizations from 2011-2013.
- Relaxation of product market regulations, lifting barriers to entry in services, and opening up closed professions will boost Greece's output by an estimated 5 to 6% of GDP.
- Liberalization of the energy sector to boost competition and encourage investments in renewable energy.
- Opening of closed professions - road freight transports, pharmacies, lawyers, notaries, architects, engineers, accountants etc - to enhance competitiveness and promote growth.
- Adoption of the Greek pension system reform. It includes a rise in the retirement age to 65 by 2013. The pension reform will considerably reduce future spending pressures, with expenditure to increase by no more than 2.5% of GDP up to 2060.
- Adoption and implementation of labor market reforms, which revise the mediation and arbitration system, introduce the prevalence of firm-level labor contracts agreements, introduce sub-minima to minimum wage, raise the minimum for collective dismissals, reduce the level of severance pay and allows more flexible forms of employment.
- Creation of a €10 billion Financial Stability Fund to provide rules-based equity to the commercial banking sector.
- Strengthening of the Central Bank's supervisory role, covering both commercial banking and the private insurance sector.
- Application of quarterly stress-tests and promotion of restructuring of the Greek banking system.

On January 20th 2011 the government published central government budget results for 2010. The immediate 2010 results of these measures include:

- 6 percentage points of GDP reduction in consolidated budget deficit in 2010, the largest fiscal consolidation by any country in EU history in one year
- 37.0%/y/y decline in state budget deficit (exceeding the targeted reduction of 33.2%)
- 66.4% y/y reduction in state budget primary deficit
- 5.5% Net revenue increase
- The government has left unchanged its estimate deficit of 9.4% of GDP for the general government deficit (according to the ESA95 system of accounts).

The 2011 budget targets a significant further reduction in ESA95 deficit next year to 7.4 percent of GDP from the 9.4 percent outturn the government now projects for 2010. The draft budget assumes real GDP declines a further 3 percent. The cash revenues of the budgetary central government are projected to increase by 9 percent in euro terms, boosting them by 2.6 percent of GDP. In part, this should reflect the full-year effects of hikes in indirect taxes carried out in 2010. Noninterest expenditures are targeted to decrease in line with GDP, with outlays on wages and healthcare reduced by 7 percent thanks to employment reductions and the abolition of the Easter bonus. Nonwage consumption spending is to be cut a further 10 percent as strict expenditure caps are implemented and the contingency reserve introduced this year is sustained and reinforced. Pension expenditures will fall with the elimination of the Easter bonus, a nominal freeze again on pensions and further cuts in higher-end pensions, all of which should enable budget transfers to the social security funds to be cut another 5 percent in nominal terms. These measures should be sufficient to increase revenues and reduce spending by another 3¾ percent of GDP in 2011. The general government deficit would narrow to 5.8 percent of GDP on an ESA95 basis, assuming no improvement in tax collection; tax compliance, however, should continue to improve.

c. Monetary and Financial Sector

Monetary policy & Inflation

Greece entered into the European Monetary Union (EMU) in 2001 and adopted the Euro in 2002. This resulted in the loss of sovereign control over monetary policy, as monetary policy for the Eurozone countries is conducted by the European Central Bank (ECB). Because the ECB is controlling monetary aggregates only at Euro-area level, there is no fine tuning mechanism to address specific problems of individual countries. Therefore, paradoxically, Greece has been in the position of having one of the highest inflation rates of Euro member countries, while simultaneously ‘enjoying’ an expansionary monetary policy at real negative rates of interest that in turn fueled credit expansion and created inflationary pressures which made more difficult the reduction of inflation domestically, and the conduct of economic policy more generally. This vicious circle, together with accommodated wage increase pressures, reduced domestic competitiveness and aggravated both internal and external imbalances.

The ECB’s central objective is to maintain the Euro's purchasing power and thus price stability in the euro area, and its basic tasks include the implementation of monetary policy for the Euro area; the conduct of foreign exchange operations; the holding and management of the official foreign reserves of Euro area countries; and the promotion of the smooth operation of payment systems¹. In addition, in response to the financial and economic crisis, and due to the absence of a cohesive EU mechanism for

¹ See ECB tasks and objectives at: <http://www.ecb.int/ecb/orga/tasks/html/index.en.html> .

dealing with financial stability or with common economic governance, the ECB has undertaken reactively and on a limited scale actions in this direction as well.

