

Greece: An overview of economic and corporate developments

Greece offers a favourable investment environment: The entrance of Greece in the eurozone and the subsequent adoption of euro is starting to pay off. The economic and political stability within eurozone, the economic growth that outpaces the EU average for a series of years, the strategic location, the highly qualified labour force, the brand new physical infrastructure network and high growth potential business sectors (shipping, banking, tourism) has made Greece an important economic player in the sizeable emerging markets of the Balkans, Black Sea, Eastern European and Eastern Mediterranean regions and today more than 3,000 Greek companies have established significant presence in the nearby regions.

The outlook for economic activity remains positive: Greece enjoys the highest GDP growth rates in the euro zone (4.1% Q2 2006 compared to 2.0% in eurozone and 2.2% in EU-25) despite soaring oil prices, fiscal consolidation process underway, increasing interest rates, moderate economic performance of the euro zone and the expectations of an economic slowdown after the Olympic Games. This performance is expected to continue with GDP forecasts of around 3.8% in 2006, above 3.6% in 2007-2008, with the GDP per capita (in PPS expected to reach the 80% of EU average in 2008 compared to 64.3% in 1998). In 2006, continuing strong domestic demand outstripped the slack created by a worsened current account balance (although exports of goods reported spectacular increase: 22.1% in Jan-June '06). In addition, business investment is expected to reach new highs, supported by the Investment Incentives Law due to expire in 2008, Public-Private Partnerships and Community Support Frameworks 2007-2013 of €20.1 billion and remaining funds from 2000-2006 of approximately €11 billion. In addition, we have witnessed a steady improvement in economic sentiment indicators that shows growth in disposable incomes, acceleration of retail sales volumes, and strong credit expansion. Also growth in exports is expected provided that demand in trading partners is robust and Greece improves its international competitiveness, while inward FDI, tourism and shipping are also on rising trend. All these positive signs are depicted in the continuous improved economic sentiment indicators.

The dynamism of the Greek economy reflects important changes on the supply side conditions. Growth-promoting reforms by the government aim at increasing country's international competitiveness and investment climate. Gradual lowering of corporate and individuals' tax rates (Tax Reform Law), simplification of bureaucracy affecting entrepreneurship, New Investment Incentives Law and Law for Public-Private Partnerships. Also, initiatives to enhance market liberalisation and competition, including ambitious privatisation programme, plans for complete liberalisation of electricity market from mid-2007, and law liberalising natural gas market.

Inflation and unemployment pose a threat but remain under control: Inflation, although remains at a higher level compared to EU, moved lower in August 2006 (3.5% from 3.9% in July '06) despite the demand-side pressures such as high oil prices and wage increases, and is expected to remain above 3% in 2006-2007. Similarly, unemployment persists as well but on a declining path (9.7% in 1Q06 vs 10.4% in 1Q05) with employment and labor productivity expected to rise. Positive impact to this direction is expected by the labor market flexibility with legislation to abolish permanent contracts for new employees in public entities and enterprises, measures to reduce cost of overtime and promote flexible working hours, and a new law to smooth immigrants' integration and curtail black economy. Additionally, shopping hours have been extended.

Significant domestic fiscal consolidation underway. Recently, we have witnessed a rationalization of public spending and increase of state revenues with the policy of gradual fiscal adjustment safeguarding the performance of the economy. Efforts to reform pension and health-care systems are on track, ensuring public finances sustainability.

Scheduled Reforms-Projects: The aforementioned significant improvements in basic fundamental figures have led to the undertaken of sizeable international projects that would help the country to maintain its leading position in the region. The energy sector with the Burgas-Alexandroupolis pipeline project, the Russia's interest in energy sector (Gazprom, Lukoil), as well as telecoms and military systems, together

September 2006

with China's shipping sector interested in Greek ports in Athens and Thessaloniki, Korea's interest in ports and shipyards, and the French interest in the banking sector are examples of these projects.

Banking and corporate developments: The structural changes in the banking sector over the past few years with a number of M&A's and privatizations taken place have led the sector to becoming the most important one for the Greek economy. The performance of the Greek banks has reached record levels compared to historical standards with the most recent results from the first half of 2006 showing a 61% y-o-y increase in profits before tax, with the return on equity amounting to 27% and the efficiency ratio further improved to below 50%, while the Greek banks maintain to preserve a significant interest margin of around 3%, twice as much compared to European peers. At the same time, the risk factors remain well under control with the capital adequacy levels offering a safe cushion. In addition, the expansion to Balkans is well underway, with the Greek banks developing a network of more than 1,000 branches enjoying double digit credit expansion, resulting to profits from the operations abroad currently more than 6% of the overall profits of the sector, an amount that is soon expected to exceed 20%, while for individual banks may reach higher levels within the next five years. At the same time, profitability of the companies with shares listed on Athens Exchange remains high increasing at a 30% pace, supported by corporate development and agreements that are taking place.

Overall, the strength of the Greek economy appears to be sustainable, while the successful outcome of the expected structural reforms and corporate developments make investments in the Greek market particularly attractive.

by **Valuation & Research Specialists (VRS)**