BANK OF GREECE

MONETARY POLICY

2004 - 2005

FEBRUARY 2005

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REPORT ON MONETARY POLICY 2004-2005

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To the Greek Parliament and
the Council of Ministers

The present Report on Monetary Policy is submitted to the Greek Parliament and the Council of Ministers in accordance with the Statute of the Bank of Greece. The Report is summarised in Chapter I. Chapters II and III examine in detail the international economic environment, the course of inflation and economic activity in the euro area and Greece in 2004 and the economic outlook for 2005.

2004 saw an appreciable increase in the growth rate of economic activity worldwide. Although subject to considerable uncertainties, world economic growth is forecast to continue in 2005, albeit at a slower rate. In the euro area, economic growth accelerated slightly in 2004, while in 2005 it is expected to remain virtually unchanged or to be a little lower than in 2004. Inflation in the euro area, which stood above 2% for most of 2004, mainly owing to the sizeable increase in oil prices, should decline during 2005 and remain slightly below 2%.

As regards economic developments and prospects for Greece, the GDP growth rate fell to 3.8% in 2004, from 4.5% in 2003. For 2005, the Report forecasts a further decrease in the growth rate of economic activity, for the reasons discussed in Chapter III. However, growth should remain considerably higher than in the euro area and therefore further progress will be made towards real convergence. Inflation fell in 2004, but this is almost exclusively attributable to a large fall in the prices of fresh fruit and vegetables. By contrast, core inflation rose further. On the basis of certain assumptions and conditions discussed in detail in Chapter III, it is estimated that in 2005 the inflation rate will accelerate slightly in comparison with 2004, while core inflation will remain virtually unchanged. Therefore, inflation will continue to be much higher than the euro area average and there will be further losses in the international competitiveness of the Greek economy. These forecasts are surrounded by considerable uncertainty, relating to the path of the fiscal deficit and oil price developments, which may influence the course of the Greek economy unfavourably. The existence of these uncertainties warrants vigilance and poses certain challenges to economic policy and the conduct of the social partners, which are described in Chapter VI.

Chapter IV analyses developments in money, credit and capital markets in Greece, while Chapter V evaluates the stability of the Greek financial system and concludes that overall it is sound and its stability has been safeguarded.

As regards monetary policy in the euro area, the European Central Bank has left its key rates unchanged at historically low levels since June 2003, because it estimates that there are no signs of inflationary pressures building up and that economic conditions in the euro area overall remain consistent with price stability over the medium term. Without a doubt, the single monetary policy helps ensure stability and fast economic growth in the euro area. However, as this policy is aimed at safeguarding monetary stability and growth in the euro area *as a whole* and not in individual countries, it is obvious that in Greece national economic policy should play a more active role in the achievement of price stability and, at the same time, seek to create conditions for higher economic growth.

Chapter VI of the Report points out that the achievement of price stability and satisfactory economic growth rates on a permanent basis will require determined fiscal adjustment, which involves the gradual elimination of the fiscal deficit and a faster decrease in the debt-to-GDP ratio. Furthermore, it will require wage increases in line with productivity growth, as well as structural reforms in a broad range of economic sectors in order to remove product and labour market rigidities. The consistent implementation of a well-designed programme of structural reforms will contribute to fiscal stability, encourage investment and new productive activities and thus boost economic growth and employment.

Athens, February 2005

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Governor

Monetary Policy Council of the Bank of Greece

Chairman

Nicholas C. Garganas

Members

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Georgios E. Oikonomou

On 1 January 2001 Greece joined the Economic and Monetary Union and adopted the euro. As of that date, the Bank of Greece participates in the Eurosystem, which is a common central banking system consisting of the European Central Bank and the twelve national central banks of the euro area countries.

The following three documents ("The mission of the Eurosystem", "The strategic intents of the Eurosystem" and "Organisational principles for the fulfilment of Eurosystem functions by all members of the Eurosystem") were adopted by the Governing Council of the ECB and were published on 5 January 2005. The documents provide concrete and tangible guidance on how the members of the Eurosystem perform the tasks and achieve the objectives that the Treaty and the ESCB Statute entrust to the Eurosystem.

The mission of the Eurosystem

The Eurosystem, which comprises the European Central Bank and the national central banks of the Member States whose currency is the euro, is the monetary authority of the euro area. We in the Eurosystem have as our primary objective the maintenance of price stability for the common good. Acting also as a leading financial authority, we aim to safeguard financial stability and promote European financial integration.

In pursuing our objectives, we attach utmost importance to credibility, trust, transparency and accountability. We aim for effective communication with the citizens of Europe and the media. We are committed to conducting our relations with European and national authorities in full accordance with the Treaty provisions and with due regard to the principle of independence.

We jointly contribute, strategically and operationally, to attaining our common goals, with due respect to the principle of decentralisation. We are committed to good governance and to performing our tasks effectively and efficiently, in a spirit of cooperation and teamwork. Drawing on the breadth and depth of our experiences as well as on the exchange of know-how, we aim to strengthen our shared identity, speak with a single voice and exploit synergies, within a framework of clearly defined roles and responsibilities for all members of the Eurosystem. →

→ The strategic intents of the Eurosystem

FIRST STRATEGIC INTENT

Acknowledged authority in monetary and financial matters

Building on its solid constitutional basis, its independence and its internal cohesion, the Eurosystem, the central banking system of the euro area, shall act as the monetary authority of the euro area and as a leading financial authority, fully recognised inside and outside Europe. In pursuing its primary objective, the maintenance of price stability, the Eurosystem shall undertake the necessary economic and monetary analyses and adopt and implement appropriate policies. It shall also properly and effectively respond to monetary and financial developments.

SECOND STRATEGIC INTENT

Financial stability and European financial integration

The Eurosystem shall aim to safeguard financial stability and promote European financial integration in cooperation with the established institutional structures. To this end, it shall contribute to policies providing for a sound European and global architecture for financial stability.

THIRD STRATEGIC INTENT

Accountability, credibility and trust. Closeness to the citizens of Europe

The Eurosystem attaches utmost importance to credibility, trust, transparency and accountability. It aims for effective communication with the citizens of Europe and the media. It is committed to conducting its relations with European and national authorities in full accordance with the Treaty provisions and with due regard to the principle of independence. To this end, the Eurosystem will keep abreast of the transformations affecting money and financial markets and will be sensitive to the public interest and market needs.

FOURTH STRATEGIC INTENT

Shared identity, clarity of roles and responsibilities and good governance

The Eurosystem shall aim to strengthen its shared identity within a framework of clearly defined roles and responsibilities for all its participants. To this end, the Eurosystem will build on the potential and deep involvement of all its members, as well as on their commitment and willingness to work towards agreement. Furthermore, the Eurosystem is committed to good governance and to applying effective and efficient organisational structures and working methods.

In performing its activities, the Eurosystem shall be guided by a number of organisational principles. →

→ Organisational principles for the fulfilment of Eurosystem functions by all members of the Eurosystem

With due respect to the principle of decentralisation which is at the root of the System:

1. Participation

All members of the Eurosystem shall contribute strategically and operationally to the goals of the Eurosystem.

2. Cooperation

All Eurosystem functions shall be performed in a spirit of cooperation and teamwork by the members of the Eurosystem.

3. Transparency and accountability

All members of the Eurosystem shall act transparently and be fully responsible and accountable for the effectiveness of all Eurosystem functions.

4. Distinguishing Eurosystem activities

Eurosystem activities performed by national central banks shall be clearly identified and distinguished —to the extent possible— from those pertaining to national responsibilities.

5. Cohesion and unity

While respecting the legal status of its members, the Eurosystem and its staff shall act and appear as a cohesive and unified entity. In that spirit and working as a team, the Eurosystem shall speak with a single voice and be close to the citizens of Europe.

6. Exchange of resources

The exchange of personnel, know-how and experience shall be promoted by and among all members of the Eurosystem.

7. Effectiveness and efficiency in decision-making

All Eurosystem decision-making and deliberative processes need to pursue effectiveness and efficiency. Decision-making shall focus on analysis and arguments as well as on expressing views in their variety. →

→ 8. Cost efficiency, measurement and methodology

The Executive Board of the ECB and the Governors of the national central banks shall manage all resources prudently and shall promote effective and cost-efficient solutions in all parts of the Eurosystem.

The ECB and the NCBs shall develop control systems and performance indicators to measure the fulfilment of Eurosystem functions and their alignment with the objectives of the Eurosystem.

Comparable cost evaluation and cost-reporting methods should be elaborated.

9. Exploit synergies and avoid duplications

Potential synergies and economies of scale shall be identified and exploited to the extent feasible.

Unnecessary duplication of work and resources at functional levels and over-extensive and inefficient coordination shall be avoided. To this end, the Eurosystem shall energetically pursue organisational options that ensure effectiveness, efficiency and prompt action, taking advantage of the experience available both at the ECB and at the NCBs through intensified use of existing resources.

The outsourcing of Eurosystem support functions and activities shall be considered against the same criteria and shall take security aspects into account

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I. Summary

The Governing Council of the European Central Bank (ECB), which is responsible for the formulation of monetary policy in the euro area, kept the key ECB rates unchanged throughout 2004 and in the first two months of 2005. With their last cut on 6 June 2003,[1] these rates have reached historic lows. Underlying the decision of the ECB Governing Council to keep the key ECB rates unchanged was its assessment that, despite the short-term effects of high oil prices on the level of prices, there are no signs of medium-term inflationary pressures building up and overall economic conditions in the euro area remain consistent with price stability. However, the ECB has repeatedly stressed the need for vigilance with respect to developments that may entail increased inflationary pressures, notably risks associated with possible further rises in oil prices and considerable second-round effects on consumer prices (through nominal wage increases), as well as with the level of liquidity in the euro area.

The money market rates in the *euro area* remained low during 2004, as the key ECB rates were unchanged in that year. Specifically, the three-month EURIBOR, which is the most representative short-term interest rate, stood at historic lows. Furthermore, government bond yields declined in 2004. As regards bank rates in the euro area, those on deposits by households and non-financial corporations remained low in 2004. Lending rates fell in most categories from the end of 2003, despite some fluctuations during 2004. The pass-through of market rate changes to bank deposit and lending rates with a similar maturity showed the typical time lag in 2004.

1 At that time the minimum bid rate for main refinancing operations stood at 2%, the marginal lending rate at 3% and the deposit rate at 1%.

The annual growth rate of M3 in the euro area decelerated in the first half of 2004, as investors gradually restructured their portfolios in favour of longer-term assets as financial market conditions improved. However, in the second half of the year restructuring was slower than expected, while the low level of ECB rates and hence of the euro area money market rates continued to fuel investors' demand for more liquid assets included in M3. As a result, the annual growth rate of M3 accelerated in the second half of 2004. Credit expansion to the private sector, notably the rate of increase in bank loans to both households and non-financial corporations, was also faster during 2004. The Governing Council of the ECB still considers that there is more liquidity in the euro area than is needed to finance non-inflationary growth and therefore continuous vigilance is warranted.

In *Greece*, the annual growth rate of the components of the Greek contribution to the euro area M3[2] (excluding currency in circulation) accelerated considerably in the second half of 2004, while throughout 2004 it was higher than the corresponding euro area rate. The very low interest rates (and hence the relatively low opportunity cost of holding money) support savers' preference for liquid assets in both Greece and the euro area and have thus contributed to a faster increase in M3. In Greece, this development was further influenced by the higher nominal GDP growth rate, differences between Greece and the euro area with respect to the degree of substitution between assets included in M3 and those not, as well as the considerable acceleration in credit expansion (as the central government borrowing requirement was much higher in 2004 than in 2003).

The annual growth rate of all deposits included in M3 changed little in 2004 (fourth quarter of 2004: 12.6%, fourth quarter of 2003: 12.2%), but the relatively low opportunity cost of holding money triggered diverging developments across the individual categories of deposits. The rate of increase in short-term (overnight) deposits accelerated significantly, while it slowed considerably for deposits with a maturity of up to two years. The decline in repo holdings slowed substantially, while the rate of increase in money market mutual fund unit holdings exhibited a declining trend during 2004, only to turn negative in the fourth quarter.

The annual growth rate of total financing of the economy by Monetary Financial Institutions (MFIs – i.e. banks and money market mutual funds) accelerated appreciably to 8.6% in the fourth quarter of 2004, from 3.2% in the fourth quarter of 2003. This reflects a much faster decrease than in the previous year in the outstanding balance of general government financing by domestic MFIs (fourth quarter 2004: –5.6%, fourth quarter 2003: –15.9%). (This decline is associated with the fact that the amount of Greek government securities held by domestic MFIs continued to drop. However, the central government borrowing requirement increased in 2004, as already mentioned, but was met by the rise in foreign inflows to government securities.) By contrast, the rate of credit expansion to enterprises and households showed a small deceleration, while still remaining relatively strong (fourth quarter of 2004: 16.1%, fourth quarter of 2003: 17.1%).

In more detail, credit expansion to *enterprises* slowed (fourth quarter of 2004: 8.6%, fourth quarter of 2003: 11.0%), as the fall in the growth rate of financing of most branches (notably industry and the "other" branches including construction firms) more than offset the increase in the corresponding rate in trade and agriculture.

2 Chapter IV.1 explains why only developments in the M3 components other than currency in circulation are examined.

The rate of credit expansion to *households* remained virtually unchanged (fourth quarter of 2004: 28.0%, fourth quarter of 2003: 28.2%); as a result, households' total indebtedness as a percentage of GDP rose to 31.4% in December 2004, from 26.3% in December 2003. Specifically, the growth rate of housing loans slowed (fourth quarter of 2004: 23.8%, fourth quarter of 2003: 27.1%), partly owing to loan securitisation activity (see Section 2 and the Appendix to Chapter IV). By contrast, the rate of increase in consumer loans accelerated substantially (fourth quarter of 2004: 37.9%, fourth quarter of 2003: 24.8%), following the removal of the last restrictions on consumer credit in June 2003. In the light of the fast pace of credit expansion to households under the pressure of competition, which may increase credit risk in the future, especially in the event of an economic slowdown, the Bank of Greece has increased the minimum provisioning ratios for loans with significant servicing delays and has pointed out that banks should take into account this factor when they grant loans, so as to mitigate credit risk. At the same time, households should evaluate carefully the outlook for their incomes before taking out loans, so as to avoid excessive indebtedness.

Bank deposit rates in Greece were little changed in 2004, as ECB rates have remained unchanged since June 2003. As regards new deposits by households, a small rise was recorded in the rates on overnight deposits and deposits with an agreed maturity of up to one year; these rates are still higher than the corresponding rates in the euro area.

Larger changes were observed in the rates on new bank loans, which generally fell during 2004. Specifically, the rates on consumer loans showed a relatively big decline (of up to 1.02 percentage points), while the rates on housing and corporate loans declined by less.

The spread between the average rate on all new bank loans and the corresponding deposit rate was almost stable in 2004, as both the average deposit and lending rates remained virtually unchanged. It should be noted, however, that the fast growth of consumer loans, which carry higher-than-average rates, leads to an increase in their share in total loans, with an upward effect on the average lending rate. This implies that the average lending rate does not fully reflect the general fall in the rates on the individual categories of loans.

The Greek banking system is sound as a whole and its stability has been safeguarded (as pointed out in Chapter V). The overall capital adequacy ratio (CAR) of Greek commercial banks (13.3% in September 2004, compared with 11.9% for euro area banks as a whole in 2003) provides an adequate cushion under the current circumstances. Only a few banks will be affected considerably by the implementation of the International Accounting Standards as from the beginning of 2005. These banks should therefore strengthen their capital base and restore their capital adequacy. However, the overall CAR of the Greek banking system will not be affected significantly. The implementation of the new supervisory framework ("Basel II") as from the end of 2006 will also have an impact on the CAR, but the magnitude and direction of this impact on individual banks cannot be estimated yet. In the light of these uncertainties, the Bank of Greece has recommended that banks increase their own funds.