Since May 2009 the ECB refinancing rate has remained at a record-low 1%, and since the start of the crisis ECB implemented a program of "enhanced credit easing", offering unlimited cheap liquidity to the banking sector. Given the need to contain the still threatening prospect of a sovereign debt crisis, which has made it difficult for some banks and countries to access liquidity in the credit market, the ECB provided support by refinancing banks in exchange of member states bonds as collateral irrespective of their risk rating.

In early 2010 the ECB also took the decision to buy bonds of Euro area member states. It stepped up these purchases in late 2010 in an effort to allay contagion fears and now faces the prospect of extending central bank support for as long as liquidity and solvency concerns persist, or until an alternative better suited mechanism is established.

Banking Sector & Capital Markets

The Greek banking system is highly concentrated, as the top five banks hold approximately two-thirds of all assets, deposits and loans. Of these, one is state controlled- the National Bank of Greece (NBG), three are established private banks- Alpha, EFG Eurobank and Piraeus Bank- and one Emporiki (Commercial) Bank is owned by the French Credit Agricole Bank. Since 1st of January 2005 banks are required to use International Accounting Standards.

Over the period leading to the crisis, bank competition has intensified resulting in squeezed margins and shift in focus away from domestic corporate customers to the retail market. Growth rate of household credit ranged between 20% and 40% a year, with mortgage lending, consumer lending, and credit cards growing rapidly. In addition, Greek banks expanded abroad, into the Balkans, the Mediterranean and the Middle East.

The crisis had a severe impact on the Greek banking system, but banks were able to withstand the initial shock. In 2010, large-scale deposit outflows of nearly 11 percent of the deposits held at the beginning of the year brought the banking system under severe strain. Foreign interbank lenders and depositors withdrew during January-October about 20 percent of banks' foreign liabilities existing at the start of the year. The situation stabilized starting with August.

During the period deposit outflows and foreign debt repayments were more than offset by large-scale liquidity support from the central bank, drawings on assets held abroad by domestic banks, unguaranteed bond issuance and drawdowns on excess reserves held with the central bank. Liquidity provision by the central bank was financed in turn via refinancing from the ECB. ECB funding has been facilitated by the issue by banks of government-guaranteed bonds and the provision of "special bonds" by the government to banks (in exchange for real estate and other collateral) under the liquidity support program set up in late 2008. This financing was sufficient to support a modest expansion of credit to the non-government sector.

However, notwithstanding abundant liquidity support from the government and the ECB, and despite beginning this year with relatively solid financial positions, deteriorating credit quality has weakened most domestic banks. Nonperforming loans rose to 9 percent of the total at the end of June from 7.7 percent at the end of 2009 and 5 percent at the end of 2008. The aggregate Tier 1 capital ratio for the system as a whole fell to 11 percent from 12 percent at the end of 2009.

Stress tests published in July by the central bank and the Committee of European Bank Supervisors for the six largest banks found that, with respect to Tier 1 capital, all six surpassed both the regulatory minimum of 4 percent and the stress test benchmark of 6 percent set in the baseline scenario.

By comparison with the banking sector and with the other EU-15 countries, the Greek insurance industry is insufficiently developed, with a very large number of small players. Its weakness has been shown by the difficulties faced by many companies to meet new solvency margins imposed by EU directives. A number of insurance companies were liquidated.

The Athens Exchange (Athex), the main stock market, was formed in 2002 through the merger of the Athens Stock Exchange (ASE) and the Athens Derivative Exchange. In December 2005 Athex restructured as a three-tier market: a large-cap board, a mid/small-Cap board and a special characteristics market for shares that do not fit elsewhere. It is regulated by the independent Capital Market Commission, which operates under the authority of the Ministry of Economy. Although some progress has been achieved in recent years, the Athens Stock Exchange is still marginal to the financial sector and is plagued by excessive volatility.

d. External Sector

Debt

Although one of the convergence criteria for entry into EMU was that public sector debt should be below 60% of GDP, it was applied with great flexibility and restated as ‘public debt should be declining towards 60% of GDP’, because certain EU members in the original establishment of EMU were well above this threshold, most notably Belgium and Italy. Greece qualified under the same restatement, since public debt was around 100% of GDP already at the time of adoption of the Euro.

