



HELLENIC REPUBLIC  
MINISTRY OF ECONOMY AND FINANCE  
GENERAL ACCOUNTING OFFICE

# GOVERNMENT BUDGET REPORT

# 2006

## Executive Summary

ATHENS, DECEMBER 2005

## I. Overview of the Greek economy

2005 was a fiscal turning point for the Greek economy, since it was the fiscal year during which the government tried to increase domestic demand to sustainable levels of growth, especially after the elimination of outlays associated with the Olympic Games which had a positive impact on domestic economic activity over the previous years.

The ongoing curtailment of public expenditure aims at the further reduction of government deficit, which leads to deceleration of domestic demand. The aforementioned economic policy mix contrasts the expansionary fiscal policy of previous years, resulting in increased government deficits and debt.

In addition, economic growth of 2005 is negatively influenced by external factors such as the unexpected increase in oil prices and the erosion of the positive economic impact of interest rate decrease over previous years.

Despite the above-mentioned impacts, the Greek economy has maintained a robust growth of 3.6% which is substantially higher than the average growth rate of the Eurozone.

This evolution confirms the correctness of the recent change in the economic policy mix, which targets the long-term fiscal consolidation, the confrontation of long-term structural economic weaknesses, the improvement of competitiveness, the enhancement of private sector investment initiatives and the simplification of the tax system and other market regulations.

This satisfactory rate of growth, currently supported by the positive contribution of the foreign balance of payments regarding products and services, is expected to be further bolstered, when all of the ongoing economic reforms begin to yield the expected benefits.

Structural economic reforms in all sectors of the economy (labor market, public administration, taxation, investment motivation) are necessary in order to increase the productivity of the Greek economy, to improve its competitiveness and enhance employment. Such reforms are necessary for the achievement of rapid and sustainable economic growth.

The national program of economic reforms is based on the planning and implementation of a long-term strategy for development and growth. The core principles of this strategy are competitiveness, openness to the world economy and development through private sector investment activities. In this context, the main strategic reforms that have been initiated and are underway for the period 2005-2008 involve:

### **Labor market**

In the context of structural reforms that take place in the labor market, special attention has been given to the promotion of part-time employment as well as other flexible types of labor. The increased flexibility in the labor market combined with securing employment will lead to the creation of new jobs and the motivation of this part of the working population that is willing to work under these certain types of working conditions.

### **Competitiveness and business environment**

The reforms that have already been established and are expected to bring in significant results are:

- Tax reform, mainly through the gradual reduction of corporate income tax rates by 10%, so that they will eventually reduce to 25% from 1-1-2007.

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- The new investment law that offers incentives for the undertaking of new private investment projects and is expected to contribute to the acceleration of regional convergence and promotion of the competitive advantages of our country.
- The improvement of the performance of the 3<sup>rd</sup> European Community Support Framework and related investment programs.
- The co-operation and collaboration of the public and private sector for the creation of public-private partnerships (PPPs).
- The provision of significant tax incentives regarding funding of research and development, which enhance corporate innovation and improve the existing global economic environment.
- A newly enacted law concerning the licensing of manufacturing corporations, as well as the upcoming law for the licensing of trade and service companies, expected to strengthen business activity and competitiveness.

### Public Sector

The fundamental objectives of the 2005 budget were:

- the restoration of the public credibility, reliability and trustworthiness of the economy,
- the fiscal improvement,
- the creation of an economic environment characterized by stability and confidence and
- the gradual restructuring of public expenditure in view of enhancing social cohesion.

All the above were attained through:

1. the restoration of transparency of public accounts and records and the reinforcement of fiscal audits that improve the effectiveness of public finances. Furthermore, it is worth noting that the current administration is making efforts for the establishment of internal audit functions in Ministries, local government and public legal entities,
2. the rationalization of public expenditure,
3. the taxation reform through the gradual reduction of corporate tax rates, the simplification of procedures, the audit transparency, the restriction of tax evasion, the rationalization of the taxation applied to real estate assets and the elimination of social imbalances,
4. the downsizing of the public sector, through privatizations, effective utilization of public assets and restructuring of public enterprises. In particular, there are thirteen (13) bidding engagements underway regarding assets that are currently managed by the Hellenic Olympic Properties Co. and the Touristic Development Co. which are both fully owned (100%) public enterprises, and
5. the modernization of public administration through the improvement of productivity and the quality of services offered to citizens, the establishment of an appraisal system regarding the performance and the implications of new legislation, the reduction of corruption, the development and promotion of e-corporate governance and a life-time education program for civil servants.

## Social Security

In the framework of improving and sustaining sound public finances, the process of a national social dialogue related to the current status of the insurance system in Greece has been announced, in order to safeguard the future adequacy of public resources for the payment of pension liabilities and the removal of the insurance system social imbalances.

In this context, implementation of existing legislation recently resolved the insurance issue of employees working in the banking sector, which was a quite difficult pending problem. Through this resolution, which exclusively refers to the auxiliary pensions of bank-employees, the following are assured and accomplished:

- securing of the payment of pensions to all bank-employees,
- good functioning and fair competition in the banking system,
- support of public-owned banks without being a burden to the ordinary budget and
- elimination of imbalances in the insurance system of the banking sector.

## Privatizations

Privatizations constitute a primary objective to enhance competition and growth in the economy. Proceeds from privatizations in 2005 rose at 2.15 billion euro (or 1.3% of GDP). Through the remarkably successful privatization of National Lotteries (OPAP) and National Telecommunications (OTE) in 2005 the target for budget proceeds from privatizations was outreached by 30%. The strategic privatization planning for the near future entails the stock market preparation and listing of Greek Postal Savings Bank (TT) and Athens International Airport (El. Benizelos) in the Athens Stock Exchange (ASE), the exploitation of ports and the utilization of all public shareholding in both listed and unlisted companies.