2004 saw a noticeable fall in yields and a considerable increase in operations on the secondary market for Greek government securities. After declining in the first three months of 2004, yields rebounded appreciably in the second quarter of 2004, as a result of the upward revision of expectations for world economic growth. However, over the next months until the end of the year, yields showed a continuous fall, mainly owing to the investors' concerns about the effects of the steep rise in oil prices. Funds raised through the primary market increased, while Greek and foreign investors showed keen interest in Greek government bonds.

Share prices in the Greek stock market followed an upward path from the beginning of 2004 to early March, reflecting a considerable improvement in business profitability in 2003. Subsequently, until the end of August, stock prices fell, mainly affected by investors' concerns about the impact of the big rise in oil prices on economic activity and business profitability. Over the next four months stock prices rebounded strongly, as a result of an improvement in business profitability in the January-September 2004 period, as well as of the favourable conditions on international exchanges. Thus, at end-2004 the composite share price index of the Athens Exchange was 23.1% higher than at end-2003. Fund raising through the stock market increased noticeably in 2004, while transactions remained almost at the same levels as in 2003.

* * *

The international economic environment was generally favourable in 2004, improving further in comparison with 2003. World GDP growth (at constant prices) rose from 3.9% in 2003 to 5.0% in 2004, the highest since 1976, while inflation remained generally low. World economic growth is forecast to continue in 2005 and 2006, albeit at somewhat lower rates, closer to the long-term trend growth of real GDP (around 4%). However, the maintenance of such growth rates is subject to considerable uncertainties and risks, mainly associated with accumulated world economic imbalances and developments in the oil market.

In the euro area, the economic recovery continued in 2004, as real GDP growth reached 2.0% (according to Eurostat's flash estimates), compared with 0.6% in 2003. Quarterly GDP growth slowed down during the year, as the steep rise in oil prices, which fed into inflation and reduced households' real incomes, had a negative impact on private consumption, while net exports were affected unfavourably by the appreciation of the euro. Real GDP growth is forecast to remain almost unchanged in 2005 and to pick up slightly in 2006. These forecasts are of course subject to uncertainties, but they are supported by the anticipated positive developments in the world economy. In addition, the maintenance of very low interest rates and favourable corporate financing conditions in the euro area, in conjunction with the forecast decline in oil prices (over the next two years) and inflation, are expected to boost investment and consumer demand.

Inflation in the euro area remained slightly above 2% for most of 2004, mainly as a result of spiralling oil prices, while the lagged impact of the appreciation of the euro is estimated to have contained the rise in import prices. In the end, average annual inflation turned out at 2.1%, i.e. it remained unchanged from 2003. Inflation is expected to fall below 2% during 2005 (and to increase by 1.5-2.5% on average), as both external and domestic inflationary pressures are expected to ease. More specifically, the forecast rise in import prices will be small and domestic cost pressures will remain moderate. In particular, a decline is expected in upward effects on prices from (i) the increases in indirect taxes and administered prices observed in certain euro area countries in 2004 and (ii) the rise in oil prices. Moreover, according to forecasts and in line with developments in the euro area labour market in recent years, wage claims will continue to be moderate and the rate of increase in labour costs will remain very low, while it is expected that any second-round effects on nominal wage growth from oil price increases will remain moderate.

* * *

Turning to the *Greek economy*, GDP growth remained high in 2004, but slowed to 3.8% (from 4.5% in 2003), primarily on account of a slackening in the growth of gross fixed capital formation (relative to 2003) following the completion of investment associated with the Athens Olympic Games. Real GDP growth is projected to edge further downwards to roughly 3.3% in 2005, nonetheless remaining markedly higher than in the euro area. The rise in private consumption is projected to remain the chief stimulus of domestic demand and output, though it will decelerate slightly compared with 2004. Private investment is also projected to contribute positively to growth, on the assumption that business investment will continue to expand (mainly as a result of the newly introduced incentive package), while residential investment should remain broadly at last year's level. In addition, as indicated by forecasts of a favourable world economic outlook, exports — especially in the services sector— should grow at a relatively robust pace. In contrast, general government investment —after being boosted by Olympic Games-related projects in 2003-04— is projected to decline, reflecting in part the need for fiscal consolidation. The latter is also expected to cause an appreciable deceleration in public consumption growth. These projections are surrounded by considerable uncertainty, associated with developments in oil prices and the possibility of adverse effects on private investment decisions as a result of the deterioration of confidence indicators in recent months.

Employment was influenced positively in 2004 by the rise in economic activity and the holding of the Athens Olympic Games, but is expected to pick up only modestly in 2005, thus keeping the unemployment rate high. The projected small increase in employment is attributable to the contraction observed in the construction sector, the restrictive hiring policy in general government (as part of the fiscal consolidation effort) and early retirement schemes in several banking institutions and large public enterprises.

The current account deficit was considerably reduced in 2004 to 3.9% (from 5.6% of GDP in 2003) and is expected to narrow further in 2005. Nonetheless it will remain relatively large, mainly as a result of Greece's structural weaknesses and continued loss of price competitiveness. The favourable external environment is expected to further boost the demand for commercial shipping, Greece's internationally most competitive sector, while travel receipts should be buoyant in the wake of the Olympic Games. Although exports of goods are also expected to benefit from a favourable external environment, weak external competitiveness will lead to further losses in export market shares. Meanwhile, import growth is expected to slow markedly in 2005, after rising to a high level in 2004 on account of special factors.

The average annual rate of inflation in Greece (based on the Harmonised Index of Consumer Prices – HICP) slowed to 3.0% in 2004, from 3.4% in 2003, mainly because of a decrease in fresh fruit and vegetable prices. Core inflation, however, as measured by the annual rate of change in the HICP excluding energy and unprocessed food, increased further and remained high (3.4% on average, against 3.1% in 2003).

HICP inflation is projected to rise slightly to 3.3% in 2005 as a result of a small recovery in fresh fruit and vegetable prices. In contrast, according to the latest crude oil price projections, fuel prices on the domestic market are expected to increase less this year than in 2004, thus accounting for a smaller direct contribution to inflation than in 2004. Core inflation, as measured by the HICP excluding energy and unprocessed food, is expected to remain roughly unchanged in 2005. The slowdown in the growth of domestic demand and unit labour costs will have a downward effect on consumer prices, which, however, will be counteracted by the upward effect of certain other factors. Import prices should contain inflation less than in 2004, as, in line with the technical assumption used (see Chapter III), the average annual appreciation of the euro in 2005 will be smaller than in 2004. Moreover, it is estimated that some of the indirect effects of the 2004 fuel price increase on the prices of goods and services failed to materialise fully during 2004 and will therefore materialise with a lag in 2005.

The Greek economy faces serious challenges. Specifically, the central government deficit and debt, which reached very high levels as percentages of GDP in 2004, are clearly unsustainable, even without taking into account the projected sharp rise in pension and health spending associated with post-2010 demographic developments. In addition, the rise in private consumption, though likely to remain an important source of growth for a few more years, will inevitably decelerate over the medium term, as household indebtedness will gradually increase and tend to stabilise as a percentage of GDP. Moreover, given the cumulative loss in competitiveness over the last several years, export growth (mostly in the services sector) has largely been sustained by the favourable external environment, which, though expected to remain favourable in 2005, is characterised by a high degree of uncertainty over the medium term.

For these reasons, it is of crucial importance to adopt macroeconomic and structural policy measures to deal with macroeconomic imbalances and foster investment and export-led growth, while the contribution of the social partners is also indispensable. More specifically, policy targets must include:

— *First*, a determined and sustained effort to attain fiscal consolidation: As the large fiscal imbalances are one of the most important and urgent problems that the Greek economy faces today, a large reduction in the fiscal deficit in 2005 and 2006 and sustained fiscal adjustment efforts in the following years are necessary to control the fiscal imbalances on a more durable basis and to achieve a budget surplus and a steady and significant decrease in the public debt in the long term. Fiscal consolidation is a top priority if Greece wants to create a stable macroeconomic environment, which is an essential prerequisite for achieving strong growth, and also because public expenditures will rise in the coming years on account of population ageing, as mentioned above. Unless the fiscal imbalances are addressed decisively, there will be adverse consequences for the viability of the social security and healthcare systems and for the economy as a whole. Fiscal adjustment is also imperative if Greece is to fulfil its obligations under both the Stability and Growth Pact and the Excessive Deficit Procedure according to Article 104 of the Maastricht Treaty, in compliance with the ECOFIN Council Decision of 17 February 2005. Greece must also comply in full with the rules laid down in the Stability and Growth Pact in order to safeguard its credibility.

— *Second*, the contribution of the social partners so that wage increases are in line with productivity growth. This year, the rate of increase in unit labour costs is projected to slow, but will nonetheless remain higher than the corresponding euro area average and inconsistent with the objective of price stability (i.e. a rate of inflation below but close to 2%). Looking forward, as pointed out in past reports, nominal wage increases will have to gradually converge towards the sum of productivity growth in Greece and the average rate of inflation in the euro area (rather than that in Greece), until the inflation differential between Greece and the euro area is essentially eliminated. Until then, the implementation of such a policy would help Greece gain some much needed external competitiveness vis-à-vis its euro area trading partners.

— *Third*, wide-ranging structural reforms to address rigidities in the product and labour markets. The consistent implementation of a well-designed programme of structural reforms, including a reform of the social security system, would contribute to fiscal stability and encourage investment and the development of new productive activities, thereby enhancing economic growth and employment and helping to reduce the unacceptably high rate of unemployment. With specific regard to goods and services markets, the enhancement of competitive conditions encourages productivity improvements and their translation into lower prices for the consumer and lower costs for other producers. Moreover, a more business-friendly environment —through a simplification of the tax system, the establishment of a stable taxation framework, a reduction in bureaucracy and, in general, a more efficient operation of the public sector— is key to encouraging investment and economic activity. Turning to the labour market, the reforms must start from the premises that neither the social support and safety net will be undermined, nor will one social group be favoured at the expense of another, but existing disincentives must be urgently removed and more effective solutions found, which will benefit all groups without compromising basic rights.

Of course, structural adjustment often has painful side-effects, which can and must be alleviated with adequate support measures. Accordingly, there is a need for a broad public dialogue with a view to securing social consensus on the reforms (including the reform of the social security system). Such a consensus should be achievable considering that the economy as a whole could benefit enormously. By contrast, if the economic policy and the social partners fail to move in the direction outlined above, this would have serious negative implications for growth and living standards in Greece.

II. The international economic environment and economic developments and prospects in the euro area

1. The international economic environment[1]

1.1 Overview

The international economic environment was generally favourable in 2004, marked by further improvement over 2003. Global GDP growth (at constant prices) sped up from 3.9% in 2003 to 5.0% in 2004 —its highest level since 1976— while overall inflation remained low. The global expansion is projected to continue in 2005 and 2006, though at a somewhat weaker, closer-to-trend rate of 4%. The sustainability of such strong growth rates is nonetheless subject to considerable uncertainty and risks, mainly on account of the accumulated global imbalances and oil market developments.

For the first time in several years, world economic activity was marked by the acceleration of GDP growth across the advanced economies to 3.6% on average, from 2.1% in 2003. Against a backdrop of a global environment marked by historically low interest rates, this acceleration was mainly driven by improving business confidence and investment and a rise in private consumption. It was supported by robust growth of world trade in both advanced and emerging market and developing economies.[2] The emerging market and

1 The estimates and projections given for 2004-2005 are based on data available until mid-February 2005. In some cases where more recent information was not available, data were also drawn from the following sources: the OECD *Economic Outlook* (November 2004), the European Commission's *Autumn Forecasts* (October 2004) and the *World Economic Outlook* (September 2004) of the International Monetary Fund (IMF). The global GDP estimates quoted in this section were computed by the IMF on the basis of purchasing power parity weights.
2 The term "emerging market and developing economies" was introduced by the IMF in April 2004 to designate the economies that are not part of the group of the 29 advanced economies. This term encompasses the transition economies (countries of Central and Eastern Europe, countries of the Commonwealth of Independent States – former USSR) and the developing economies (in Africa, Asia, Latin America and the Western Hemisphere).

Table II.1
Real GDP: Latest available forecasts of the IMF, the European Commission, the OECD and Consensus Economics
(Annual percentage changes)

	2004 (estimates)				2005 (forecasts)			
	IMF 29.9.04	Eur. Com. 26.10.04	OECD 17.2.05	Consensus 14.2.05	IMF 29.9.04	Eur. Com. 26.10.04	OECD Dec. 04	Consensus 14.2.05
World economy*	5.0	5.0	-	3.9	4.3	4.2	-	3.0
USA	4.3	4.4	4.4	4.4	3.5	3.0	3.3	3.5
Japan	4.4	4.2	2.6	2.9	2.3	2.1	2.1	1.1
China	9.0	9.2	9.2[1]	-	7.5	8.2	8.0	-
United Kingdom	3.4	3.3	3.1	3.1	2.5	2.8	2.6	2.5
Euro area	2.2	2.1	1.8	2.0	2.2	2.0	1.9	1.7

1 OECD, December 2004.
* Based on purchasing power parities for 2003 (with the exception of Consensus Economics, whose calculations are based on exchange rates for 2000).
Sources: IMF, *World Economic Outlook*, September 2004. European Commission, *Autumn 2004 Economic Forecasts*, October 2004. OECD, *Economic Outlook*, December 2004, and *An interim assessment*, 17.2.2005. Consensus Economics, *Consensus Forecasts*, February 2005.

developing economies saw their already robust GDP growth rate of 6.1% in 2003 pick up to 6.6% in 2004. Among the larger countries, the strongest GDP growth in 2004 was recorded by the developing economies of China (9.5%) and India (6.4%) and the advanced economies of the United States, the United Kingdom and Japan. GDP growth in the euro area picked up by more than one percentage point to 2.0% in 2004 (according to Eurostat's flash estimates), but nonetheless remained weaker than in the other advanced economies (see Table II.1).

The impact of the recent sharp rise in oil prices on the global economy has been moderate, compared with the shock experienced during the first and second oil crises of the 1970s. This outcome can be explained by the smaller size of the recent oil price increase in real terms, compared with the earlier shocks, and by the increased ability of many economies to cope with such shocks, in the light of developed economies' reduced dependence on oil. Indeed, research studies[3] indicate that the oil dependency of developed economies, measured as the quantity of oil used per unit of real GDP, is currently one half of what it was during the 1970 oil crises. However, less developed economies, such as China with its substantial oil consumption, continue to be heavily dependent on oil.

The outlook for the global economy remains encouraging for 2005 and 2006, in spite of the significant downside uncertainties. Interest rates remain very low by historical standards, in spite of the successive increases in key short-term interest rates by some advanced economies. Meanwhile, other factors that had favourably affected the economic cycle of the global economy in 2003-04 are expected to remain in place in 2005-06. Earlier projections made in September 2004 by the International Monetary Fund indicated that global GDP would increase at a rate of 4.3% in 2005.[4] However, the projections have since been revised downwards, to closer to 4.0%, owing to the persistence of higher-than-expected oil prices and a

3 See, for instance, OECD, *Economic Outlook*, November 2004.
4 Similarly, the European Commission (October) projected global GDP growth to reach 4.2%.

decrease in quarterly GDP growth in some of the large economies in the second half of 2004. The growth of global GDP at such a rate seems sustainable for 2005 so long as there are no further large oil price increases or any disorderly adjustment in the global economic imbalances.