Alongside the budget figures, debt figures were also altered following the 2004 fiscal audit, and revised upward by approximately 10% of GDP, peaking at 108.5% of GDP for 2004. The revision of government finances by the Eurostat in 2010 had the same result, of an upwards restatement of debt figures going back to 2006.

In late 2009 revelations of budget deficits in effect about three times larger than initially expected ignited panic. Credit markets were faced with the specter of sovereign debt crisis, not only in Greece but across the EU peripheral small and open economies. Although Greece represents only about 2% of EU GDP, there were immediate concerns about contagion risk. And these risks were not necessarily triggered by the interconnected position of Greece, but by the acknowledgement that the problem is wider, potentially systemic, and that other nations are caught in the same loss of competitiveness and foreign financed domestic consumption led growth.

The BIS international banking statistics show that the total consolidated foreign claims of BIS-reporting banks on Greece amounted to US\$298.3 billion as of September 30, 2009 (24 countries, on an ultimate risk basis). Of these, the claims of European banks on Greece were US\$272 billion. On a country-by-country basis, French and Swiss banks appear particularly exposed to Greece with claims exceeding US\$78 billion each. German banks follow, with claims of US\$43 billion. Moreover, the breakdown by sector shows that all BIS-reporting banks held aggregate foreign claims of US\$115 billion on the Greek public sector, US\$50 billion in interbank claims and about US\$132 billion on the non-bank sector. ECB statistics show that, as of February 2010, Greek banks held €96.9 billion in external assets and external liabilities of €64.1 billion.

However, among the peripheral Eurozone members Greece holds the smallest total debt (public and private) and represents the most isolated problem, from the systemic risk perspective. Because the Greek debt is mostly public, Greece is the country where an adjustment program is likeliest to succeed.

Consequent to the above, Greece entered into an agreement with the EU and the IMF for a structural adjustment program supported by a EUR 110 billion financing package, to disburse in tranches up to 2013. The majority of the IMF/euro zone lending facility comprises bilateral loans that are offered at an interest rate of around 5.2%. Although this is significantly lower than the rate that would otherwise be available in the market, it remains higher than the cost of borrowing for other similarly rated countries, and certainly higher than what the economy could afford given its growth prospects. Currently there is a three-year grace period, and loan repayment is required in the two years thereafter, but recent discussions in Brussels – confirmed by the IMF – indicate the likely possibility of an extension of the repayment over a revised extended period of 10 years.

The Eurozone leaders and Ecofin, together with the Commission, IMF and the Greek Government consider a new assistance program, which may be finalized shortly, which would provide Greece with the liquidity needed to repay maturing debt and to postpone accessing the markets until after 2014. In the meantime, the Greek Government is expected to adopt and implement substantial structural reform and a set of measures aimed at further fiscal consolidation, including an ambitious privatization plan.

Trade and the Current Account

Greece consistently runs large deficits on the merchandise trade balance on the order of 15-16% of GDP, with exports amounting to about one-third of the value of imports. The situation deteriorated in 2007 and 2008, with the trade balance showing a deficit of over 18% of GDP. There are structural reasons for this deficit, including (i) real exchange rate appreciation (and absolute lack of any possibility of devaluing the currency to support export competitiveness) caused by cost increases in the Greek economy, high inflation and the appreciation of the Euro, (ii) the service orientation of the Greek economy in which tourism and shipping are the critical economic sectors earning foreign income, while the quasi totality of goods is imported, (iii) acceleration in consumption created by remittances and cheap and abundant foreign credit, and (iv) the high dependence of Greece on energy imports.

As a result of the trade deficit, Greece also runs high current account deficits, which reached 7.9% of GDP in 2005 and increased thereafter to reach 14 to 15% of GDP in 2007 and 2008. The difference between the trade and current account deficit is mainly due to the positive impact of services balance surpluses in the tourism and transportation. The largest component of the income balance is EU transfers to the Greek government, which decreased during 2006., and are likely to be lower in the next period up to 2013.

e. Forecast for 2011-2014

In the period ahead, the budget deficit may narrow to 5.8% of GDP in 2011, 3.5% in 2012 1.5% in 2013. Fiscal adjustment measures totaling 17% of GDP from the start of 2010 through 2013 are intended to assure the eventual reduction of the fiscal deficit to less than the 3 percent of GDP Maastricht limit, and the attainment of a balanced budget by 2014.