## Prospects of 2006

The growth momentum of the economy is supported by a series of structural reforms aiming at enhancing productivity and employment. The government is applying an economic policy mix, targeted at improving the business environment, rationalizing and simplifying the tax system, cutting red tape, facilitating business start-ups and providing additional investment incentives so as to boost private investment activity. In addition, privatizations are targeted at opening markets to competition and attracting further private investment.

An indicative list of structural reforms already initiated includes:

- the tax reform which reduces the corporate income tax rate to 25% by 2007 (a 10 percentage points decrease), simplifies tax audits and institutes generous deductions of corporate research and development (R&D) expenses,
- the new and improved investment incentives law,
- the establishment of a legal framework for public-private partnerships (PPPs),
- the acceleration of privatizations,
- the pension reform in the banking sector,
- the rationalization in the operation of public sector enterprises,
- the simplification in licensing procedures for business start-ups,
- the liberalization in retail shopping hours,
- the introduction of flexibility in working hours and the reduction in overtime pay.

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These reforms are expected to stimulate economic growth and diffuse its results to all sectors of the economy. For example, the corporate tax reforms may contribute up to 0.5 percentage points to GDP growth in the medium term.

The opportunities of 2006 are even more favorable despite the expected increase in oil prices. The rate of economic growth is expected to reach 3.8%, compared to 3.6% in 2005. Private consumption will increase by 3.2% as in 2005, while the rate of public consumption increase will reduce significantly to 1.2%. Total investments will increase by 5.4% as will exports of goods and services by 6.8%. Imported goods and services are expected to increase by 4.9%.

Finally, unemployment is expected to decrease to 9.8% and the rate of increase in labor costs is anticipated to slow down by approximately 1 percentage point. These two factors combined will contribute to a decrease in inflation to 3.2% in 2006.

General government deficit will be restricted to 2.6% of GDP in 2006.

## II. Implementation of the 2005 budget

The main objective of the economic policy for 2005 was to restore fiscal transparency and to establish a climate of trust and economic stability.

Economic growth, employment enhancement and strengthening of social cohesion were achieved through the gradual implementation of the requirements of the government budget.

One of the main targets of the 2005 government budget was to achieve fiscal consolidation with specific objectives such as:

- to restrict the deficit,
- to reduce public debt,
- to continuously reduce public spending as a percentage of GDP,
- to reduce unnecessary military defense programs and consumption expenditure,
- to support the financially weaker social groups.

The above objectives are expected to be achieved as the central government deficit is restricted to 5.9% of GDP compared to 7.7% in 2004. Overall, general government deficit is expected to be 4.3% of GDP, showing a 2.3% decrease compared to 2004. The public debt is anticipated to be reduced by 1.4% of GDP and ordinary budget expenditure is expected to reach 26.6% of GDP compared to 27.2% in 2004.

### 1. Ordinary Budget

#### Revenue

Ordinary budget revenues for 2005, before tax refunds, are expected to reach 44,170 million euro showing an increase of about 5% compared to 2004.

This is mainly due to the significant contribution of the following:

- the 1 percentage point increase in almost all kinds of VAT (Value-added tax) rates since April 1<sup>st</sup> 2005,
- the imposition of a minimum excise tax on tobacco products (65% of the Most Preferred Price Category),
- the increase in the excise tax rate on alcoholic beverages which rises to 1,090 euro/1000 lts,
- the closing of pending tax cases,
- the settlement of pending tax liabilities,
- the acceptance of overdue tax statements without extra penalties or sanctions,
- the tax and customs audits of the new Service for Special Audits.

### **Direct taxation**

Cash receipts from direct taxation are expected to reach 17,940 million euro, representing an increase of 8.8% compared to 2004.

Tax revenues regarding taxation of prior fiscal years (tax arrears) are expected to rise to 2,275 million euro, showing a remarkable increase as compared to the relative figure of 2004. This evolution is mainly the result of the tax settlements announced in 2004 as well as intensified audits of tax authorities. More specifically, the closing of pending tax cases is expected to yield over 800 million euro.

### **Indirect taxation**

Total revenues from indirect taxation are estimated to reach 23,480 million euro, representing an increase of 2.1%.

### **Non-tax revenues**

Non-tax revenues are expected to reach 2,750 million euro showing an annual rise of 7%.

### **Tax refunds**

Tax refunds are estimated to reach 2,300 million euro, reduced by 17.8% compared to 2004.

## **Expenditure per categories**

### **Wages and Pensions**

The wages and pensions expenditure is expected to exceed the budget forecasts by 207 million euro, mainly due to additional personnel hiring in the health and education sectors.

### **Grants to Social Security Funds and Medical Care**

Grants to Social Security funds and health care expenditure are expected to reach 7,880 million euro, i.e. 90 million lower than the original forecast. The expenditure related to the state contribution to social security funds and the Complementary Pension Allowance paid (EKAS) is expected to exceed the initial target by 150 million euro, whereas expenditure associated to the medical care is expected to decrease substantially mainly through the audits conducted and the corrective measures taken.

### **Operating and miscellaneous expenditure**

Operating and other expenses are estimated to exceed the initial forecast by 326 million euro. The main reasons underlying this deviation can be summarised to the following:

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- the extra financing (with 56 million euro) for the operating expenses of the newly established Citizen Service Centres (CSC) and the payroll of part-time employees that were hired in the Local Authorities (40 million euro),
- the subsidies of about 70 million euro given to the agricultural sector, for the implementation of a wide range of programs that are co-financed by the European Union,
- the further funding of universities and other public educational institutions (50 million euro),
- the provision of further ordinary budget funding for subsidies regarding social allowances and health benefits (116 million euro). This is the result of an institutional change in the way social protection and health care grants are paid, since of this year on they are recorded in the ordinary budget expenditure instead of being paid from central independent resources of prefectures.