From a regional perspective, the economic outlook for 2005 can be described as follows: GDP growth in the United States is expected to slow to between 3.3% (OECD) and 3.5% (IMF), i.e. to close to potential, from 4.4% in 2004. In Japan, GDP growth is projected to drop to between 2.1% and 2.3%, from 2.6% in 2004, as the relative contribution of exports to economic growth gradually declines. It should be noted, however, that the respective share of domestic demand increases. The latest Consensus Economics forecasts (14 February 2005) show a downward revision of Japan's GDP growth prospects to 1.1% for 2005. In the United Kingdom, GDP growth is expected to moderate to 2.8%, from 3.1% in 2004. In China, a tightening of monetary policy, combined with certain administrative measures aimed at curtailing investment in specific industrial sectors, is expected to rein in the vigorous growth rate to 7.5% in 2005 (from 9.5% in 2004). In Latin America, GDP growth is projected to remain robust at 3.6%, though weaker than last year (4.6%), when the region made an impressive economic rebound.

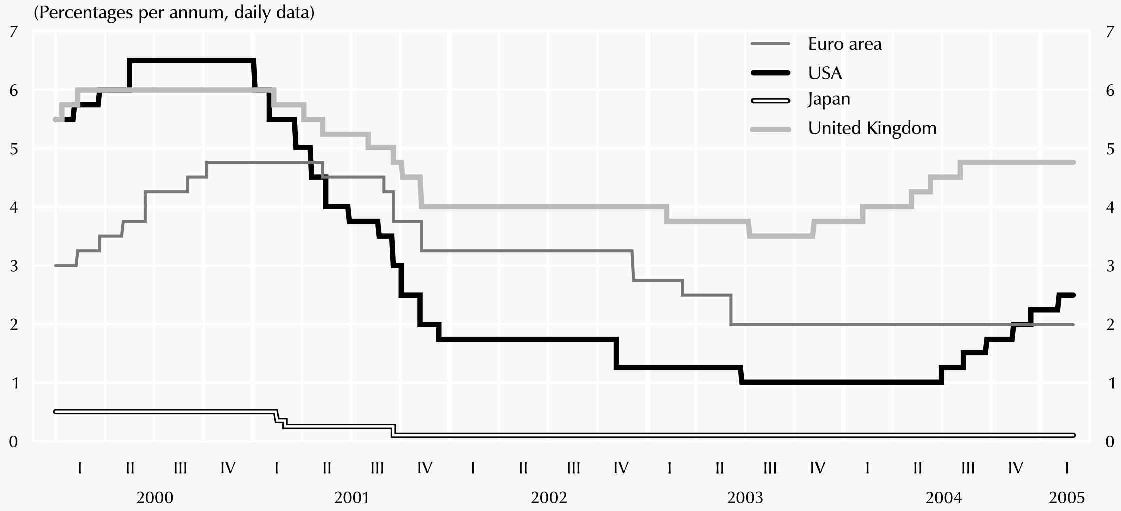
The quiescence of global inflation at relatively low levels, in spite of the strong upturn of real growth and the sharp rise in oil prices, has allowed monetary policy to remain accommodative, although some moves were made towards a tighter stance. Moreover, the expansionary stance of monetary policy implemented over the past 2-3 years by the central banks of several advanced economies continued to have a significant —lagged— impact on economic activity. Monetary policy in 2004 became less expansionary in the United States and more restrictive in the United Kingdom. The ECB maintained its key policy rates unchanged from June 2003 onwards (see Section 3 below), while the stance of Japan's monetary policy remained highly accommodative. The US Federal Reserve, which had cut its targeted interest rate (i.e. the federal funds rate) a number of times from January 2001 to June 2003 and then maintained it at a 45-year low of 1% for roughly one year, has since reverted to interest rate increases, judging that economic recovery in the US is well-entrenched, as supported by the release of strong employment figures. The targeted federal funds rate was raised six times, by 25 basis points on each occasion: five of the hikes occurred in the second half of 2004 and the other on 2 February 2005, when the rate was brought up to 2.50%. In the United Kingdom, the initial move towards monetary tightening occurred on 6 November 2003, amid robust private consumption and strong rises in real estate prices. The Bank of England raised its key short-term interest rate (repo rate) an additional four times in the course of 2004, bringing it up to 4.75% on 5 August (see Chart II.1). In contrast, the Bank of Japan maintained its zero interest rate policy, amid concerns that the persistence of deflationary trends had not dissipated; as a result, the monetary base continued to rise sharply.

Even though fiscal policy in the major advanced economies remained generally accommodative in 2004, fiscal deficits did not worsen, on account of the favourable economic conjuncture. After three years of deterioration, the general government deficit in the 7 largest advanced economies (G-7) as a whole is estimated to have stabilised at 4.5% of GDP in 2004, compared with 4.6% in 2003 and only 0.2% in 2000. However, the cyclically-adjusted deficit continued to widen, reaching 3.9%

Chart II.1

Central bank key rates (1 January 2000 - 20 February 2005)

(Percentages per annum, daily data)

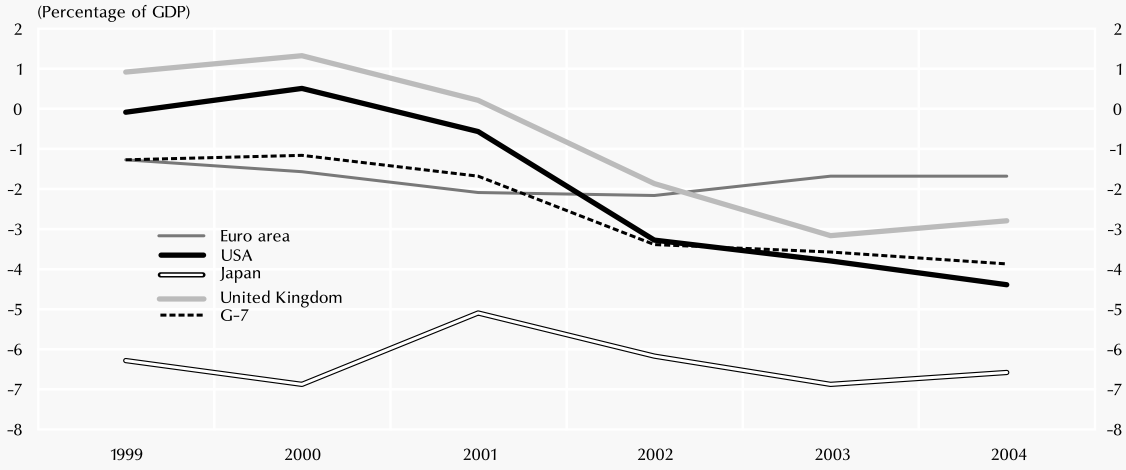


Sources: For the euro area: ECB, minimum bid rate on the main refinancing operations. For the USA: Federal Reserve targeted federal funds rate. For Japan: Central Bank of Japan, official discount rate. For the United Kingdom: Bank of England, repo rate.

Chart II.2

Cyclically adjusted fiscal balance (1999-2004)

(Percentage of GDP)



Note: Cyclically adjusted fiscal balance at general government level. G-7: The 7 most advanced economies. For the euro area and the United Kingdom: excluding one-off proceeds from the sale of mobile phone licenses. The euro area is here understood as not including Luxembourg.

Source: IMF, *World Economic Outlook*, September 2004.

of potential output in 2004, from 3.6% in 2003 and 1.2% in 2000 (see Chart II.2). Fiscal policy in the advanced economies will most likely be tightened in 2005, as the cyclically-adjusted deficit of the G-7 is, according to the IMF, expected to be reduced by 0.5 percentage point of GDP in the course of the year.

The main downside risks to the sustainability of strong global growth are oil price volatility and the global economic imbalances. Whereas the effect of high oil prices has been rather limited until now, further increases or even the persistence of permanently high levels of oil prices are likely to have an impact both on inflation, through second-round effects, and on economic activity. Meanwhile, the large and widening US current account deficit has exerted downward pressure on the dollar and poses a risk to the continuation of robust growth. The objective, announced by the US administration, of halving the US budget deficit over the next five years[5] is a necessary, but not a sufficient condition to reduce the current account deficit to sustainable levels. Such an improvement would also require an increase in net private savings.

1.2 International trade and commodity prices

The *volume of world trade* in goods and services in 2004 registered its highest growth rate since 2000 (8.8%, against 5.1% in 2003). The strongest import and export growth was recorded by emerging market and developing economies (11.8%), while the corresponding rates in the advanced economies in 2004 stood around 8%.

Commodity prices increased significantly in 2004 for the second year in a row. More specifically, non-fuel commodity prices, in US dollars, picked up at a quicker pace in 2004 (16.8%) than in 2003 (7.1%). Metals were the commodity with the sharpest annual price increase rate (31.2%, against 11.9% in 2003). The brisk rise in commodity prices is mainly the result of the robustness of economic activity in all of the economic regions, in particular China. Additionally, the rise in international commodity prices is, in part, attributable to the depreciation of the US dollar. When these prices are expressed in Special Drawing Right (SDR) terms, the annual rate of increase in the composite IMF commodity price index falls to 11.3%, from 16.8%, while, when they are expressed in euro, the increase is reduced further to 8.5%.

International oil prices followed an upward course throughout 2004, registering their sharpest increases from July to October. This development was mainly driven by the strength of global demand, estimated by the International Energy Agency (IEA) to have reached an annual growth rate of 3.4% in 2004, i.e. its highest level in three decades. Other factors underlying the rise in international oil prices were the limited supply of high-quality oil reserves, unfavourable weather conditions (mainly in the Gulf of Mexico) which disrupted fuel distribution by sea, heightened uncertainty about the security of oil production facilities and exports from the Middle East, and the political crisis in Nigeria and Venezuela. Brent crude oil prices, in US dollar terms, increased at an average annual rate of 33.5% in 2004 (21.5% in euro terms), compared with a 13.3% increase in 2003 (–5.3% in euro).

According to the latest forecasts for 2005, the average annual price of Brent crude will reach $44 per barrel, from $38 in 2004.[6]

2. Macroeconomic developments and prospects in the euro area[7]

For 2004 as a whole, the euro area continued to experience an economic upswing, amid a slowdown in GDP growth in the second half of the year. Inflation remained above 2% during most of the year, but is expected to fall below 2% in the course of 2005. According to Eurosystem staff projections, GDP growth should range

5 See the US President's "State of the Union" address of 2 February 2005.
6 See Chapter III.2.
7 The references to the economic outlook for 2005 are based on the European Commission's *Autumn Projections* (October 2004) and the Eurosystem Staff Projections (ECB, *Monthly Bulletin,* December 2004), while more recent data have been taken into account where available.

between 1.4% and 2.4%[8] (1.9%-2.0% according to OECD and European Commission estimates). Employment is expected to increase by 0.9% over 2004.

2.1 Inflation

Average annual euro area inflation, measured in HICP terms, was 2.1% in 2004, unchanged from 2003. Inflation remained above 2% over most of 2004, mainly because of the sharp rise in oil prices, while the lagged effect of the past appreciation of the euro is estimated to have contained the rise in import prices in 2004. Inflation peaked at 2.4% in October, its highest level since May (2.5%), and decreased to 2.2% in November before rising back to 2.4% in December. Core inflation (i.e. the HICP excluding energy and unprocessed food prices) also reached 2.1% in 2004 (against 2.0% in 2003). This persistence of inflation above 2% in 2004 is attributable *inter alia* to increases in indirect taxes and administered prices in several euro area countries. According to Eurostat's flash estimates, euro area HICP inflation fell to 2.1% in January 2005.

According to the Eurosystem Staff Projections (December 2004), euro area inflation is projected to fall back below 2% in 2005 (the average annual increase is forecast to range between 1.5% and 2.5%), since both external and domestic inflationary pressures are expected to subside. Specifically, the rate of increase in HICP excluding energy is expected to ease in 2005. This prospect reflects estimates that the rise in import prices will be limited and that pressures from internal costs will remain subdued. Wage moderation and the particularly low rates of increase in labour costs which have characterised the euro area labour market over the past few years are also projected to continue. (In 2004, average nominal earnings and unit labour costs in the euro area increased by roughly 2% and 0.5% respectively[9].) These projections are based on the appraisal that the second-round effects of the rise in oil prices on nominal wages will continue to be contained. Furthermore, upward pressure on prices from the increase in indirect taxes and administered prices observed in certain countries in 2004 and from the rise in oil prices is expected to moderate.

2.2 Economic activity

The economic recovery in the euro area continued in 2004, with GDP growth estimated to have reached 2.0%,[10] compared with 0.6% in 2003. However, quarter-on-quarter GDP growth lost momentum in the course of the year, as the sharp rise in oil prices, which fed into inflation and reduced real household income, had a dampening effect on private consumption, while net exports were negatively affected by the appreciation of the euro. An encouraging development came from the pick-up in the quarter-on-quarter growth of investment to 0.7% in the third quarter, from 0.3% in the second. This upswing in investment is attributable to continued favourable financing conditions, the improvement in the financial situation of firms and enhanced profitability prospects. According to provisional estimates, quarter-on-quarter GDP growth in the euro area fell to 0.2% in the fourth quarter, reflecting mainly the negative growth rates of Germany (–0.2%) and Italy (–0.3%), while relatively strong fourth-quarter growth rates were observed in France (0.7%) and Spain (0.8%). The European Commission's latest projection (15 February

8 The results of the Eurosystem Staff Projections for each variable are given in range form, in order to express the uncertainty surrounding the projections. These ranges are based on the differences between actual outcomes and previous projections carried out by euro area central banks over a number of years. The width of the ranges is twice the average absolute value of these differences.
9 Based on data for the first three quarters.
10 Eurostat flash estimates.

2005) based on short-term indicators places the quarterly euro area GDP growth rate for the first and the second quarter of 2005 between 0.2% and 0.6%.

GDP growth in 2005 is projected to maintain the same momentum as in 2004 and to pick up slightly more in 2006. According to Eurosystem Staff Projections, real GDP growth is expected to range between 1.4% and 2.4% in 2005 and between 1.7% and 2.7% in 2006. The European Commission projects GDP growth to reach 2% in 2005 and 2.2% in 2006, while the OECD projects even higher GDP growth for 2006 (2.5%, up from 1.9% in 2005).[11]

The ECB's projections of a continuation of economic recovery in the euro area in 2005 and 2006 are supported by the likely developments in the global economy and by internal factors. These projections are, however, subject to significant downside uncertainties.

More specifically, the growth rates of both the global economy and world trade are expected to remain vigorous, albeit at somewhat lower, more sustainable levels than in the prior several years, thus providing a continued boost to euro area exports. According to the Eurosystem staff macroeconomic projections, the export markets of the euro area should see their growth rates slow slightly, to 8%, in 2005, from an estimated rate of 8.7% for 2004. Moreover, the combination of low interest rates, favourable financing conditions for firms, the anticipated drop in oil prices (over a two-year horizon) and the deceleration of inflation is expected to boost investment and consumer demand. In this respect, it is projected that in 2005 euro-area private consumption will increase by almost 2% (against 1.5% in 2004) and total investment growth will reach 3% (against 2.2%). As noted, however, there are downside risks associated with these projections, notably the possibility of a further increase in oil prices, a continued appreciation of the euro and the economic impact of an abrupt adjustment in the accumulated global imbalances.

2.3 Labour market

Euro area labour market developments in 2004 were marked by sluggish employment growth, likely a result of the limited negative impact of the protracted economic slowdown of the previous years on the labour market. Employment growth in the euro area is estimated to have accelerated by a mild 0.5% in 2004, which, in absolute terms, translates into 600,000 new jobs, compared with 0.2% in 2003. The unemployment rate is estimated to have remained stable at 8.9%.

Employment growth is expected to pick up to 0.9% this year. This estimate (a) reflects the projections of sustained GDP growth at close to 2% in 2005 and (b) takes into consideration the usual time lags with which the economic conjuncture usually affects the labour market. The unemployment rate is expected to remain broadly stable at 8.9% in 2005, reflecting the concurrent increases in both job creation and labour supply; with real growth expected to pick up in 2006, the unemployment rate is projected to decrease to 8.6% that year.