Import volumes should contract substantially as a result of further contractions in real GDP in 2011 and decreases in domestic demand as household spending declines further and decreases in

government consumption are sustained. Imports will contract in 2011 and further in 2012, before stagnating in 2013 and growing weakly in 2014. Improvements in competitiveness as labor costs decline, renewed GDP growth, and recovery in foreign demand on the other hand, should boost export growth. In 2010 exports recorded a positive rate 3,8% and imports fell significantly by 4,8%. Regarding the medium-term macroeconomic prospects export growth is projected to be 6,6% on average during the 2011-2015 period and low import growth by 0,1% on average is expected during the same period. The shipping industry in particular will be buoyed by improved global economic conditions in 2013-15. Tourism earnings should also recover. Coupled with improved utilization of EU structural funds, these factors should bring the current account into surplus by 2012.

The heavy emphasis put on structural reforms by the government, the EU, the IMF and the ECB are proof of the strong hopes that accelerated growth will stabilize the government debt relative to GDP, would enable debt servicing, and would facilitate bringing steady declines in debt to GDP ratios from 2014 onwards.

Furthermore, the Economic Adjustment Program adopted in May 2010 aims to achieve:

- front loaded fiscal consolidation to reduce the deficit and to administer the public debt on a sustainable trajectory
- labor market, product market, and business environment reforms to increase competitiveness, and
- a fundamental shift in the growth model to one based on productive investment of goods and services.

The Medium Term Fiscal Strategy 2012 - 2015 is based on the following policy pillars:

- the continuation of the fiscal adjustment effort, in order to reduce the general government deficit below 3,0% of GDP by 2014,
- the implementation of structural reforms which are expected to boost growth and enhance competitiveness, in order to increase the nominal GDP by more than 3,0% in 2014,
- the implementation of a privatization and real estate development program, which will significantly contribute to public debt reduction and will strengthen economic growth prospects.

The EUR 110 billion package from the IMF and the Euro zone is sufficient to cover debt financing needs in 2011-12, but thereafter Greece would need to refinance its debt from the international capital markets.

Disbursements from the EU and IMF are estimated at EUR 32 billion in 2010, EUR 47 billion in 2011, EUR 24 billion in 2012, and EUR 8 billion in 2013. The IMF also estimates that principal payments of medium- and long-term debt to foreign holders of Greek government bonds and other foreign lenders amounts to EUR 23 billion in 2010, EUR 28 billion in 2011, EUR 26 billion in 2012, and EUR 25 billion in 2013. This leaves a gap of at least EUR 17 billion that would need to be refinanced from the market in 2013. In addition, it is estimated that over the same period amortization payments by domestic banks would amount to EUR 25 billion and those by non-financial companies would add at least another EUR 4 billion in debt repayments.

If notwithstanding the above successes doubts about the economy's creditworthiness would persist, ongoing efforts to cut spending and raise taxes will remain essential but might not be sufficient. As growth is expected to pick up from 2013 onwards, stronger efforts might be needed to be taken in 2011 and 2012 to recover most of the estimated 13% of GDP in overdue taxes. Significant potential

also remains to realize sizable sums from the resolution of the unclear status of structures constructed illegally on state-owned land. Realizing this considerable financial potential, together with the sale of some of state owned financial assets, would allow the Government to use the proceeds in order to retire outstanding debt which at current discounts would be equivalent to up to 40% of GDP. A reduction of the outstanding debt by 2014 would regain confidence of market participants and reopen access to financing at acceptable terms and conditions. In addition, would provide opportunities for faster economic growth underpinned not only by public investment, but also by potentially vast foreign direct investment in economic sectors where Greece has an untapped considerable comparative and competitive advantage, like solar and wind energy, extraction and transportation of recently discovered and potentially huge reserves of crude oil and natural gas, health care, entertainment, fish farming and high-end food processing, in addition to the consecrated domains of shipping and tourism.