### Returned resources

Refunding of revenue on behalf of third parties is expected to reach 3,809 million euro, 11.7% higher than the relative amount of 2004. The main part of this increased amount will be directed to local authorities.

### Interest payments

Interest payments will reach 9,730 million euro, lower by 70 million euro than the original forecast of the budget.

## 2. Public Investment Programme

The Public Investment Programme of 2005 shows a remarkable decrease relative to that of 2004 which was particularly expanded due to the funds used for the preparation and successful completion of the Olympic Games.

Total expenditure in the public investment programme is expected to reach 7,700 million euro, 5,150 million euro of which will be directed to EU co-financed projects and the remaining euro 2,550 million to projects exclusively financed by national funds.

## III. The 2006 Government Budget

The effort for a gradual fiscal adjustment of the economy, which was a strategic economic policy choice for restoring fiscal balance, has already born fruits.

The continuous improvement of the main fiscal indicators confirms that this policy was appropriate in order to establish and maintain a stable macro-economic environment that enhances the growth potential of the economy, improves its competitiveness and promotes social cohesion, for the maximization of the benefits attributable to the tax-payer.

In parallel to pursuing economic stability, many structural reforms have already been implemented and more are being planned aiming at contributing to:

- the preservation and acceleration of the growth rate, as well as the distribution of benefits to all through regional convergence,

- the rise in employment and the reduction of unemployment, as well as the more effective connection of the labour market with the educational, training, re-training and life-long learning systems,
- increasing labour productivity by tackling structural deficiencies of the economy,
- improving the business environment,
- increasing competition in the markets,
- increasing the outward orientation of the Greek economy,
- ensuring economic conditions and incentives for boosting economic activity and attracting foreign direct investment,
- the fulfilment of commitments that enhance social cohesion and limit the risk of social exclusion.

Through the Budget of 2006, the acceleration and deepening of reforms efforts is pursued, in order to enhance the growth potential of the economy and ensure fiscal consolidation and a climate of trust and discipline.

The basic target of 2006 budget is lowering the general government deficit further and bringing it below the 3% of GDP limit; more specifically, the 2006 Budget provides for a general government deficit of 2.6% of GDP. Fiscal consolidation is based on restraining expenditure further without affecting the basic services offered by the state and increasing revenue through broadening the tax base and limiting tax evasion. The 2006 budget is also aiming at the acceleration of the public debt's pace of reduction and the fulfilment of government's commitments.

### **The main figures of the 2006 budget**

The 2006 State Budget provides for net revenue of 50,040 million euro, corresponding to 25.9% of GDP. Ordinary budget revenue is expected to increase by 7.9%, thus reaching 24.6% of GDP compared to 24.5% in 2005.

Central government expenditure is restricted at 30.3% of GDP, which is substantially lower than in 2005 and 2004 (30.9% and 32.9% respectively). This is expected to be accomplished despite the significant increase in the Public Investment Programme expenditure by 700 million euro in order to safeguard the growth dynamism of the Greek economy.

The restraint of expenditure stems mainly from the primary expenditure of the ordinary budget which is expected to be reduced through saving on non-productive and low-priority expenses and the reduction in interest payments.

The central government deficit is restricted at 4.4% of GDP, compared to 5.9% and 7.7% in 2005 and 2004 respectively. The general government deficit will reach 2.6% of GDP, down from 4.3% in 2005 and 6.6% in 2004.

## **1. Ordinary Budget**

### **Revenue**

The goals of the government's tax policy for the next three years are:

- to boost competitiveness and business activity, through the gradual reduction of corporate income tax rates and by attracting more foreign investment,

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- to alleviate the tax burden on households through the reduction, starting from 2007, of the personal income tax rates and the increase of the tax-free bracket which is expected to decrease the tax burden on low-income earners,
- to combat tax evasion, smuggling and corruption through the improvement in the tax audit system and the introduction of modern procedures and methods by the auditing authorities.

The forecast of ordinary budget revenue for 2006 is based on the projections for nominal economic growth (estimated at 7.4%), the income elasticity of tax revenue and factors affecting specific revenue categories.

Ordinary budget revenue in 2006 is expected to reach 48,750 million euro, recording an increase of 10.4% compared to the budget implementation estimates for 2005. Measures already enforced are expected to contribute to this outcome; these include tax measures regarding settlements of assessed and overdue liabilities, overdue tax returns to be submitted with no imposition of penalties or other sanctions, the settlement of pending tax cases with favourable terms for taxpayers, the increase in Value Added Tax (VAT) rates and excise taxes on tobacco and alcohol products. Moreover, intensified tax and customs audits against tax evasion and corruption are expected to have a positive impact on reaching the 2006 budget revenue target .

### **Direct taxes**

Direct tax revenue is expected to reach 19,065 million euro, recording an increase of 6.3% compared to the estimated budget outcome for 2005.

The rate of growth of corporate tax revenue is expected to accelerate, although corporate tax rates have been lowered.

Tax arrears are expected to reach 2,410 million euro, mainly due to the completion of tax settlements that had been initiated in 2004 as well as to the effectiveness of special tax audits.

### **Indirect taxes**

Indirect tax revenue is expected to reach 25,540 million euro, recording an increase of 8.8% over 2005.

Value Added Tax revenue is expected to reach 15.148 million euro, recording an increase of 9.2% compared to the outcome in 2005. This forecast is based on the mean income elasticity of VAT revenue (over the last decade) as well as the continuously improving performance of tax audits.

### **Non tax revenue**

Non-tax revenue is expected to reach 3,045 million euro, recording an increase of 10.7% over the estimated budget outcome for 2005.