A comment is in order regarding labour market developments in the European Union and the euro area, in relation to the Lisbon objectives. Based on the latest forecasts, most economies

11 The Eurosystem Staff Projections were based on the assumption that oil prices would rise from \$39.3 per barrel in 2004 to \$44.4 in 2005, before declining to \$40.8 in 2006. The technical assumption of constant exchange rates implies that the euro/dollar exchange rate remains at 1.29 over the projection horizon. The European Commission adopted similar assumptions for oil price developments, while its technical assumption regarding stable exchange rates placed the dollar/euro exchange rate at 1.23.

(including the four largest euro area members) are not expected to meet the interim target set for 2005, putting the 2010 objective in jeopardy. This view is reflected in the Kok report,[12] which shows that progress towards the specific targets of achieving an employment rate of 67% by 2005 and of 70% by 2010 has been slow.

2.4 Fiscal developments

The fiscal position of the euro area as a whole deteriorated further in 2004, as the general government deficit-to-GDP ratio is estimated to have risen to 2.9%, from 2.7% in 2003, while the cyclically adjusted deficit similarly increased to 2.5% of GDP from 2.2% in 2003. The ratio of the general government debt to GDP in the euro area also worsened, from 70.7% in 2003 to 71.1% in 2004. The fiscal policy stance in the euro area, after being slightly expansionary in 2004, is expected to become slightly restrictive in 2005, as the nominal and the cyclically adjusted deficits are projected (by the European Commission) to fall to 2.7% and 2.1%, respectively. The general government debt in 2005 is expected to remain unchanged (at 71.1% of GDP).

The projected decrease in the cyclically adjusted deficit this year is indicative of the euro area countries' commitment to achieve the medium-term objective of a budgetary position close to balance or in surplus, as set out in the Stability and Growth Pact. This projection for the euro area as a whole is based on similar forecasts of a reduction, in individual economies, of the general government cyclically adjusted deficit in 2005 (by 0.5 percentage point of GDP in Germany, 0.7 in France, 1.7 in Greece and 0.4 in the Netherlands).

In accordance with the Excessive Deficit Procedure launched against all four of the aforementioned euro area countries, the ECOFIN Council recommended to the national authorities in question to put an end to their present excessive deficit situations.[13] According to European Commission estimates, the fiscal deficit of the Netherlands was reduced to 2.9% in 2004 and will be further cut back in 2005. The European Commission also re-assessed the fiscal situation and outlook for France and Germany and, on 14 December 2004, announced that no further steps were necessary at this point under the Excessive Deficit Procedure in both instances, as both countries have committed themselves to correcting the excessive deficit problem by end-2005, commitments which have been included in their respective national budgets for 2005. As stated in the communication, the EU Commission would have to recommend to the ECOFIN Council to enhance the budgetary surveillance and to take the necessary action, if the envisaged correction measures taken by both countries should, at a later stage, prove to be insufficient. In its 18 January 2005 session, the ECOFIN Council examined the excessive deficits of France and Germany and agreed with the Commission that further steps under the Excessive Deficit Procedure were at that point unnecessary in both cases. The ECOFIN Council also pointed out in its conclusion that it remains ready, in cooperation with the Commission, to take the warranted measures whenever necessary. The details of the Excessive Deficit Procedure launched against Greece are reported in Box VI.1. The Commission, in its communication to the ECOFIN and the European Parliament on 12 December 2004, also laid down the governance strategy it intends to follow in an aim to upgrade

12 See "Facing the challenge - The Lisbon strategy for growth and employment". Report from the High Level Group chaired by Wim Kok, November 2004.

13 Apart from these euro area countries, the Excessive Deficit Procedure has been launched against six of the recently acceded EU members, namely Cyprus, the Czech Republic, Hungary, Malta, Poland and Slovakia. the ECOFIN has warned these countries about the need to drastically reduce their deficits.

the quality of budgetary statistics used for EU fiscal surveillance purposes.[14]

According to the updated stability programmes, the euro area general government deficit is projected to improve from 2.8% of GDP in 2004 to 2.3% in 2005, i.e. to a level slightly lower than projected by the European Commission. In general terms, the stability programmes set objectives for the further reduction of the fiscal deficits from 2006 onwards, usually based on the assumption that GDP growth will be close to or slightly above potential.

2.5 The exchange rate of the euro and Exchange Rate Mechanism II

The *euro exchange rate* strengthened for the fourth consecutive year in 2004, though less than in 2003. The broad index of the nominal effective exchange rate of the euro,[15] which had risen by an average 12.4% in 2003, gained an additional 4.1% in 2004. The appreciation of the euro in 2004 reflects its strengthening mainly against the US dollar and, to a lesser extent (owing to lower weighting coefficients) against the yuan (which is pegged to the dollar) and the yen. The upward course of the euro's weighted exchange rate was, however, moderated by developments in the bilateral exchange rate of the euro against the pound sterling.

The euro continued to gain ground against the *US dollar* in 2004. The dollar's bilateral exchange rate against the euro rose by 10% in average annual terms (or by 9.1% December-on-December). The total appreciation of the euro vis-à-vis the US currency, from the historically low levels of June 2001 (0.8532 dollar to the euro) to the historic high of 1.3408 dollars to the euro in December 2004, amounts to 57.1%. This weakening of the dollar steepened in the last quarter of 2004, when it more than offset a prior appreciation (from March to June). Market analysts attribute the continued depreciation of the US currency mainly to the increasing importance placed by international markets on the risks posed by the very large and deteriorating US current account deficit (5.4% of GDP in 2004, against 4.8% of GDP in 2003), which, in turn, is linked with the very high fiscal deficit and the very low savings of households in the United States. In these conditions of high and rising US current account deficit-to-GDP ratios, the possibility of an abrupt adjustment of global imbalances remains a concern. In January 2005, the dollar regained some of the ground it had lost in 2004, with its exchange rate against the euro rising to $1.31, from $1.34 in December and an average $1.24 in 2004. The strengthening of the dollar against the euro at the beginning of this year is attributable to the market expectations of a further widening of interest rate differentials in favour of US-dollar denominated financial instruments, in conjunction with the projected pick-up in GDP growth in the US, as well as the US government's commitment (announced in January 2005) to drastically reduce the fiscal deficit over the next five years.

As regards *other currencies,* the euro also appreciated slightly in 2004 against the yen. The bilateral euro/yen exchange rate was marked by small fluctuations during most of the year (mainly between 132 and 135 yen to the euro, see Chart II.3), but the Japanese currency lost considerable ground against the euro in the last quarter of the year. This latter development is to some extent associated with the greater-than-anticipated slowdown in the recovery of the Japanese economy. In

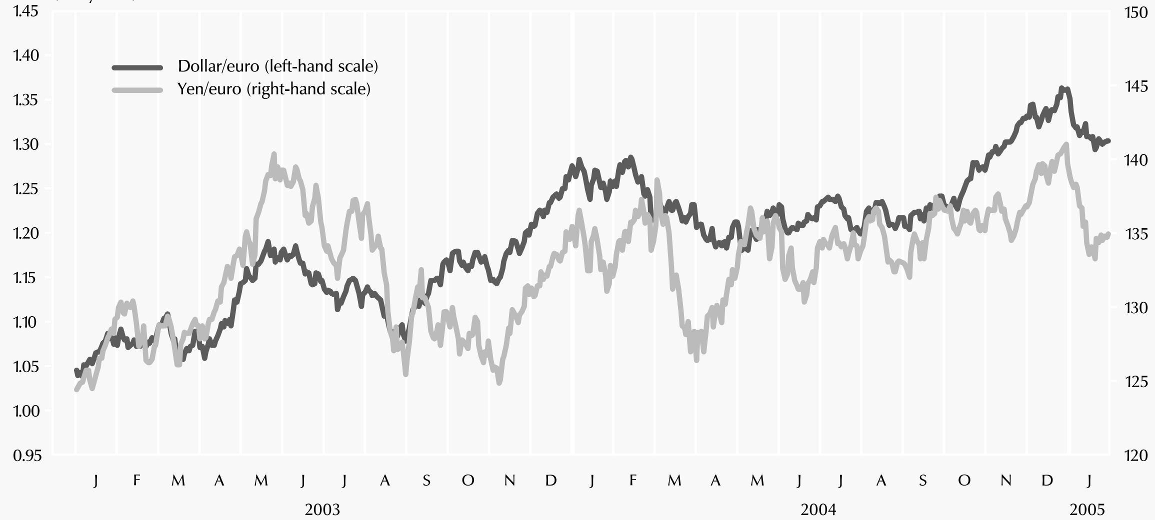
14 Communication of the Commission to the Council and the European Parliament "Towards a European Governance Strategy for Fiscal Statistics", Brussels, 22 December 2004.

15 The bilateral exchange rates of the euro are weighted on the basis of the relative shares of the 42 largest partners in the external trade of the euro area.

Chart II.3

Exchange rate of the euro against the US dollar and the Japanese yen

(Daily data)

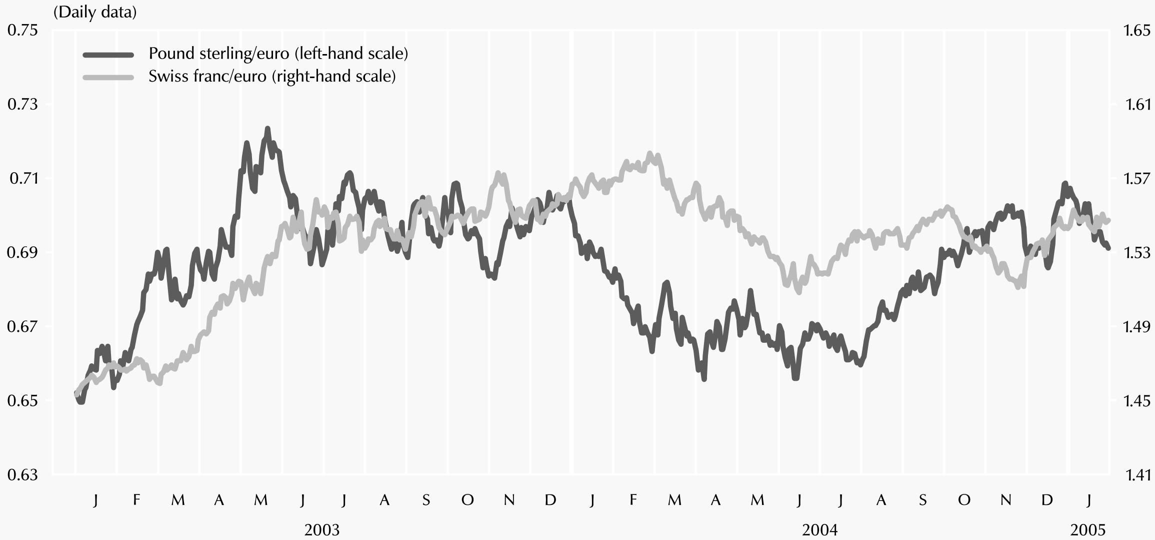


Sources: ECB and Bank of Greece.

Chart II.4

Exchange rate of the euro against the pound sterling and the Swiss franc

(Daily data)



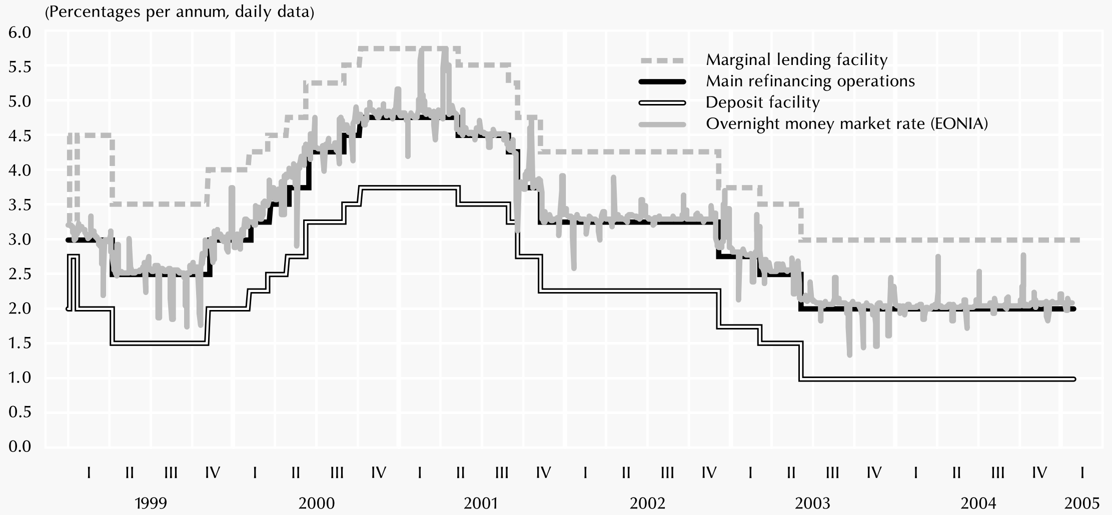
Sources: ECB and Bank of Greece.

December 2004, the euro had gained 5.9% against the yen from its average level of 2003. However, in average annual terms, the ground gained by the euro against the yen was 2.6% less. Also in average terms, the euro lost 2.9% against the pound sterling in 2004, but gained 1.5% against the Swiss franc.

Within the Exchange Rate Mechanism II (ERM II), the Danish krone and the Slovenian tolar, which jointed ERM II in 2004, fluctuated within narrow bands, close to their central parities. The Estonian kroon and the Lithuanian litas, both of which also joined ERM II in 2004, were unchanged relative to their ERM-II central parities, in line with those

Chart II.5

ECB interest rates and the overnight money market rate (EONIA)
(1 January 1999 - 10 February 2005)
(Percentages per annum, daily data)



Source: ECB.

countries' unilateral commitments to maintain currency board arrangements within the standard ERM II fluctuation band.

3. Monetary developments and policy in the euro area

3.1 The monetary policy of the ECB

ECB key interest rates remained unchanged in 2004 at the low levels reached following the last cut on 6 June 2003. More specifically, the minimum bid rate on the main refinancing operations remained at 2%, the marginal lending facility rate at 3% and the deposit facility rate at 1% (see Chart II.5 and Table II.2). On the basis of the economic and monetary analysis, the Governing Council of the ECB has estimated that, despite the short-term effects of high oil prices on the price level in the second half of 2004, there are no signs that inflationary pressures will strengthen over the medium term and overall economic conditions remain in line with price stability (see Sections 2.1 and 2.2). However, the ECB has repeatedly emphasised the need for vigilance with regard to developments that might entail inflationary risks. These risks are mainly related to the possibility of a further rise in oil prices and of significant second-round effects on nominal wages, though such effects have been limited so far. Furthermore, it has been noted that liquidity in the euro area remains higher than needed to finance non-inflationary growth and could have an upward impact on inflation over the medium term, given also that the low level of interest rates continues to fuel credit expansion to the private sector.