II. Overview of Current BSTDB Portfolio

Currently the Bank's active portfolio consists of 4 BoD approved operations, for a total of about EUR 72 million, and ranks fourth among Member States in terms of the outstanding amounts.

Table 2: Current BSTDB exposure to Greece in USD

Operation	Date BoD approved	Amount approved	Outstanding amount
Shelman	30-Jul-05	19,875,000	3,312,500
Alumil Syndicated Bond Loan*	7-Oct-09	29,017,500	29,017,500
Velti Corporate Loan	23-Jul-10	19,875,000	19,875,000
Terna S.A.	23-Jul-10	26,500,000	26,500,000

III. Review of Country Strategy 2007-2010

INTRODUCTION

The current evaluation was performed by the Bank's Evaluation Office as per the respective Evaluation Policy. It reveals the performance of the Bank's 2007-2010 Country Strategy for Greece. Its goal is to provide accountability to the Board of Directors and Board of Governors as well as facilitate the decision-making by the Bank's Management and Boards on the eventual update of the country strategies.

The evaluation of the respective country strategy compares the stated targets with results as of end of 2010, and provides a country-oriented analytical picture.

PERFORMANCE OF GREECE COUNTRY STRATEGY 2007-2010

The 2007-2010 country strategy for Greece was approved by the Board of Directors in early 2007, reflecting an in-depth independent evaluation of the implementation of the BSTDB's earlier strategies, conducted by the Evaluation Office in late 2006. The recent country strategy was aligned with the objectives of the Bank's Business Plan 2007-2010 and was therefore evaluated in its overall context.

Overall, the implementation of the Country Strategy is Partly Unsatisfactory, as the achieved volume indicators are in the range of 50-80% of the target, with the sector outreach having corresponding shortfalls, with particular reference to the transport sector. Please refer to the table below for further detail.

Table3

Post Evaluation of 2007-2010 Country Strategy Greece (approved 04.02.2007)				
2007- 2010 TARGETS			RESULTS (end of 2010)	
General	Sectors	Target operations: Number approved/ number signed; USD approved/ USD signed (million)	Actual operations: Number approved/ number signed; USD approved/ USD signed (million)	Evaluation and Prospects
<p>Focus on better implementation, the expansion of operations and cooperation with Greek firms, aiming at more cross-border operations.</p> <p>Make the Bank better known in the Greek marketplace, especially in Athens, and demonstrate the advantages of cooperation with Greek firms.</p>	<p>1. Manufacturing and Transport</p> <ul style="list-style-type: none"> ▪ Restructuring and upgrading of ports ▪ Investment in facilities that were used for the 2004 Olympic games ▪ Expand the involvement in shipping ▪ Road linkages with neighbor countries ▪ Black Sea Ring Highway project ▪ Corporate, multi-purpose loans and participation in syndicated loans ▪ Cooperation with Greek organizations assisting counterpart organizations in other BSEC countries <p>2. Infrastructure, Energy, Natural Resources, Telecommunications</p> <ul style="list-style-type: none"> ▪ Small scale infrastructure ventures that promote cross-border cooperation ▪ Participation with IFIs in oil and gas import/transit infrastructure ▪ Regional electricity markets ▪ Private independent power production ▪ Renewable energy technologies such as wind power and hydroelectric power 	<p>10/8</p> <p>116/99</p>	<p>4*/4*</p> <p>81**/81</p> <p>*(4 were approved but one was removed)</p> <p>** (81m approved/signed of which \$ 6m belonged to the removed project)</p>	<p>1. Volume:</p> <p>Volume: modest</p> <p>Approved number: 40%</p> <p>Approved volume: 70%</p> <p>Signed number: 50%</p> <p>Signed volume: 82%</p> <p>2. Sector coverage:</p> <p>2.1. Alumil (co-financed) (Manufacturing)</p>