### **Non-recurring revenue**

The 2006 Budget includes non-ordinary revenue in the order of 1,100 million euro. This amount includes:

- the receipt of extra dividends (550 million euro),
- the concession of licences and rights (440 million euro),
- proceeds from the clearance of the revenue of the Hellenic Communications and Post Commission (NCPC).

Revenue from the securitisation of delinquent claims is not included in the budget outcome for 2005 or in the forecasts for the 2006. Eurostat has not yet concluded its technical evaluation on the statistical treatment of this type of transaction.

### **Tax refunds**

For fiscal year 2006, tax refunds are anticipated to reach 2,200 million euro.

### **Expenditure**

Ordinary budget expenditure (excluding amortization payments) is expected to be lower as a ratio to GDP and will reach 25.9% in 2006, down from 26.6% and 27.2% in 2005 and 2004 respectively.

In particular, ordinary budget expenditure is forecasted to reach 50,190 million euro, increasing by 4.8% compared to 2005. Among the several categories of primary expenditure, there are non-recurring expenditure items as well as items concerning remedy of injustices done to several social groups in the past. Examples of such expenditure items include the return to pensioners of the contribution on behalf of the Solidarity Account of Social Security Funds (LAFKA) amounting to 144 mio euro, the arrangements concerning policemen and retired military personnel (120 mio), the elections for local government (60 mio).

If the aforementioned items are excluded, the rate of growth of expenditure would be significantly lower (4.1%), while growth of primary expenditure would be reduced to 5.5%, down from 5.9% in 2005. Interest payments are also expected to reach 5% of GDP in 2006, as compared to 5.4% and 5.7% in 2005 and 2004 respectively.

### **Wages and pensions**

The wage bill is expected to increase by 6.1% as a result of:

- the income policy,
- wage maturity
- the provision of special income allowances to police, coast-guard and military employees, and
- the rate of growth of pensions, which will exceed that of wages, along with the aforementioned arrangements for military personnel and relevant categories.

### **Grants to social security funds and medical care**

Expenditure on social security and medical care is expected to increase at a higher rate (8.2%) compared to other ordinary budget primary expenditure items, thus still accounting for a significant part (21%) of total primary expenditure.

The main part of this expenditure represents grants to social security funds which increase by 9.2%. This expenditure item is expected to cover:

- the financing of the increase in farmers' pensions (OGA -Farmers' Insurance Fund),
- the increase in EKAS (Pensioners' Social Solidarity Allowance),
- the increase in Seamen's pensions,
- the grant to IKA (Wage Earners' Social Insurance Fund) and
- the refund of the contribution on behalf of the Solidarity Account of Social Security Funds (LAFKA).

### **Operating and miscellaneous expenditure**

Operating expenditure is expected to rise by 5.5% in 2006 due to the following reasons:

- grants to higher education institutions, mainly for establishing new departments,
- commitments that have been undertaken, such as subsidies to the Greek Farmers' Social Security Compensation Account (ELGA) and increased subsidies to farmers,
- higher national contributions to the EU,
- higher social protection allowances,
- funding in order to continue part-time employment programmes,
- funding for the local government elections.

### **New policies - programs**

At this point of time, funding is mainly related to new policies, programs and initiatives. During the fiscal year they are reallocated to other expenditure items.

### **Returned resources**

This item, which is expected to increase by 5.7% in 2006 (down from 11.7% in 2005), refers to restitutions of revenue to local authorities and social security funds (in particular, to the Farmers Insurance Fund and the Attorneys Insurance Fund).

### **Interest payments**

Interest payments are estimated to reach 5% of GDP in 2006, down from 5.4% in 2005.

## **2. Public Investment Budget**

Public Investment Budget (PIB) expenditure is forecasted to reach 8,400 million euro; 6,100 million euro are allocated to projects co-financed by EU Structural Funds, while the remaining 2,300 million euro correspond to the national strand of the PIB. It should be mentioned that the new law for Public Private Partnerships (PPPs) is expected to contribute significantly to enhancing investment activity without burdening the Public Investment Budget .

Since 2006 is the final year for signing the contracts regarding infrastructure projects that will take place the following two years (2007 and 2008) under the 3<sup>rd</sup> Community Support Framework (CSF III), the aforementioned amounts were allocated with a view to expedite and improve the absorption and utilisation of resources of CSF III.

The strategic objective of the 3rd Community Support Framework is the continuation and reinforcement of policies that will accelerate real convergence, regional development and social cohesion. Through the National Strategic Development Framework for the 2007-2013 period, financing will be provided for projects and initiatives that will stimulate labour productivity growth and enhance the competitiveness of the economy.

The national strand of the PIB is designed with a view to pursuing the rational and effective allocation and utilisation of funds while supporting and complementing co-financed projects.

The critical contribution of the PIB programmes is the option to finance investment projects related to strategic infrastructure projects in sectors such as transportation, environment, public health, education

and social cohesion. Furthermore, PIB provides funding to projects that aim at enhancing regional convergence, primarily with a view to addressing issues and problems in insular or mountainous areas of Greece. Finally, it finances projects that are undertaken by the private sector and, especially by the small and medium enterprises, in the framework of the new investment incentives law.

Investment projects financed by the PIB create a more attractive business environment, which has positive spillovers for all sectors of economic activity and improves the competitive position of the country.

Complementary to the role of the PIB, the recent law regarding Public Private Partnerships (PPPs) promotes a wide variety of investment projects that are realised through the co-operation and co-financing of the public and the private sector. This framework boosts entrepreneurship, provides better quality infrastructure and services and increases the number of total investment projects undertaken. The completion of all these investment projects is expected to favourably affect employment growth and allow the provision of higher quality services to citizens.