3.2 The evolution of M3 and its counterparts

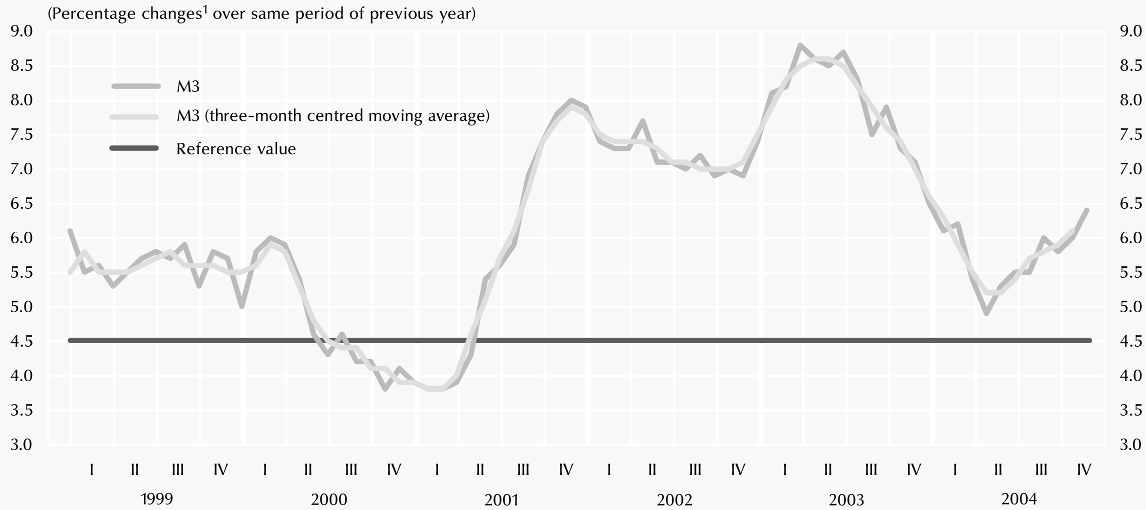
In the first half of 2004, the annual growth rate of M3 continuously slowed, something which was reversed in the second half. In particular, it fell to 5.3% in the second quarter of 2004, from 7.5% in the last quarter of 2003 (see Chart II.6 and Table II.3). This development largely reflected portfolio shifts to longer-term assets, against a background of improved financial market conditions. In the

Table II.2
Changes in key ECB interest rates
(Percentages per annum)

Date of interest rate change[1]	Deposit facility	Main refinancing operations	Marginal lending facility
6 December 2002	1.75	2.75	3.75
7 March 2003	1.50	2.50	3.50
6 June 2003	1.00	2.00	3.00

1 For the deposit and marginal lending facilities, effective dates of interest rate changes (one day following the relevant ECB decision); for the main refinancing operations, interest rate changes are effective from the first operation following the date indicated.
Source: ECB.

Chart II.6
M3 in the euro area (January 1999 - December 2004)
(Percentage changes[1] over same period of previous year)



1 Adjusted for seasonal and calendar effects.
Source: ECB.

second half of 2004, however, the growth rate of M3 accelerated and reached 6% in the fourth quarter. The level of interest rates resulted in a low opportunity cost of holding money[16] and fuelled in particular the demand for assets included in M1, thereby offsetting portfolio shifts towards longer-term financial assets, i.e. assets not included in M3. It is worth noting that portfolio restructuring continued, but at a slower pace than expected, as investors remained cautious about investing in higher-risk assets, following the adverse stock market developments of recent years. Moreover, demand for euro banknotes by both euro area residents and non-residents remained high. Thus, the annual growth rate of M1 stood at high levels throughout 2004 (fourth quarter of 2004: 9.3%, fourth quarter of 2003: 11%, see Table II.3).

The most recent developments in M3 growth mainly reflect the strengthening of credit expansion to the private sector in the second half of

16 The opportunity cost of holding money is measured by the ECB as the difference between the 3-month EURIBOR and the weighted average of the rates of return on M3 components (own rate of return of M3).

T a b l e II.3

Main components of M3 in the euro area

(Annual percentage changes,[1] derived from data adjusted for seasonal and calendar effects, quarterly averages[2])

	2003	2004				
	Q4	Q1	Q2	Q3	Q4	December
M1	**11.0**	**11.0**	**10.2**	**9.6**	**9.3**	**8.4**
Currency in circulation. M0	26.5	24.0	21.6	20.3	19.1	17.0
Overnight deposits	8.7	9.1	8.5	7.9	7.6	6.9
Other short-term deposits (=M2–M1)	**4.8**	**3.3**	**1.7**	**2.0**	**3.4**	**4.5**
Deposits with an agreed maturity of up to two years	–3.0	–4.4	–7.0	–5.9	–2.3	0.4
Deposits redeemable at notice of up to three months	11.0	9.2	8.1	7.6	7.4	7.3
M2	**7.9**	**7.2**	**6.0**	**5.8**	**6.4**	**6.5**
Marketable instruments (=M3–M2)	**5.6**	**2.2**	**1.9**	**3.9**	**3.7**	**6.3**
Repurchase agreements	–1.6	–4.0	–1.7	2.9	2.9	9.8
Money market fund shares/units	12.8	8.5	5.9	4.3	4.3	3.5
Money market paper and debt securities issued with a maturity of up to two years	–13.2	–16.2	–11.7	3.8	2.1	15.8
M3	**7.5**	**6.4**	**5.3**	**5.6**	**6.0**	**6.4**

1 Annual rates of change in the corresponding index, which is compiled on the basis of outstanding stocks for December 2001 and cumulative monthly flows, adjusted for exchange rate variations, reclassifications etc.

2 The quarterly average is derived from monthly averages (which are calculated as arithmetic means of two successive end-of-month figures) and is not the three-month average of end-of-month annual growth rates (see the "Technical Notes" in the ECB *Monthly Bulletin*).

Source: ECB.

2004. In the main, it is the low level of interest rates in the euro area that lies behind the increased demand for loans by the private sector, which account for the bulk of total credit and grew at 6.8% in the fourth quarter of 2004, compared with 5.3% in the fourth quarter of 2003 (see Table II.4). According to the results of the latest Eurosystem bank lending survey (January 2005),[17] in the fourth quarter of 2004, despite the downward revision of bank perceptions with regard to the economic outlook, the percentage of banks that reported a tightening of credit standards for loans to enterprises and households was smaller than the percentage of banks that reported an easing of credit standards. This development can be attributed to increased competition among credit institutions and confirms the general improvement in financing conditions. The higher growth rate of loans to the private sector is a consequence of the continuous pick-up in the rate of increase in loans to households (December 2004: 7.8%, December 2003: 6.4%), particularly housing loans, due to the ongoing increase in dwelling prices in some euro area countries. Moreover, after a continuous slowdown up to the first quarter of 2004, the annual growth rate of bank loans to non-financial corporations accelerated in the following months (December 2004: 5.4%, December 2003: 3.5%). It is worth noting that, despite the effort of enterprises to limit their borrowing in order to improve their gearing ratios, the improvement in financing conditions and economic conditions in the euro area led to a recovery of bank loan demand. Moreover, the annual growth rate of the outstanding amount of debt securities issued by non-financial corporations dropped considerably in 2004 to 3.3% in the fourth quarter of the year, compared with 9.9% in the last quarter of 2003.

The annual rate of credit expansion to general government fluctuated at high levels in the first

17 See ECB website, www.ecb.int, and ECB, *Monthly Bulletin,* February 2005 (Box 1).

T a b l e II.4
Main counterparts of M3 in the euro area
(Annual percentage changes,[1] derived from data adjusted for seasonal and calendar effects, quarterly averages[2])

	2003	2004				
	Q4	Q1	Q2	Q3	Q4	December
Longer-term financial liabilities of MFIs	**5.9**	**6.2**	**7.4**	**7.6**	**7.9**	**8.1**
Deposits with an agreed maturity of over two years	5.1	5.5	6.4	7.1	7.7	8.3
Deposits redeemable at notice of over three months	–14.0	–11.5	–8.5	–4.4	–1.8	–1.2
Debt securities issued with a maturity of over two years	8.7	9.6	10.6	10.3	10.4	10.6
Capital and reserves	4.4	3.3	4.9	4.5	4.4	4.4
Credit to euro area residents	**5.8**	**5.8**	**6.0**	**6.2**	**6.0**	**6.0**
Credit to general government	**6.6**	**6.0**	**6.4**	**6.4**	**3.8**	**2.4**
– Debt securities other than shares	9.9	9.1	9.0	8.9	5.7	4.2
– Loans	1.5	1.2	2.3	2.3	0.7	–0.7
Credit to other euro area residents	**5.6**	**5.7**	**5.9**	**6.2**	**6.6**	**7.0**
– Debt securities other than shares	15.8	12.3	9.0	9.7	6.8	8.2
– Shares and other equity	3.6	4.9	7.2	3.6	4.3	5.3
– Loans	5.3	5.4	5.6	6.2	6.8	7.0

1 Annual rates of change in the corresponding index, which is compiled on the basis of outstanding stocks for December 2001 and cumulative monthly flows, adjusted for exchange rate variations, reclassifications etc.
2 The quarterly average is derived from monthly averages (which are calculated as arithmetic means of two successive end-of-month figures) and is not the three-month average of end-of-month annual growth rates (see the "Technical Notes" in the ECB *Monthly Bulletin*).
Source: ECB.

three quarters of 2004 (ranging from 6% to 6.4%) due to higher public sector borrowing requirements in some countries of the euro area. However, in the fourth quarter it fell significantly to 3.8%. The annual growth rate in the outstanding balance of debt securities issued by general government in the euro area countries accelerated to 5.8% in the third quarter of 2004, compared with 5.4% in the last quarter of 2003, but subsided to 5.1% in the fourth quarter of 2004.

3.3 Money market interest rates, bank rates and long-term government bond yields

Interest rates in the single euro area money market remained at low levels in 2004 (see Chart II.7), reflecting stable key ECB interest rates during this period. In particular, the overnight interest rate in the interbank market (EONIA) fluctuated within a narrow range close to the ECB minimum bid rate on main refinancing operations, which has remained unchanged since June 2003 (see Chart II.5). The three-month EURIBOR, which is the most representative short-term money market rate in the euro area, also fluctuated around historically low levels (see Chart II.7) and on some days in March 2004 it even fell below 2%. Afterwards, it stabilised at a slightly higher level (January 2005: 2.15%). The money market yield curve, as measured by the spread between twelve- and one-month EURIBOR rates, flattened slightly in January 2005, compared with December 2003 (see Charts II.7 and II.8). However, in the course of the year it was subject to significant fluctuations, which were almost exclusively due to the evolution of the twelve-month EURIBOR.

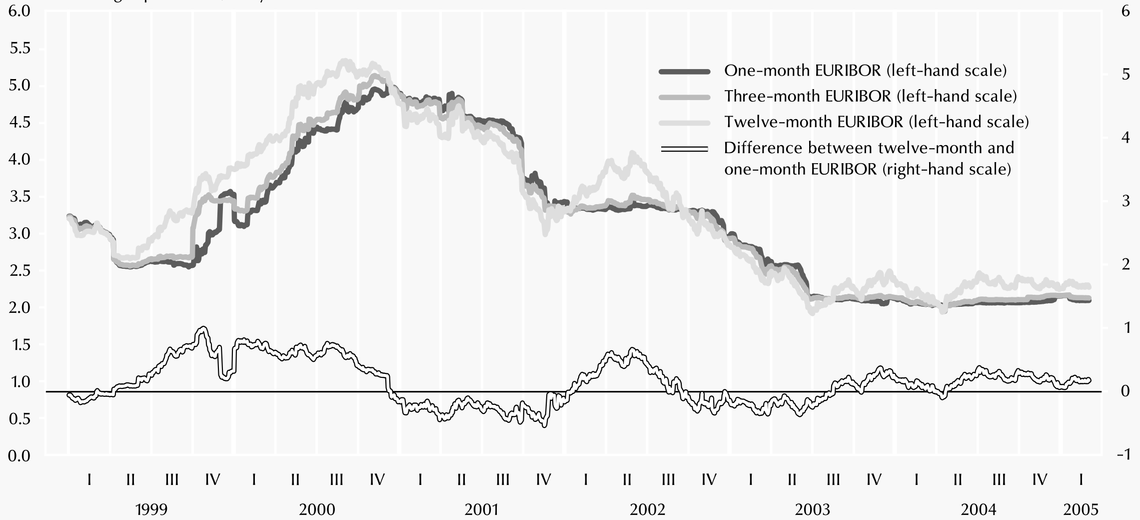
A downward shift was also recorded in the curve of implied forward overnight interest rates,[18] which was lower on 2 February 2005

18 This curve is constructed by the ECB on the basis of overnight interest rate swaps for periods between one day and ten years. Details see in ECB, *Monthly Bulletin*, January 1999, page 26.

Chart II.7

Short-term interest rates in the euro area (1 January 1999 - 10 February 2005)

(Percentages per annum, daily data)

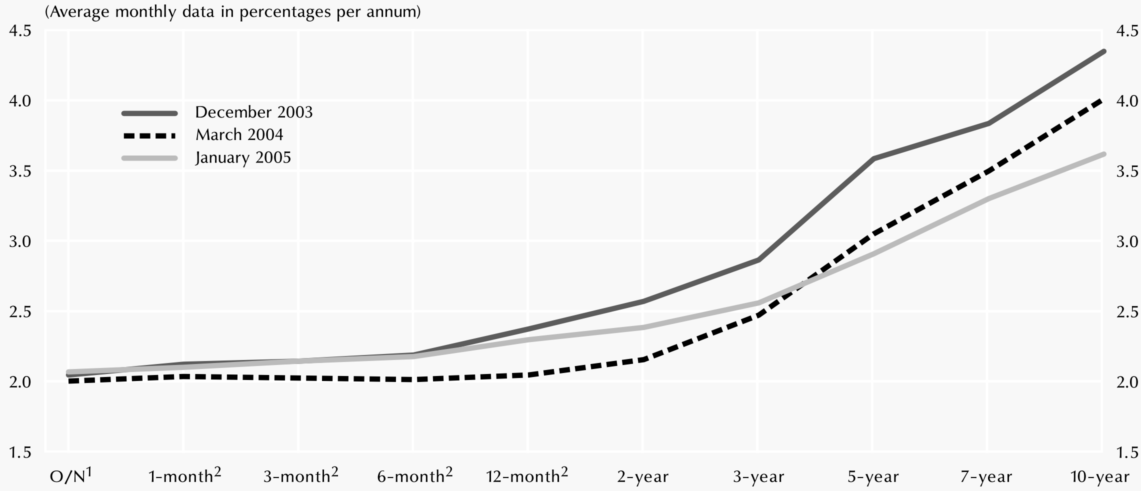


Source: ECB.

Chart II.8

Money market and bond market yield curves in the euro area

(Average monthly data in percentages per annum)



1 Overnight money market rate (EONIA).
2 Interbank offered rates (EURIBOR).

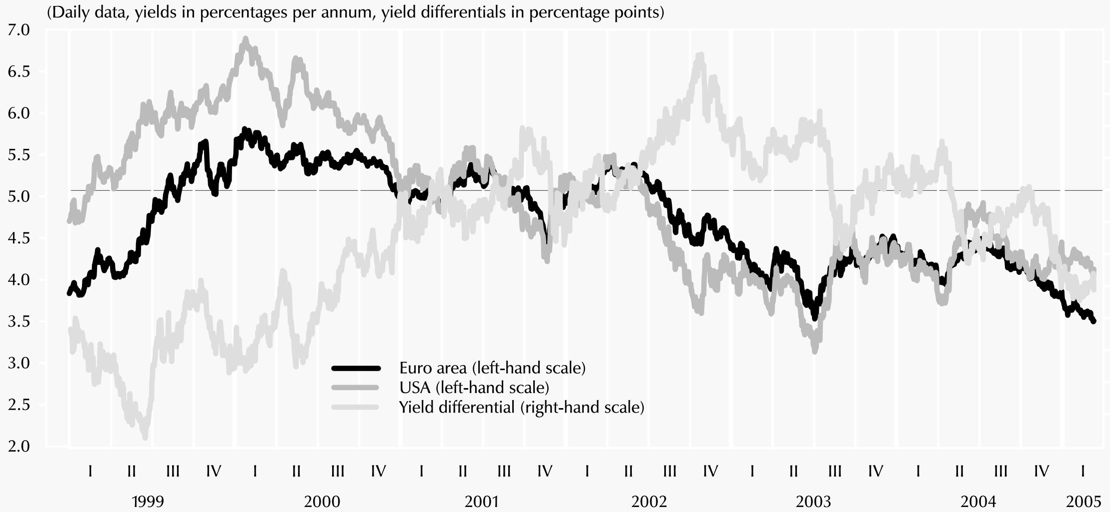
Source: ECB.

compared with the end of 2003, particularly at longer time horizons. This curve incorporates market expectations about the future path of short-term interest rates, which are connected to the outlook for economic activity and inflation. Thus, the downward shift in the implied forward overnight interest rates in 2004 reflects the downward revision of market expectations regarding the increase in economic activity, while the flatter slope compared with the end of 2003 suggests improved expectations for price stability in the euro area.