	<ul style="list-style-type: none"> ▪ Purchase of telecommunication equipment from BSTDB countries <p>3. Trade Finance and Financial Sector</p> <ul style="list-style-type: none"> ▪ Help Greek financial institutions extend their presence in countries of the region ▪ Co-financing with Greek banks towards Greek corporations' local and/or cross border projects. ▪ Private investment/ equity funds investing in Greece and/or other Member Countries. ▪ SME development 			<p>2.2. Velti (Telecom)</p> <p>2.3. Terna S.A. (Construction)</p> <p>2.4. Ebik (Manufacturing Removed)</p> <p>3. Performance:</p> <p>Partly unsatisfactory: The overall volume and sector underperformance is partly attributed to the recent economic downturn.</p>
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IV. BSTDB Operational Priorities for 2011 - 2014

Government priorities

The priorities of the Government regarding the areas for BSTDB financing, are the support of small and medium enterprises (SME), the operations involving renewable energy sources, as well as the country's strong interest in the increase of PPPs projects and intraregional projects that create synergies for economic development.

The BSTDB will focus in the next four years on providing support for the implementation of the Government program and priorities, while responding to market demand. The Bank will consider undertaking activities and providing services as may advance its purpose, paying special attention to activities promoting export of goods and services, and development of infrastructure and regional development, including energy efficiency, with a focus on SMEs. To this end, the Bank would explore possibilities to cooperate with the specialized Government agencies and to participate in the JESSICA – Joint European Support for Sustainable Investment in City Areas – initiative of the European Commission in cooperation with the European Investment Bank (EIB) and the Council of Europe Development Bank (CEB), in order to promote sustainable investment, support economic growth and help create jobs. In addition, the Bank will support Government initiatives which promote regional development and cooperation between Greece and other BSEC member countries.

Areas for BSTDB Financing

The changing conditions, characterized by increased risk aversion and tightening of the credit markets, provide confidence that over the coming years financing provided by BSTDB will be in higher demand. The increased attractiveness of Bank funding and the greater capacity of the Bank to respond to clients' needs are an expression of the risk rating upgrade to A3 by Moody's, and of the doubling in the subscribed capital of the Bank. BSTDB would be in a position to offer qualifying clients larger amounts for longer maturities at suitable interest rates. In order for this potential to materialize, the Bank would need to continue to enjoy the strong support of shareholders, demonstrated in particular by payment of the capital subscriptions in due time.

BSTDB will strive to mobilize both foreign and domestic financial resources for investments in Greece. In this respect the Bank will explore co-financing possibilities with other MDBs and DFIs, in particular those who hold observer status in the Bank, involving financing facilities, guarantees, or in any other adequate ways. For operations undertaken in Greece, the Bank would focus on regional cooperation aspect of its mandate, but also would seek to extend assistance to SMEs and also to finance projects in the public and the private sectors which are relevant for the government's development objectives.

The Bank's role and priorities are defined (i) in accordance with the priorities and targets laid out in its *Medium-term Strategy and Business Plan 2011-2014* and (ii) country needs and objectives, as well as (iii) available resources, strategies and policies of BSTDB. In this respect, BSTDB will seek viable opportunities and will continue closely monitoring the developments in the Greek economy in order to stand prepared to support bankable projects in all sectors pertaining to the Bank's field of action. In addition the Bank shall seek co-financing opportunities with IFIs, public sector institutions and private partners.

Based on the 2011- 2014 BSTDB Medium Term Strategy and Business Plan (MTSBP), the Bank would expect to approve about 4 new operations per annum during this period, for approximately EUR 47.3 million per year. Over the four year period, this implies around 14 to 18 approved operations for approximately EUR 166.5 million to EUR 212 million. This scenario would involve a substantial expansion of activities in Greece during the 2011-2014 period. With the Bank determined to raise the level of commitments (signed operations) to approved operations to over 85%, the Bank expects signings for 2011-2014 to be on the order of 13 to 16 operations for EUR 167 million (a range of EUR 147 million to EUR 187 million).

These indicative targets are based on the Base Case Scenario of the MTSBP, and given appropriate circumstances and sufficient operational opportunities the Bank would make efforts to exceed this level. In case of higher regional economic growth rates, increased demand for Bank funding, and an improved situation in financial markets, a phased increase in the average number and size of operations would allow the Bank to move towards achieving the targets envisaged under the High Case Scenario. Moreover, at the Mid-Term Review, depending upon performance and prospects, the above targets may be revised upwards².