## IV. Public debt

The continuous reduction of public debt is a basic target of the government's fiscal policy for 2006. The accomplishment of this goal, coupled with the reduction of deficit below 3% of GDP and the maintenance of high growth rates, are expected to ensure conditions of long-term fiscal stability.

The long-term reduction of debt is based on the government's political commitment for establishing a flexible institutional framework in various sectors of the economy. This framework is underpinned by an agenda of structural reforms, such as the privatization programme, public private partnerships (PPPs), better use of public assets (mainly real estate), and increased efficiency of public enterprises. This policy, being implemented for the last two years, has already born fruits, as illustrated by a significant decrease of the public debt as a ratio to GDP (estimated to exceed 4 percentage points for the period 2005-2006).

### 1. Composition of public debt

#### Composition of Central Government Debt

The outstanding Central Government debt is estimated at 215,428 million euro in 2005, thus reaching 119.7% of GDP, compared to 201,244 million euro or 120.4% of GDP in 2004. It is estimated that the Central Government debt on 31/12/2006 will have reached 226,637 million euro, recording a further decrease to 117.2% as a ratio to GDP.

At the end of 2005, the non-euro denominated Central Government debt accounts for only 1.3% of the total outstanding debt, a share that practically highlights the elimination of the exchange rate risk for the debt portfolio.

#### Structure and characteristics of the Central Government Debt

The share of short-term securities (T-bills) in the Central Government Debt amounts to 0.7% in 2005, compared to 0.9% in 2004. On 31/10/2005 the fixed rate represented 78.7% of the total volume of securities, whereas the floating rate 21.3%, compared to 81.6% and 18.4% respectively on 31/12/2004.

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The average residual maturity of the Central Government debt remained on an upward trend during the last years. Thus, on 31/10/2005, 47.1% of the tradable debt had a residual maturity exceeding 5 years.

In 2004 the outstanding military debt amounted to 6,536 million euro or 3.9% of GDP, while in 2005 it is estimated to reach 5,840 million euro or 3.2% of GDP. In 2006 a further reduction is foreseen.

The total expenditure for debt servicing (interest payments, amortization and other related expenditure) in 2005 is estimated to reach 30,016 million euro compared to 27,799 in 2004, mainly due to the redemption of large volumes of short and medium term securities. Interest payments remain on a downward trend as a ratio to GDP and they expected to reach 5.0% in 2006 down from 7.4% in 2001.

### **2. General government debt**

The General Government debt on 31/12/05 is estimated to reach 107.9% of the GDP, while a further reduction to 104.8% of GDP is foreseen for 2006.

### **3. The Greek Government Securities Market**

The Greek Government Securities Market has closely followed the general trend of the integrated Eurobonds market. Thus, during the 3<sup>rd</sup> quarter of 2005, a decrease in the prices of short- and medium-term tenors has been recorded, coupled with historical high prices of long-term tenors. As a result, the yield curve of the Hellenic Republic securities has shifted downwards and, at the same time, its slope at the short- and medium-term part has decreased further.

#### **Primary market**

The largest part of the total yearly issuance activity had been carried out by 31/10/2005.

The prime objective of the 2005 issuance policy (as also in previous years) was the establishment of 3, 5 and 10-year benchmark bonds, with high liquidity (at least 5 bn euro), following a frontloaded issuance pattern.

Following the successful placement of the two 30-year privately placed issues in 2004 and taking full advantage of the investment opportunities offered by the historically low levels of long-term interest rates, the first long-term benchmark bond was successfully issued in 2005, thus extending the Greek yield curve to more than 30 years (September 2037).

#### **Secondary market**

During the 3<sup>rd</sup> quarter of 2005 the turnover of Government Securities both in the Electronic Secondary market (HDAT) and in the Securities Settlement System (BOGSS) remained at high levels. The average daily trading volume was 2,873 and 25,303 million euro in HDAT and in BOGSS respectively. The new 10 year benchmark bond (maturity 20/7/2015) has attracted a 29.31% of the total volume of transactions.

### **4. Basic characteristics of the borrowing strategy and management targets of 2006**

The borrowing strategy for 2006 is dictated by cash requirements arising from the redemption schedule, the borrowing requirements of the State Budget and the implementation of the privatisation programme.

The main characteristics of the borrowing plan are the following:

- bond issuance will focus again on the 3, 5 and 10-year tenors, as well as on T-Bills,
- re-openings of the long-term (over 30 years) benchmark bond, following its successful issuance,
- strategic issues in order to diversify the investor base and exploit potential investment opportunities,
- depending on market conditions, the strategy on the inflation-linked bonds' issuance will be implemented either through increasing the liquidity of the existing 20-year benchmark bond, or through issuance of a new –different tenure- benchmark bond.

The portfolio debt management targets will be focused in:

- Keeping the duration within the desired band of 3.5-4.5 years,
- keeping the fixed/ floating rate notes ratio around the level of 80%- 20%.