Chart II.9

Ten-year bond yields in the euro area and the United States
(1 January 1999 - 10 February 2005)

(Daily data, yields in percentages per annum, yield differentials in percentage points)



Source: ECB.

In 2004, the average monthly interest rates applied by MFIs[19] on deposits held by households and non-financial corporations remained stable at low levels. The changes (increases or declines) in these interest rates in December 2004, compared with December 2003, did not exceed 4 basis points for the most significant deposit categories in terms of volume (overnight deposits by households and non-financial corporations and households' deposits redeemable at a period of notice of up to three months).

Overall, lending rates fell in most categories, compared with December 2003, though they displayed some volatility during 2004. The rate on overdrafts by non-financial corporations, which account for the bulk of new loans, fell by 32 basis points in December 2004, compared with December 2003, while the rate on households' overdrafts fell by a total of 18 basis points in 2004.

In 2004, as has been the case in the past, the pass-through of market interest rate changes to bank deposit and lending rates with a comparable maturity occurred with time lags, reflecting the effort of banks to smooth out the evolution of their rates. The decline in lending rates, in particular, seems to reflect mainly a similar decrease in credit risk for the corresponding loan categories, given also the relative stability of deposit rates. This can also be concluded from the aforementioned Eurosystem bank lending survey (January 2005).

Government bond yields in the euro area declined overall in 2004. In the first quarter of 2004 they followed a downward course, which was reversed from April (see Chart II.9) due to market expectations about economic recovery in the euro area. From July, however, the rise in oil prices, together with the ongoing strengthening of the euro exchange rate, led to less favourable expectations about economic growth and, consequently, to a

19 The data refer to weighted interest rate averages applied to new deposits and loans in the period under review. Weighting is based on the volume of the deposit or loan; thus, weighted average interest rates for the euro area as a whole reflect changes in both the level of interest rates and the volume of new deposits and loans across euro area countries.

new decline in bond yields, which continued until January 2005. Thus, euro area bond yields stood at a lower level in January 2005, compared with December 2003. For example, the ten-year bond yield in the euro area fell by 73 basis points, compared with December 2003, and stood at 3.63% in January 2005. Over the same period, uncertainty in euro area bond markets, as reflected in the volatility[20] of government bond prices, declined and stood at a level lower than the average for the past six years.

In international bond markets, long-term government bond yields followed a downward course from mid-2004, while the uncertainty of market participants displayed, in general, a continuously declining trend in the course of the year.[21] Over almost a year up to June 2004, ten-year government bond yields moved upwards (albeit with fluctuations), following both the gradual strengthening of the global recovery and estimates of a slight rise in inflation in advanced economies. Since July 2004, however, the combined effect of the economic downturn, which was recorded in several advanced economies and was more severe than expected, and estimates of the effects of the high and rising world oil prices on world GDP caused yields to take a downward path. In the last quarter of 2004, developments in the US long-term bond market seemed to deviate from those in the euro area and Japan. US ten-year government bond yields resumed their upward course, widening the yield differential between these bonds and the corresponding bonds in the euro area (see Chart II.9) and Japan, where yields continued on their slightly downward trend. In average annual terms, US ten-year government bond yields rose to 4.26%, compared with 4.00% in 2003, while the corresponding bond yields in Japan rose to 1.50% in 2004, against 0.99% in the previous year. In January 2005, ten-year government bond yields in the United States and Japan declined marginally.

3.4 Stock market developments

During 2004, share prices in euro area stock markets followed in general an upward course, with the exception of the period between March and August (see Chart II.10). In particular, stock prices were continuously rising between March 2003 (when a six-year low was recorded) and March 2004, due to the upward revision of market expectations regarding the outlook for economic activity and corporate profits. In March 2004 this rise came to a halt and up to mid-August stock prices fell to the lowest levels of the year. From end-August, however, they recovered owing to the low real interest rates and the positive expectations about corporate profits. Thus, at end-December 2004, the broad Dow Jones EURO STOXX index[22] stood 9.9% higher than at end-December 2003, while its upward course continued in January 2005. In December, uncertainty in stock markets[23] had also declined (compared with the average for the past six years), as reflected in lower stock price volatility, which embodies investor expectations about the future path of stock prices.

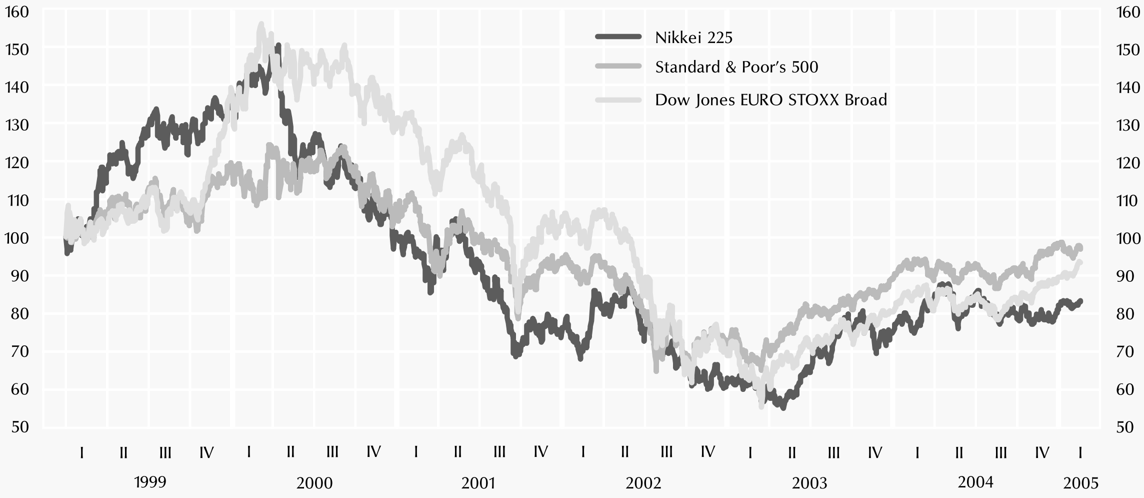
In the United States, the Standard & Poor's 500 index increased after mid-August 2004, when it had recorded the lowest level for the year, and at the end of 2004 stood 9% higher than at the end of 2003. Uncertainty in the US stock market declined, mainly after March 2004, and continues

20 Uncertainty is measured by the implied volatility of bond markets, a time series derived from futures data. Volatility in the euro area government bond market is calculated on the basis of implied volatility of the prices of options on ten-year German Bund futures, which is compiled by Bloomberg and monitored by the ECB.
21 See previous footnote.
22 This index, which is compiled on the basis of the stock prices of the approximately 300 euro area companies with the highest level of capitalisation, is designed in a way that provides a representative picture of the euro area stock market.
23 Stock market uncertainty is measured by an index compiled by Bloomberg following a similar approach to the one described in footnote 20 on bond market uncertainty.

Chart II.10

Stock price indices (1 January 1999 - 10 February 2005)

(31 December 1998 =100, daily data)



Source: ECB.

to stand at low levels compared with the average for the past six years. These positive developments primarily reflect the further improvement in corporate profits which, as expected, were not significantly affected by the rise in oil prices. Market expectations for a further rise in real interest rates are estimated to have led to a minor drop of the Standard & Poor's 500 index in January 2005. In Japan, the primary stock market index (Nikkei 225) reached its highest level for 2004 in April and followed a downward course thereafter, mirroring, to a large extent, the significant slowdown of economic activity in the second and third quarters of 2004. In particular, the above index declined after having risen by 16% in the period between December 2003 and April 2004. At the end of December 2004 it was 7.6% higher than at the end of December 2003.

III. Macroeconomic developments and prospects in Greece

1. Inflation: developments and determinants in 2004

1.1 Summary of developments

Average annual inflation in Greece fell in 2004, exclusively as a result of exogenous factors, while core inflation rose. The average annual rate of increase in the Harmonised Index of Consumer Prices (HICP) eased from 3.4% in 2003 to 3.0% in 2004 (see Chart III.1), mainly due to a fall in fresh fruit and vegetable prices. During 2004, the annual rate of increase in the HICP initially fell, but in the fourth quarter it stood at the same level as in the last quarter of 2003 (3.2%). By contrast, core inflation, as measured by the average annual rate of change in the HICP excluding energy and unprocessed food (see Chart III.2), rose further and remained high (3.4% on average, compared with 3.1% in 2003). Core inflation followed a steadily upward course from the second quarter of 2003 until the third quarter of 2004, but fell slightly in the final quarter of the year (to 3.2%).[1]

The final inflation outcomes for 2004 were more favourable than had been forecast in the two previous monetary policy reports.[2] This development is a reflection of (a) the large fall in fresh fruit and vegetable prices, which could not have been forecast, and (b) the fact that, thanks to efforts by the

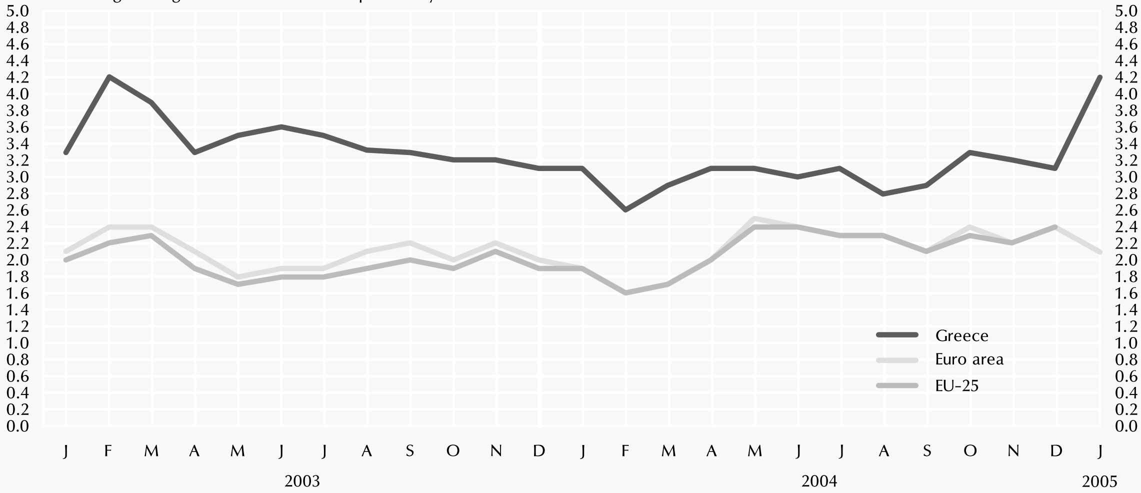
1 Based on the Consumer Price Index (CPI), average annual inflation fell to 2.9% in 2004 from 3.5% in 2003. Core inflation, as measured here by the annual rate of change in the CPI excluding fuel and fresh fruit and vegetables, remained high (3.3% on average, compared with 3.2% in 2003 – see Chart III.3).

2 In the March 2004 Report it had been forecast that the average annual inflation rate would, in effect, remain at the same level as in 2003 or accelerate marginally (actually, it fell). In the October 2004 Report, the average annual increase in inflation was forecast accurately (3.0% on the basis of the HICP and 2.9% on the basis of the CPI), while the forecast figures for core inflation (as measured on the basis of both the HICP and the CPI) were only marginally (0.1-0.2 percentage point) higher than the figures actually recorded.

Chart III.1

Harmonised index of consumer prices in Greece, the euro area and the European Union
(January 2003 - January 2005)

(Percentage changes over same month of previous year)

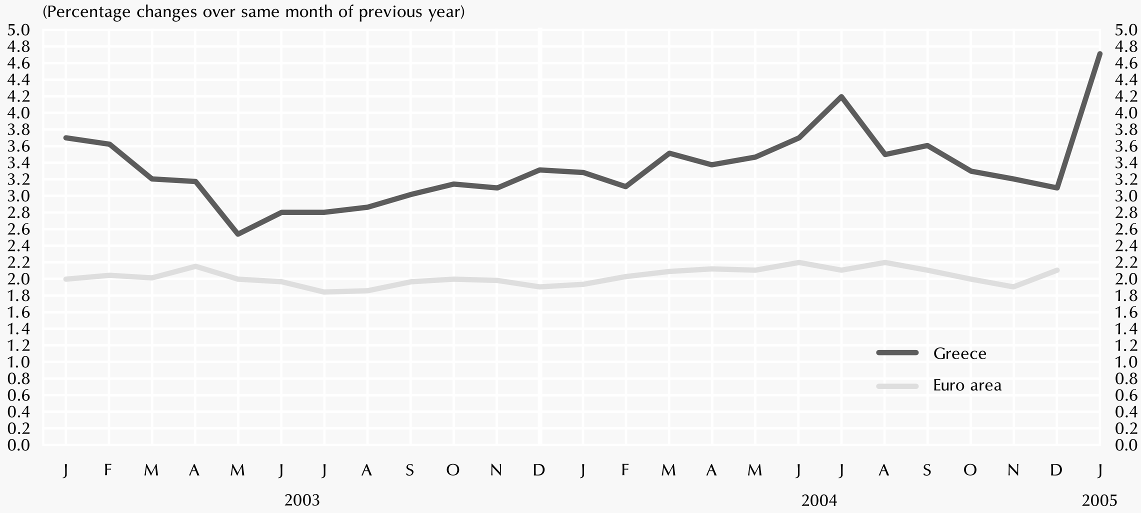


Sources: NSSG and Eurostat. Data for January 2005 are provisional estimates.

Chart III.2

Core inflation in Greece and the euro area on the basis of the HICP excluding energy and unprocessed food
(January 2003 - January 2005)

(Percentage changes over same month of previous year)



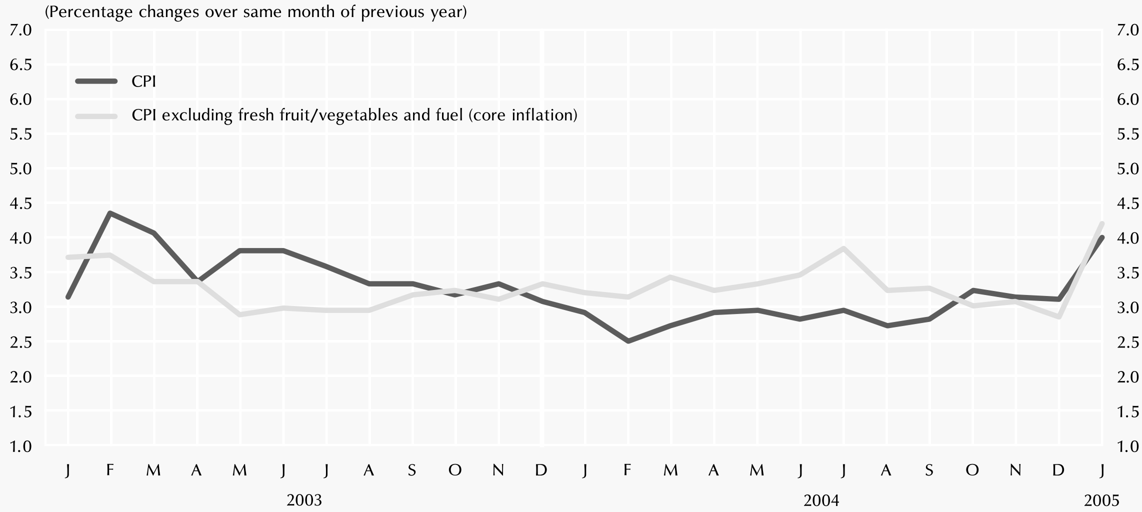
Sources: NSSG and Eurostat.

government and the social partners, concerns that inflation would rise during the Olympic Games were not confirmed by the turn of events.