The scenario presented above would involve a substantial expansion of activities in Greece during the 2011-2014 period, which would build upon the recent increase in the Bank's portfolio in Greece. The Bank will need to make a substantially greater effort to introducing itself to Greek firms and financial institutions, particularly those which are also active in other BSTDB Member Countries.

BSTDB Financial Sector Strategy

Similarly to its strategy with Greek manufacturing firms, in dealing with Greek financial institutions, the Bank's strategy will seek to help them extend their presence in countries of the Region and support them in efforts to establish and enhance relationships with other financial institutions active in the Region. Such work may take place either via the parent bank headquartered in Greece, or via the subsidiary, local branch, or otherwise related financial institution operating in other Member Countries.

As far as small and medium enterprise (SME) development is concerned, any activities considered by the Bank will seek to capitalize upon the existence of EU programs to support SME development in Greece.

Overall plans are to consider possible provision of loans to Greek banks to facilitate support of their subsidiaries in other BSTDB Member Countries and to evaluate opportunities to participate in equity funds to support local SMEs in cooperation with EU structures

Manufacturing and Enterprise Sector

Greece is currently undergoing a strict austerity program in line with the implementation of the fiscal and structural reforms agreed under the EU-IMF program.

The overwhelming majority of Greek companies have traditionally been highly leveraged with short-term loans constituting a larger part of their total borrowings. The economic recession resulted in

² Under no circumstances would targets be revised downwards unless the lower case scenario of the 2011-2014 BSTDB Business Plan were to be followed.

the reduction of sales and profitability of operations of the Greek general industries. The commercial banking sector reduced its lending activities and the interest rates had demonstrated a pronounced trend to growth.

Under the circumstances above most of the Greek businesses are now in need of restructuring of their short-term indebtedness to the financial sector. During the next years the Bank will undertake steps to identify and support Greek companies that have good capabilities and prospects to restructure their operations, increase their competitiveness and prepare themselves for expansion once the world economy comes out of the recession. The main product which matches this objective is mid- and long-term corporate loans to Greek companies that require restructuring of their short-term indebtedness to the local financial sector. The Bank will also attempt to participate in syndicated loans arranged by Greek and international commercial banking institutions.

The Bank shall be seeking its participation in greenfield investment projects implemented by both Greek and foreign companies in the sectors of the general industries and transport. BSTDB shall be offering project debt and equity financing in this area.

BSTDB will be working with Greek companies that implement investments in other countries, members of the Bank. Such projects ideally correspond to the political mandate of BSTDB and constitute priority for the Bank's operations.

BSTDB Project Finance Strategy – Infrastructure, Energy, Natural Resources, Telecommunications

Generally, there are limited opportunities for BSTDB to finance infrastructure projects, as most of them are financed by EIB and EU funds, which can be mobilized on a far greater scale and more cheaply- including in grant form. The Bank will work in cooperation with other IFIs and commercial banks in joint energy and infrastructure sector projects as an important source of institutional knowledge transfer.

However, the Bank will seek to participate with other international financial institutions in projects focusing on the development of oil and gas import and transit transportation infrastructure, especially components of operations which contribute to the development of cooperation with energy rich regional neighbors. Greece is seeking to become an energy hub for transport in the Region, and in this context, the Bank will follow and seek added value involvement in projects under discussion such as the Burgas-Alexandroupolis Oil Pipeline, gas storage projects, and gas pipelines connecting Italy, Greece and Turkey as well as one being considered between Greece and Albania.

The Bank will also seek more actively to support the development and upgrading of regional electricity markets. On the transmission side, this may involve participating in projects entailing reinforcement of power transmission infrastructure, especially the interconnection with neighboring BSEC Member Countries. On the generation side, the Bank will seek opportunities to work with private Greek groups interested in becoming involved in independent power production schemes. The Bank will be especially keen to participate in operations involving renewable energy technologies such as wind, solar power and hydroelectric power, as this is an area of increasing priority for Greece, for which a number of major projects are scheduled.

Limited opportunities in the telecommunications sector may exist in helping to finance the purchase of equipment from other Black Sea Countries. There may also be favorable prospects to work with Greek telecommunication and telecommunication equipment firms which have been very active in the BSEC region, particularly as neighboring countries open their market and permit the entry of new competitors.