Table 1. Central Government Budget 2006 (in million euros)						
	2004	2005		2006	Change %	
	Outcome	Budget	Estimate	Budget	2005/04	2006/05
	(a)	(b)	(c)	(d)	(c)/(a)	(d)/(c)
<b>ORDINARY BUDGET</b>						
<b>1. Net revenue (a+b-c)</b>	<b>39,257</b>	<b>43,710</b>	<b>41,870</b>	<b>46,550</b>	<b>6.7</b>	<b>11.2</b>
a. Revenue	42,055	46,310	44,170	47,650	5.0	7.9
b. Non-ordinary revenue				1,100		
c. Tax refunds	2,798	2,600	2,300	2,200	-17.8	-4.3
<b>2. Expenditure (a+b)</b>	<b>45,490</b>	<b>47,577</b>	<b>47,884</b>	<b>50,190</b>	<b>5.3</b>	<b>4.8</b>
a. Interest payments	9,464	9,800	9,730	9,600	2.8	-1.3
b. Primary expenditure	36,025	37,777	38,154	40,590	5.9	6.4
<b>3. Ordinary budget deficit (1-2)</b>	<b>-6,233</b>	<b>-3,867</b>	<b>-6,014</b>	<b>-3,640</b>	<b>-3.5</b>	<b>-39.5</b>
<b>PUBLIC INVESTMENT PROGRAMME</b>						
<b>4. Revenue (a+b)</b>	<b>2,894</b>	<b>3,400</b>	<b>3,078</b>	<b>3,490</b>	<b>6.4</b>	<b>13.4</b>
a. Inflows from EU	2,811	3,300	2,998	3,400	6.7	13.4
b. Other	83	100	80	90	-3.6	12.5
<b>5. Expenditure</b>	<b>9,522</b>	<b>8,050</b>	<b>7,700</b>	<b>8,400</b>	<b>-19.1</b>	<b>9.1</b>
<b>6. Public investment programme deficit (4-5)</b>	<b>-6,628</b>	<b>-4,650</b>	<b>-4,622</b>	<b>-4,910</b>	<b>-30.3</b>	<b>6.2</b>
<b>7. Central Government Deficit (3+6)</b>	<b>-12,861</b>	<b>-8,517</b>	<b>-10,636</b>	<b>-8,550</b>	<b>-17.3</b>	<b>-19.6</b>
<i>(% of GDP)</i>	<i>-7.7%</i>	<i>-4.8%</i>	<i>-5.9%</i>	<i>-4.4%</i>		
GDP	167,169	177,393	180,045	193,427		

Table 2. General Government Deficit (in million euros)				
	2004	2005		2006
	Outcome	Budget	Estimate	Budget
a. Central Government Deficit	-12,861	-8,517	-10,636	-8,550
b. Surplus of public entities etc.	5,836	4,260	4,390	4,990
c. Financing of social security funds	-1,916	-450	-450	-400
d. Military procurement expenditure	-1,792	-1,600	-1,400	-1,500
e. Other adjustments (ESA 95)	-372	1,300	347	450
<b>f. General Government deficit (a+b+c+d+e)</b>	<b>-11,105</b>	<b>-5,007</b>	<b>-7,749</b>	<b>-5,010</b>
<i>(% of GDP)</i>	<i>-6.6</i>	<i>-2.8</i>	<i>-4.3</i>	<i>-2.6</i>
GDP	167,169	177,393	180,045	193,427

**Table 3. Ordinary budget revenue  
(in million euros)**

	2004 Outcome	2005 Budget	2005 Estimates	2006 Budget	Change %	
					2005/04	2006/05
<b>A. ORDINARY REVENUE (I+II+III+IV)</b>	<b>42,055</b>	<b>46,310</b>	<b>44,170</b>	<b>47,650</b>	<b>5.0</b>	<b>7.9</b>
<b>I DIRECT TAXES</b>	<b>16,484</b>	<b>18,145</b>	<b>17,940</b>	<b>19,065</b>	<b>8.8</b>	<b>6.3</b>
1. Income tax	13,307	14,620	13,920	14,760	4.6	6.0
(Personal income tax)	7,785	8,365	8,117	8,860	4.3	9.2
(Corporate income tax)	4,724	5,240	4,718	4,900	-0.1	3.9
(Other)	798	1,015	1,085	1,000	36.0	-7.8
2. Property taxes	422	490	528	550	25.1	4.2
3. Tax arrears	1,569	1,690	2,275	2,410	45.0	5.9
4. Other direct taxes	1,186	1,345	1,217	1,345	2.6	10.5
<b>II INDIRECT TAXES</b>	<b>23,000</b>	<b>25,595</b>	<b>23,480</b>	<b>25,540</b>	<b>2.1</b>	<b>8.8</b>
1. Transaction taxes	15,255	17,085	15,493	16,828	1.6	8.6
1.1 V.A.T.	13,741	15,430	13,875	15,148	1.0	9.2
(fuel)	1,141	1,160	1,422	1,600	24.6	12.5
(tobacco)	550	605	553	593	0.5	7.2
(Other)	12,050	13,665	11,900	12,955	-1.2	8.9
1.2 Other transaction taxes	1,514	1,655	1,618	1,680	6.9	3.8
(Capital transfers)	(798)	(885)	(890)	(918)	(11.5)	(3.1)
(Stamp duty)	(624)	(675)	(625)	(650)	(0.2)	(4.0)
2. Consumption taxes	7,051	7,530	7,180	7,797	1.8	8.6
2.1 Turnover tax	269	295	280	300	4.1	7.1
2.2 On vehicles	908	935	868	886	-4.4	2.1
2.3 Excise tax on fuel	2,461	2,665	2,505	2,848	1.8	13.7
2.4 Other excise taxes tobacco etc	2,524	2,755	2,605	2,778	3.2	6.6
2.5 Road duties	694	715	754	802	8.6	6.4
2.6 Other	195	165	168	183	-13.8	8.9
3. Tax arrears	290	520	396	455	36.6	14.9
4. Other indirect taxes	404	460	411	460	1.7	11.9
(For E.U.)	(269)	(295)	(256)	(267)	(-4.8)	(4.3)
<b>Tax Revenue (I+II)</b>	<b>39,484</b>	<b>43,740</b>	<b>41,420</b>	<b>44,605</b>	<b>4.9</b>	<b>7.7</b>
<b>III FROM E.U.</b>	<b>164</b>	<b>229</b>	<b>237</b>	<b>190</b>	<b>44.5</b>	<b>-19.8</b>
<b>IV OTHER NON-TAX REVENUE</b>	<b>2,407</b>	<b>2,341</b>	<b>2,513</b>	<b>2,855</b>	<b>4.4</b>	<b>13.6</b>
<b>Non-tax Revenue (III+IV)</b>	<b>2,571</b>	<b>2,570</b>	<b>2,750</b>	<b>3,045</b>	<b>7.0</b>	<b>10.7</b>
<b>B. NON RECURRING REVENUE</b>				<b>1,100</b>		
<b>TOTAL REVENUE</b>	<b>42,055</b>	<b>46,310</b>	<b>44,170</b>	<b>48,750</b>	<b>5.0</b>	<b>10.4</b>
<b>Tax refunds</b>	<b>2,798</b>	<b>2,600</b>	<b>2,300</b>	<b>2,200</b>	<b>-17.8</b>	<b>-4.3</b>
<b>NET REVENUE</b>	<b>39,257</b>	<b>43,710</b>	<b>41,870</b>	<b>46,550</b>	<b>6.7</b>	<b>11.2</b>