The differential between average annual HICP inflation in Greece (3.0%) and in the euro area (2.1%) narrowed to 0.9 percentage point in 2004, from 1.3 percentage points in 2003. However, the differential of average annual core inflation (3.4% against 2.1%) rose to 1.3 percentage points from 1.1 percentage points in 2003. In December 2004, the core inflation differential was 1.2 percentage points (3.1% against 1.9%).

Chart III.3

Consumer price index and core inflation in Greece
(January 2003 - January 2005)
(Percentage changes over same month of previous year)



Source: Calculations based on NSSG data.

The slowdown in the average annual rate of increase in the HICP (and the CPI) in 2004 was almost entirely due to a substantial drop in unprocessed food prices from the second quarter until the end[3] of 2004 thanks to favourable weather conditions (see Chart III.4). The prices of fuels which are included in the CPI were down in the first quarter of 2004 in comparison with the same period in 2003 (when international crude oil prices had reached a very high level as a result of uncertainty surrounding the then expected military conflict in Iraq). However, in 2004 as a whole, the prices of fuels included in the CPI rose at an average annual rate of 7.5%, compared with 3.9% in 2003[4] – see Charts III.5 and III.6. In particular, world prices of Brent oil in US dollars rose at a high average annual rate (33.5%) in 2004. However, due to the average annual increase of 10% in the euro exchange rate against the US dollar, Brent oil prices in euro rose at an average annual rate of 21.5%. The reasons behind the differential between price changes for crude oil on the world market and wholesale or retail price changes for oil products on the domestic market are presented in detail in Box III.1

The increase in core inflation reflects the steeper rise in the prices of goods (excluding fuel and fresh fruit and vegetables),[5] which was only partly offset by the small slowdown in the average annual rate of increase in the prices of services.[6] The latter rate, however, is still higher than the average inflation rate. As for goods, the growing inflationary pressures stem mainly from processed food, the prices of which rose at a high average annual rate in 2004 (4.8%, compared with 3.6% in 2003, on the basis of the HICP).[7] The goods and services which contributed to a

3 The average rate of change in the prices of fresh fruit and vegetables (based on the CPI) was negative in 2004 (–11.9%), whereas in 2003 it had been positive (+10.7%).
4 In addition, wholesale fuel prices rose at an average annual rate of 9.6%, compared with 2.1% in 2003.
5 The annual rate of increase in their prices (based on the CPI) was 2.8% in 2004, compared with 2.4% in 2003.
6 To 3.8% in 2004, from 4.1% in 2003, based on the HICP.
7 Prices for other industrial consumer goods (excluding energy products and food) rose just 2.3%, although this was still more than in 2003 (1.6%).

Chart III.4

Core inflation, prices of fresh fruit/vegetables and fuel
(January 2003 - January 2005)
(Annual percentage changes)

Source: Calculations based on NSSG data.

relatively high rate of inflation are listed in Table 4 of the Statistical Appendix.

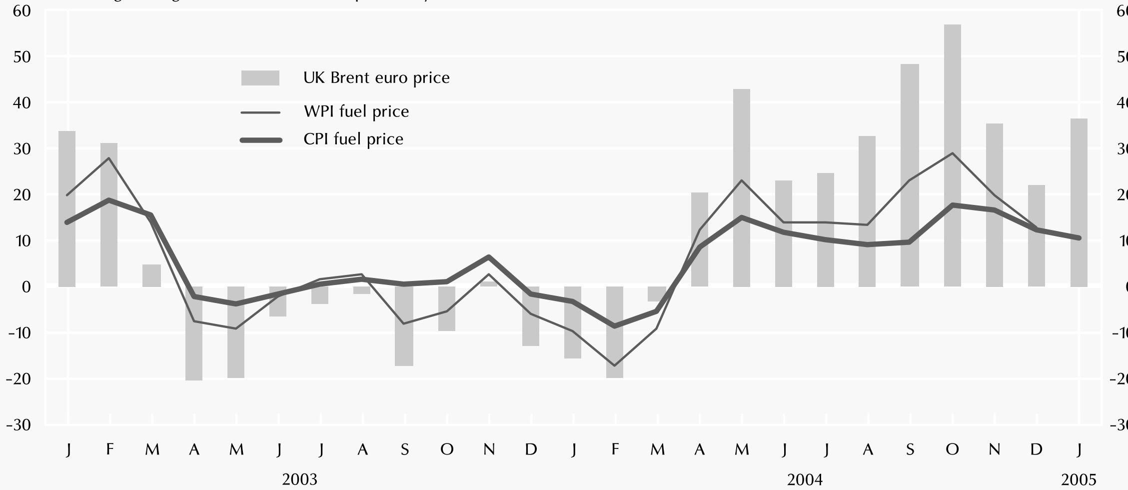
This outturn of core inflation was combined with stronger inflationary pressures on wholesale prices. Indeed, wholesale prices of domestic industrial products for home consumption (excluding fuel) rose at an average annual rate of 4.1% in 2004, compared with 2.9% in 2003.

These unfavourable developments in core inflation mainly reflect the faster rise in unit labour costs in 2004 than in 2003, combined with persisting pressures on the demand side (for greater analysis of this, see below). They are also indirectly attributable to the effects of the rise in oil prices (which began in the second quarter of 2004) on the prices of other goods and services. To some extent, these inflationary pressures were mitigated by the continuing appreciation of the euro, which limited the effects of imported inflation. Specifically, despite rising less in 2004 (0.8%) than in 2003 (2.9%), the exchange rate of the euro, weighted on the basis of Greece's exter-

Ghart III.5

Evolution of CPI/WPI fuel prices and of the euro price of Brent crude oil (January 2003 - January 2005)

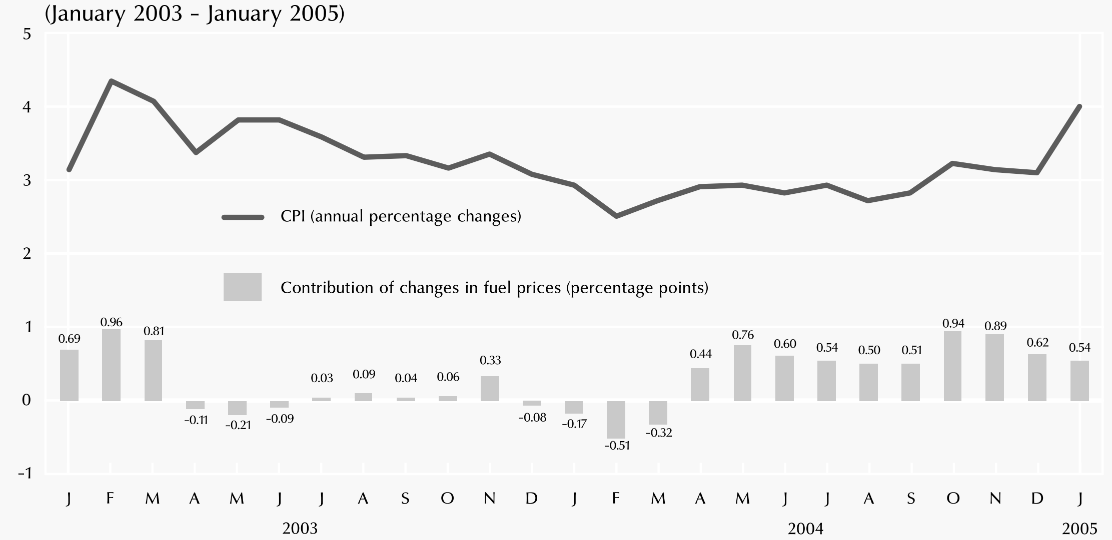
(Percentage changes over same month of previous year)



Source: Calculations based on NSSG data and, for crude oil prices (UK Brent), on US Department of Energy data.

Chart III.6

Inflationary contribution of changes in fuel prices (January 2003 - January 2005)



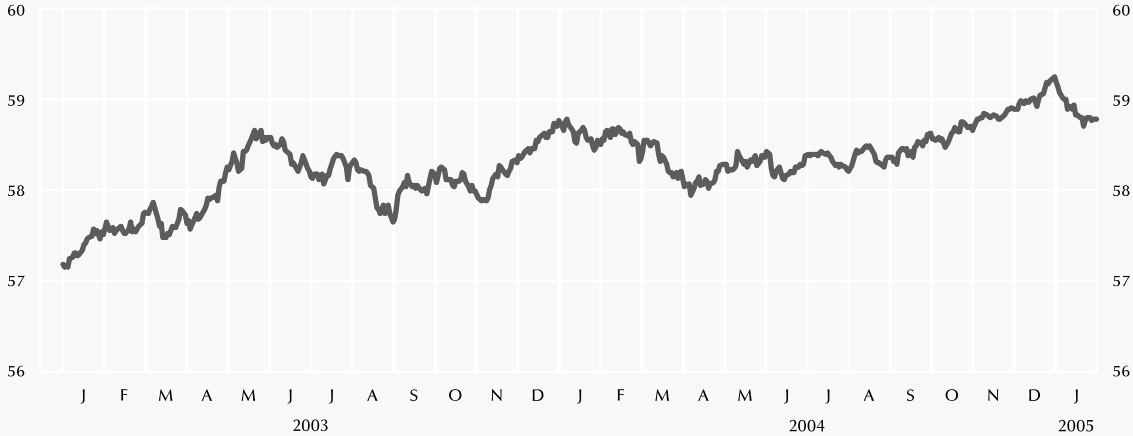
Source: Calculations based on NSSG data.

nal trade (see Chart III.7), helped to further contain the increase in the wholesale prices of imported goods (excluding fuel) to 0.3% in 2004,[8] from 0.9% in 2003 (see Chart III.8).

As pointed out in the previous report on monetary policy, the upward trend of core inflation, the considerably faster rise in wholesale prices of domestic industrial products for home consump-

8 According to an approximate calculation, had the wholesale prices of imported goods risen by 3% rather than 0.3% (i.e. at a rate corresponding to the domestic inflation rate), the average annual increase in consumer prices would have been 0.6 percentage point higher.

Chart III.7
Effective exchange rate index, weighted on the basis of Greece's external trade
(January 2003 - January 2005)
(1990=100, daily data)



Note: As of January 2001, changes in this index are relatively limited, since Greece's trade with the other euro area countries (which are among its most important trading partners) is carried out in euro.

Source: Bank of Greece.

BOX III.1

Developments in oil prices, their direct effect on consumer prices and the energy/oil dependence of the Greek economy

The price of Brent oil: recent developments and forecasts

Between December 2003 and December 2004 the price of Brent crude oil rose by 36.4% in US dollars, or by 25.0% in euro, given that in the same period the euro appreciated by 9.1% vis-à-vis the US dollar. Its average price in December 2004 was $40.2, or €30.0 per barrel, while the average annual price for 2004 as a whole was $38 (an increase of 33.5%), or €30.5 (an increase of 21.5%). As mentioned in the main text of this chapter, in 2005 the average annual price of crude oil is expected to rise by 15.5-16% in US dollars and by 10-10.5% in euro (on the basis of a *technical assumption* regarding the exchange rate of the euro).

The oil dependence of the Greek economy

The Greek economy's dependence on energy imports and particularly liquid fuels is relatively high. According to an indicator compiled by Eurostat *(Structural Indicators – Energy intensity of the economy)*, energy consumption per unit of real GDP between 1991 and 2002 remained unchanged in Greece, while it fell by 12% in the EU-15 and by 9% in the euro area. Moreover, in 2002 energy consumption per unit of GDP in Greece was 35% higher than the EU-15 average. Therefore, the Greek economy is quite energy-consuming. Although Greece utilises hydroelectric energy, lignite and —more recently— wind energy, its reliance on oil remains heavy: according to Eurostat data for 2002 *(Statistics in Focus – Statistical aspects of the energy economy in 2002)*, net oil imports represent 65.2% of the country's gross energy consumption, compared with 44.0% in the euro area and only 32.9% in the EU-15 (which includes the United Kingdom, a petroleum-producing country). Obviously, for the situation to change there is a need for better organisation of production (through the introduction of less energy-consuming technologies) and of life in the cities (e.g. through improvements in the public transport system to reduce energy waste related to passenger car use, and employment of new technologies and alternative energy sources for house heating). Consequently, ➔

→ sound planning and appropriate incentives for energy saving are required.

The effect of the rise in oil prices on consumer prices in Greece[1]

It is calculated that a 10% increase in crude oil prices in euro may have a direct upward effect on the Greek CPI of up to 0.19% (all other factors —such as refinement costs or profit margins— remaining unchanged).[2]

This conclusion is reached after taking into account the following:

(a) Domestic consumer prices of fuel change less than world prices of crude oil. The deviation between changes in world prices of crude oil and changes in the retail or wholesale prices of oil products in the domestic market reflects developments in other components of domestic fuel prices, such as processing-distribution-trading costs, profits and taxes. Specifically, indirect taxes, most of which are fixed (defined per unit of volume and not of value) and therefore uninfluenced by changes in product prices (with the exception of VAT), account for 55% and 54% of the retail prices of *gasoline* and *motor oil*, respectively. Furthermore, 19% and 16% of the retail prices of *gasoline* and *motor oil*, respectively, reflect the relevant processing, distribution and trading costs and profit margins. Thus, raw material cost only accounts for the remaining 26% and 30% of the retail prices of *gasoline* and *motor oil*, respectively – see also the study by "Hellenic Petroleum S.A.": *Petroleum Products Market* (10 May 2004), available in Greek at the website of the Greek Ministry of Development (http://www.ypan.gr/docs/1.ppt). Nevertheless, in the winter period (15 October to 30 April), the share of indirect taxes in the retail price of *heating oil* is significantly smaller and close to the minimum levels determined by the EU, so that the share of raw material cost in that price is much higher (around 63%). As a result, a 10% increase in crude oil prices in euro during winter directly causes the retail fuel prices for the consumer to rise by 2.6% (for gasoline) and 6.3% (for heating oil), or by 3.8% on average (after weighting), assuming of course that the other components of fuel prices remain unchanged.

(b) Fuel contributes to the CPI "basket" with a weight of around 5%. Thus, a 3.8% increase in its (average weighted) retail price (following a 10% increase in crude oil prices in euro) directly leads to a 0.19% rise of the general CPI.

Recent developments in Greece

Between December 2003 and December 2004, fuel prices included in the CPI rose by 12.1% (4.4% for gasoline and 27.1% for heating oil), while their direct contribution to the 3.1% increase of the CPI in the same period was 0.62 percentage point.

Given that, as mentioned above, between December 2003 and December 2004 the price of Brent oil rose by 25.0% in euro, the *expected* weighted average increase of fuel retail prices in the same twelve months was 9.5% (25.0%x0.38), i.e. 6.5% (25.0%x0.26) for gasoline and 15.7% (25.0%x0.63) for heating oil. Thus, the actual increases were considerably higher than those *expected* for heating oil and quite a bit lower for gasoline – however, on aggregate they were higher. These deviations may reflect time lags between the procurement of crude oil and the supply of refined oil products to the domestic market, as well as the possibility that production and distribution companies implement →

1 For the effects of rises in world crude oil prices on other key economic aggregates, see OECD "Oil prices: developments, drivers, economic consequences and policy responses", *Economic Outlook*, December 2004.