**Table 4. Central Government Budget 2006**  
(in million euro)

	2004	2005		2006	Change %	
	Outcome	Budget	Estimate	Budget	2005/04	2006/05
	(1)	(2)	(3)	(4)	(3/1)	(4/3)
<b>ORDINARY BUDGET</b>						
<b>REVENUE</b>	<b>42,055</b>	<b>46,310</b>	<b>44,170</b>	<b>48,750</b>	<b>5.0</b>	<b>10.4</b>
Tax revenue	39,484	43,740	41,420	44,605	4.9	7.7
Non-tax revenue and EU	2,571	2,570	2,750	3,045	7.0	10.7
Non-ordinary revenue				1,100		
Tax refunds (-)	2,798	2,600	2,300	2,200	-17.8	-4.3
<b>NET Revenue</b>	<b>39,257</b>	<b>43,710</b>	<b>41,870</b>	<b>46,550</b>	<b>6.7</b>	<b>11.2</b>
<b>PRIMARY EXPENDITURE</b>	<b>36,025</b>	<b>37,777</b>	<b>38,154</b>	<b>40,590</b>	<b>5.9</b>	<b>6.4</b>
Salaries and pensions	17,496	18,312	18,518	19,648	5.8	6.1
Wages	12,427	13,061	13,278	14,096	6.8	6.2
Grants to social security and medical care	7,236	7,970	7,880	8,530	8.9	8.2
Operating expenditure	7,883	7,621	7,946	8,387	0.8	5.5
Returned resources	3,410	3,875	3,809	4,026	11.7	5.7
Primary surplus	3,232	5,933	3,716	5,960	15.0	60.4
<b>Interest payments</b>	<b>9,464</b>	<b>9,800</b>	<b>9,730</b>	<b>9,600</b>	<b>2.8</b>	<b>-1.3</b>
<b>TOTAL EXPENDITURE</b>	<b>45,490</b>	<b>47,577</b>	<b>47,884</b>	<b>50,190</b>	<b>5.3</b>	<b>4.8</b>
Ordinary Budget Deficit	-6,233	-3,867	-6,014	-3,640	-3.5	-39.5
Amortization	20,356	21,786	21,767	18,136	6.9	-16.7
Military procurement expenditure	826	1,600	1,400	1,500	69.5	7.1
<b>PUBLIC INVESTMENT PROGRAMME</b>						
<b>REVENUE</b>	<b>2,894</b>	<b>3,400</b>	<b>3,078</b>	<b>3,490</b>	<b>6.4</b>	<b>13.4</b>
Inflows from EU	2,811	3,300	2,998	3,400	6.7	13.4
Other	83	100	80	90		
<b>Expenditure</b>	<b>9,522</b>	<b>8,050</b>	<b>7,700</b>	<b>8,400</b>	<b>-19.1</b>	<b>9.1</b>
Public Investment Programme Deficit	-6,628	-4,650	-4,622	-4,910	-30.3	6.2
<b>CENTRAL GOVERNMENT BUDGET</b>						
<b>Net revenue</b>	<b>42,151</b>	<b>47,110</b>	<b>44,948</b>	<b>50,040</b>	<b>6.6</b>	<b>11.3</b>
<b>Expenditure</b>	<b>55,012</b>	<b>55,627</b>	<b>55,584</b>	<b>58,590</b>	<b>1.0</b>	<b>5.4</b>
<b>Central Government Deficit</b>	<b>-12,861</b>	<b>-8,517</b>	<b>-10,636</b>	<b>-8,550</b>	<b>-17.3</b>	<b>-19.6</b>
<b>Surplus of public entities and other adjustments (ESA 95)</b>	<b>1,756</b>	<b>3,510</b>	<b>2,887</b>	<b>3,540</b>		
<b>GENERAL GOVERNMENT DEFICIT</b>	<b>-11,105</b>	<b>-5,007</b>	<b>-7,749</b>	<b>-5,010</b>		
<b>GDP (Revised)</b>	<b>167,169</b>	<b>177,393</b>	<b>180,045</b>	<b>193,427</b>	<b>7.7</b>	<b>7.4</b>

Source: Ministry of Economy and Finance

<b>Table 5. Central Government Budget 2006 (% of GDP)</b>				
	2004	2005		2006
	Outcome	Budget	Estimate	Budget
	(1)	(2)	(3)	(4)
<b>ORDINARY BUDGET</b>				
<b>REVENUE</b>	<b>25.2</b>	<b>26.1</b>	<b>24.5</b>	<b>25.2</b>
Tax revenue	23.6	24.7	23.0	23.1
Non-tax revenue and EU	1.5	1.4	1.5	1.6
Non-ordinary revenue				0.6
Tax refunds (-)	1.7	1.5	1.3	1.1
<b>NET Revenue</b>	<b>23.5</b>	<b>24.6</b>	<b>23.3</b>	<b>24.1</b>
<b>PRIMARY EXPENDITURE</b>	<b>21.6</b>	<b>21.3</b>	<b>21.2</b>	<b>21.0</b>
Salaries and pensions	10.5	10.3	10.3	10.2
Wages	7.4	7.4	7.4	7.3
Grants to social security and medical care	4.3	4.5	4.4	4.4
Operating expenditure	4.7	4.3	4.4	4.3
Returned resources	2.0	2.2	2.1	2.1
Primary surplus	1.9	3.3	2.1	3.1
<b>Interest payments</b>	<b>5.7</b>	<b>5.5</b>	<b>5.4</b>	<b>5.0</b>
<b>TOTAL EXPENDITURE</b>	<b>27.2</b>	<b>26.8</b>	<b>26.6</b>	<b>25.9</b>
Ordinary Budget Deficit	-3.7	-2.2	-3.3	-1.9
Amortization	12.2	12.3	12.1	9.4
Military procurement expenditure	0.5	0.9	0.8	0.8
<b>PUBLIC INVESTMENT PROGRAMME</b>				
<b>REVENUE</b>	<b>1.7</b>	<b>1.9</b>	<b>1.7</b>	<b>1.8</b>
Inflows from EU	1.7	1.9	1.7	1.8
Other	0.0	0.1	0.0	0.0
<b>Expenditure</b>	<b>5.7</b>	<b>4.5</b>	<b>4.3</b>	<b>4.3</b>
Public Investment Programme Deficit	-4.0	-2.6	-2.6	-2.5
<b>CENTRAL GOVERNMENT BUDGET</b>				
<b>Net revenue</b>	<b>25.2</b>	<b>26.6</b>	<b>25.0</b>	<b>25.9</b>
<b>Expenditure</b>	<b>32.9</b>	<b>31.4</b>	<b>30.9</b>	<b>30.3</b>
<b>Central Government Deficit</b>	<b>-7.7</b>	<b>-4.8</b>	<b>-5.9</b>	<b>-4.4</b>
<b>Surplus of public entities and other adjustments (ESA 95)</b>	<b>1.1</b>	<b>2.0</b>	<b>1.6</b>	<b>1.8</b>
<b>GENERAL GOVERNMENT DEFICIT</b>	<b>-6.6</b>	<b>-2.8</b>	<b>-4.3</b>	<b>-2.6</b>

Table 6. Central and General Government Debt (in million euro)				
	2003	2004	2005*	2006**
<b>A. Debt in euro</b>	<b>179,008</b>	<b>198,741</b>	<b>212,687</b>	<b>223,989</b>
(as % of GDP)	116.1%	118.9%	118.1%	115.8%
1. Treasury Bills	958	1,842	1,461	1,390
<i>(held by the public sector)</i>	<i>407</i>	<i>369</i>	<i>305</i>	<i>290</i>
<i>(held by the private sector)</i>	<i>551</i>	<i>1,473</i>	<i>1,156</i>	<i>1,100</i>
2. Government bonds (auctions and other issues)	137,684	157,124	173,816	186,471
<i>Bonds</i>	<i>136,335</i>	<i>155,930</i>	<i>172,661</i>	<i>185,419</i>
<i>Consolidated loans</i>	<i>1,349</i>	<i>1,194</i>	<i>1,155</i>	<i>1,052</i>
3. Syndicated and other loans in euro	24,377	26,779	27,013	26,500
4. Liabilities to the Bank of Greece	9,018	8,488	8,025	7,522
5. ESA 95 adjustments ( <i>privatization certificates, securitization, convertible bonds</i> )	6,971	4,508	2,372	2,106
<b>B. Non euro zone debt</b>	<b>3,382</b>	<b>2,503</b>	<b>2,741</b>	<b>2,648</b>
(as % of GDP)	2.2%	1.5%	1.5%	1.4%
1. Loans in foreign currency	2,809	2,003	2,205	2,142
2. Foreign currency-linked bonds and loans	573	500	536	506
<b>C. Total Central Government Debt (A+B)</b>	<b>182,390</b>	<b>201,244</b>	<b>215,428</b>	<b>226,637</b>
(as % of GDP)	118.3%	120.4%	119.7%	117.2%
D. Debt of public entities, coins etc	986	513	700	774
<b>E. Central Government Debt (ESA adjustments)(C+D)</b>	<b>183,376</b>	<b>201,757</b>	<b>216,128</b>	<b>227,411</b>
F. Debt of OTA, OKA	2,170	2,152	2,092	2,110
G. Intragovernmental Debt(-)	-17,824	-21,207	-23,885	-26,751
<b>H. General Government Debt (E+F+G)</b>	<b>167,722</b>	<b>182,702</b>	<b>194,335</b>	<b>202,770</b>
As % of GDP	<b>108.8%</b>	109.3%	107.9%	104.8%
<b>GDP</b>	<b>154,153</b>	<b>167,169</b>	<b>180,045</b>	<b>193,427</b>

\* Estimates

\*\* Forecasts

Source: Ministry of Economy and Finance

<b>Table 7. Expenses for Olympic Games (in million euro)</b>	
	<b>Estimates 2005</b>
Public expenses	6,676
Organizing Committee – "Athens 2004" Ltd expenses	1,810
<b>Total</b>	<b>8,486</b>

According to final (audited) data, the total cost of the Olympic Games reached 8,486 million euro as compared to the original estimate of 8,954 million euro, which was prepared in September 2004. This amount includes both the expenses incurred by the central government budget (public expenses) and those financed by the budget of the Organizing Committee – Athens 2004.