2 This effect is stronger than for the euro area as a whole. In fact, according to ECB estimates, in the euro area as a whole a 10% increase in crude oil prices (in euro) directly entails a rise in HICP inflation of approximately 0.1 percentage point. It should be clear that the effects of rises in world prices of crude oil on inflation are distinguished into direct, indirect and second-round effects. *Direct* effects refer to changes in the general CPI entailed by changes in the prices of oil products included in the CPI (i.e. gasoline and heating oil). *Indirect* effects refer to changes in the general CPI entailed by changes in the prices of other goods and services the production cost of which is affected by changes in the cost of fuel. Finally, *second-round* effects refer to the fact that a change in the CPI (due to the direct and indirect effects of a rise in oil prices) may have an impact on wage negotiations and wage increases and —through those— on the pricing policy of enterprises (see also ECB, *Monthly Bulletin*, July 2004, p. 29-30).

→ differential pricing policies for gasoline and heating oil. In addition, a comparative analysis of developments in world prices of Brent oil and developments in fuel prices in the domestic market (both retail prices recorded in the CPI and refinery prices net of tax in the 2001-2004 period) reveals that: (i) *The prices of Greek refineries* for heating oil and gasoline generally follow both upward and downward movements in world prices of crude oil. (ii) However, changes in *fuel retail prices* in the domestic market behave asymmetrically with respect to changes in world prices of crude oil – during periods of declines in world oil prices, retail fuel prices in Greece fall on average by much less.[3] This implies in principle that *increases* in world prices of oil are passed on to the consumer to a greater extent than the respective decreases, implying a corresponding widening of profit margins.

3 Indicatively, according to the results of a simple regression for the 1999-2004 period, more than 65% of the *increases* in retail prices of gasoline is explained —all other factors remaining unchanged— by increases in world prices of crude oil, while only 33% of the *decreases* in retail prices is explained by respective decreases in world prices. In any event, the most recent reduction of indirect taxes on liquid fuel was effected in autumn 1999.

tion (in contrast to a minimal rise in the prices of imported goods) and, finally, the faster increase in the prices at which exporters offer their products (whether expressed in euro or in foreign currencies)[9] suggest that domestic inflationary pressures, combined with the lower inflation rates enjoyed by our trading partners and the appreciation of the euro, are having a negative effect on the price competitiveness of Greek products,[10] both in the domestic and in foreign markets.

1.2 The inflation differential between Greece and the euro area

The persistent inflation differential between Greece and the euro area (see Table III.2 and Chart III.1) may in principle be attributed to macroeconomic factors (see below for further details) associated with:

— First, the faster growth rate of domestic demand compared with supply. This is reflected, *inter alia*, in the positive "output gap"[11] that has been observed in Greece since 2001 and is in part due to the expansionary fiscal policy pursued in Greece in recent years.[12] By contrast, the "output gap" in many other euro area countries is negative.

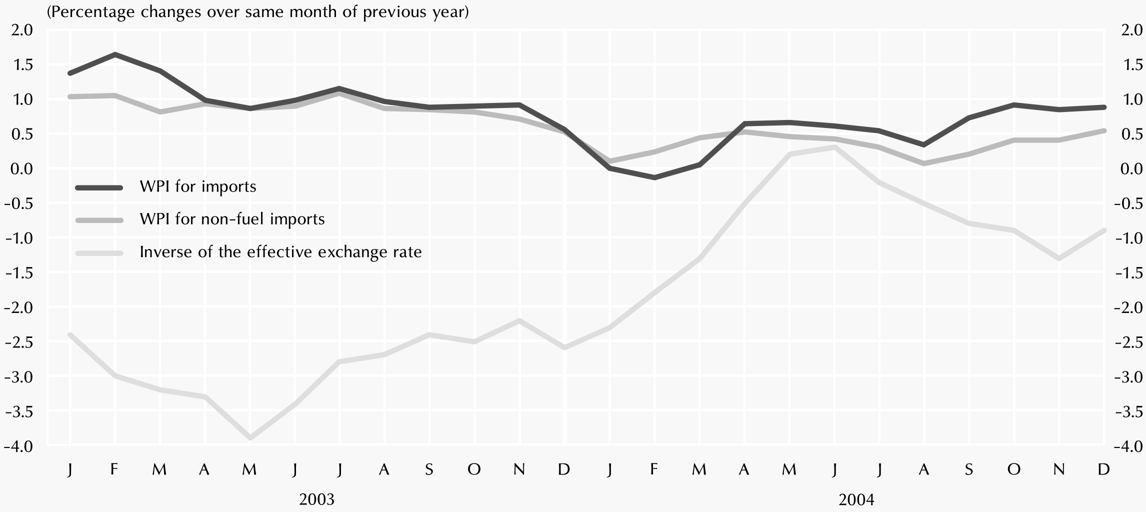
— Second, the rise in unit labour costs in Greece, which was greater than the euro area average. Moreover, the positive differential of Greek inflation from that of the euro area can be attributed partly to the convergence of price and income levels, which is linked with the process of real convergence (the "Balassa-Samuelson effect"). At the same time, the differential is also the result of

9 The wholesale prices of goods (excluding fuel) for export rose at an average annual rate of 2.7% in 2004, whereas they had fallen by 0.2% in 2003. If these prices are expressed in foreign currency (using the effective exchange rate of the euro weighted on the basis of Greece's external trade), they are estimated to have risen at an average annual rate of 3.6% in 2004 (compared with 2.7% in 2003 – see also Table III.1). It should be remembered that in the first 8-9 months of 2003, exporters were lowering or keeping unchanged their prices in euro (thus limiting the price increase in foreign currency that would have occurred as a result of the appreciation of the euro), although there are indications that this pricing policy has been abandoned since the last quarter of 2003, due partly to increased pressures as a result of production costs and partly to the fact that a significant increase was observed in commodity prices in the global market in 2004. However, under pressure from the rising euro, the annual rate of increase in the wholesale prices of exported products showed a marked slowdown from September 2004 and turned slightly negative in December.
10 The decline in the price competitiveness of Greek products is measured, *inter alia*, by the rise in the *real* effective exchange rate (EER) of the euro weighted on the basis of Greece's external trade. Specifically, it is estimated that: (a) the real EER of the euro calculated on the basis of relative unit labour costs in manufacturing rose at an average annual rate of 6% in 2004 (due primarily to the increase in relative labour costs and, secondarily, to the appreciation of the euro) and (b) the index calculated on the basis of relative consumer prices rose at an average annual rate of 2.0% (due almost as much to the increase in relative prices as to the appreciation of the euro).
11 The "output gap" is defined as the difference between the level of actual output (GDP) and the country's production capacity (level of potential GDP), as a percentage of the level of potential GDP.
12 See Bank of Greece, *Monetary Policy, Interim Report*, Chapter IV, October 2004.

Chart III.8

Wholesale import price index and the inverse of the effective exchange rate of the euro, weighted on the basis of Greece's external trade (January 2003 - December 2004)

(Percentage changes over same month of previous year)



Sources: NSSG and Bank of Greece.

Table III.1

Export price index and effective exchange rate of the currrency (2003-2004)

(Percentage changes over same month of previous year)

	Exchange rate of the euro weighted by Greece's external trade	Wholesale prices of exported products			
		Total		Excluding oil	
		In euro	In foreign currency	In euro	In foreign currency
2003 Jan.	2.4	1.4	3.7	–1.0	1.3
Feb.	3.0	1.9	4.9	–1.4	1.6
March	3.2	0.0	3.2	–1.5	1.6
Apr.	3.3	–2.2	1.0	–1.3	1.9
May	3.9	–3.3	0.5	–2.4	1.4
June	3.4	–0.3	3.1	–0.2	3.2
July	2.8	0.7	3.5	0.3	3.1
Aug.	2.7	0.7	3.3	0.1	2.7
Sept.	2.4	–0.7	1.7	0.5	3.0
Oct.	2.5	0.2	2.8	1.2	3.7
Nov.	2.2	1.8	4.1	1.8	4.1
Dec.	2.6	1.1	3.7	2.2	4.9
Year average	2.9	0.1	3.0	–0.2	2.7
2004 Jan.	2.3	1.9	4.2	3.7	6.1
Feb.	1.8	0.5	2.3	3.4	5.2
March	1.3	2.3	3.6	3.9	5.2
Apr.	0.5	4.6	5.2	3.6	4.1
May	–0.2	7.5	7.3	5.5	5.3
June	–0.3	4.8	4.5	3.7	3.3
July	0.2	4.1	4.3	3.0	3.2
Aug.	0.5	4.0	4.5	2.9	3.4
Sept.	0.8	4.2	5.1	1.9	2.7
Oct.	0.9	4.1	5.0	1.2	2.0
Nov.	1.3	2.2	3.4	0.2	1.5
Dec.	0.9	1.1	2.1	–0.1	0.9
Year average	0.8	3.4	4.2	2.7	3.6

Source: Calculations based on NSSG and Bank of Greece data.

Table III.2

Harmonised index of consumer prices: Greece and the EU (2003-2004)

(Annual percentage changes)

Country	2003 (year average)	Dec. 2003	2004 (year average)	Dec. 2004
Austria	1.3	1.3	2.0	2.5
Belgium	1.5	1.7	1.9	1.9
Cyprus	4.0	2.2	1.9	3.9
Czech Republic	–0.1	1.0	2.6	2.5
Denmark	2.0	1.2	0.9	1.0
Estonia	1.4	1.2	3.0	4.8
Finland	1.3	1.2	0.1	0.1
France	2.2	2.4	2.3	2.2
Germany	1.0	1.1	1.8	2.2
Greece	*3.4*	*3.1*	*3.0*	*3.1*
Hungary	4.7	5.6	6.8	5.5
Ireland	4.0	2.9	2.3	2.4
Italy	2.8	2.5	2.3	2.4
Latvia	2.9	3.5	6.2	7.4
Lithouania	–1.1	–1.3	1.1	2.8
Luxembourg	2.5	2.4	3.2	3.5
Malta	1.9	2.4	2.7	1.9
Netherlands	2.2	1.6	1.4	1.2
Poland	0.7	1.6	3.6	4.4
Portugal	3.3	2.3	2.5	2.6
Slovakia	8.5	9.3	7.4	5.8
Slovenia	5.7	4.7	3.6	3.3
Spain	3.1	2.7	3.1	3.3
Sweden	2.3	1.8	1.0	0.9
United Kingdom	1.4	1.3	1.3	1.6
EU–15	2.0	1.8	2.0	2.2
EU–25	1.9	1.9	2.1	2.4
Euro area	2.1	2.0	2.1	2.4

Source: Eurostat.

structural weaknesses, such as price rigidities and inadequate competitive conditions in key domestic markets (see Appendix to this chapter).

From the point of view of competitiveness, the inflation differential is especially significant in the case of tradable goods (and —especially for Greece— tradable services, e.g. tourism). An analysis of price developments concerning the three groups of goods and services (non-energy industrial goods, processed food and services) that make up the "basket" used to calculate core inflation on a harmonised basis (see Chart III.9 and Table III.3)[13] shows the following:

— The positive differential between Greece and the euro area as to the average annual rate of increase in the prices of non-energy industrial goods (a major category of internationally tradable goods) rose from 0.8 percentage point in 2003 to 1.5 percentage points in 2004.

13 An examination of inflation differentials using data on consumer prices is useful, but is not enough to allow conclusions to be drawn about the development of competitiveness. It should be pointed out that: (a) consumer price changes incorporate the effects of imported inflation and, therefore, any change in inflation differentials between Greece and the euro area may in part reflect differences between these effects, not simply differentials relating to "domestic" inflation, and (b) because enterprises change their profit margins, price changes do not give a full picture of changes in competitiveness.

Table III.3

Contribution to the inflation differential between Greece and the euro area (2001-2004)

(Percentage points)

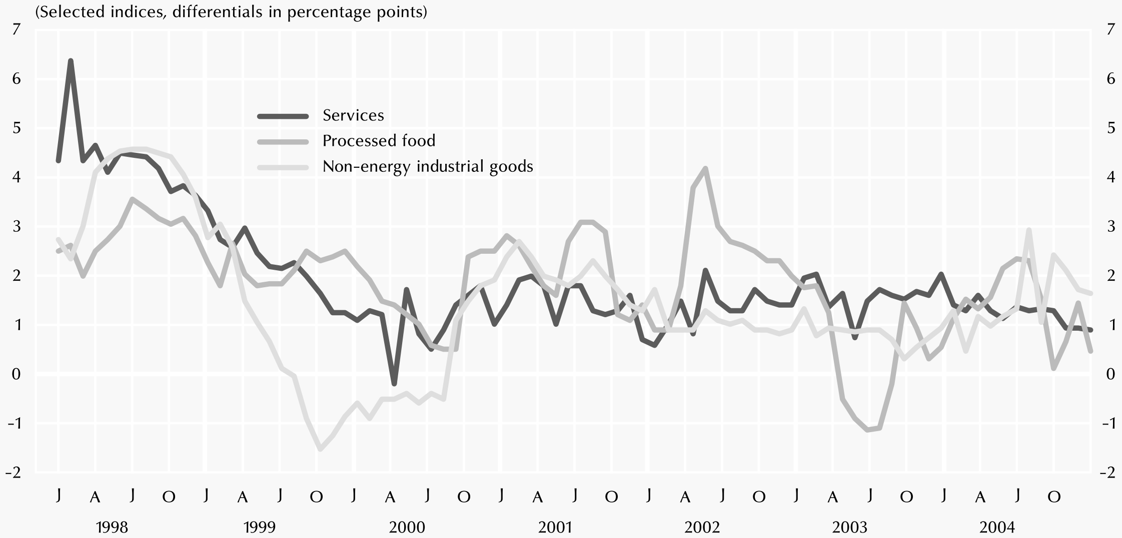
	2001	2002	2003	2004
Differential of average annual rates of HICP change	**1.4**	**1.6**	**1.3**	**0.9**
Contribution to the inflation differential stemming from the difference in the average annual rates of change in:				
Core inflation	1.6	1.2	0.9	1.2
Services prices	*0.6*	*0.5*	*0.6*	*0.5*
Processed food prices	*0.4*	*0.4*	*0.0*	*0.2*
Non-energy industrial goods prices	*0.6*	*0.3*	*0.3*	*0.5*
Unprocessed food prices	0.1	0.4	0.4	–0.4
Energy prices	–0.3	0.0	0.0	0.1

Source: Calculations based on Eurostat and ECB data.

Chart III.9

Annual inflation differentials between Greece and the euro area (1998-2004)

(Selected indices, differentials in percentage points)



Source: Calculations based on Eurostat and ECB data.

— As for processed food (another major category of internationally tradable goods), the positive inflation differential between Greece and the euro area widened much more, from just 0.3 percentage point in 2003 to 1.4 percentage points in 2004.

— For services (which, with the exception of tourism, are not internationally tradable), the positive differential remained high, but decreased slightly, from 1.6 percentage points in 2003 to 1.2 percentage points in 2004. This was partly due to efforts to restrain inflationary pressures during the Olympic Games.

During the four-year period 2001-2004, the differential between the cumulative increase in the prices of goods and services (excluding energy and unprocessed food) in Greece (15.0%) and the corresponding increase in euro area prices (8.8%) was more than six percentage points. This implies an appreciable loss of price competitiveness for Greece against other euro area countries. In addition, price competitiveness against non-euro area countries is affected by the continuing appreciation of the euro. Obviously —following the adoption of the single currency— such a loss of competitiveness cannot be dealt with by an exchange rate adjustment at the national level, but requires other policy measures (see Chapter VI).

1.3 Persistently high core inflation

The persistently high levels of core inflation are attributable to the same factors that underlie the inflation differential, i.e. macroeconomic factors and unsatisfactory competitive conditions in certain markets which do not operate efficiently (see Appendix to this chapter).

Depending on the particular case, excess demand, price inelasticity of demand (for some articles) or the fact that a number of companies take advantage of their dominant market position, all lead to price increases greater than justified by developments in cost factors. According to available data, profit margins continued to widen in 2004 (this had begun in 2003, following a decrease in profit margins in 2001-2002), especially in industries which strongly affect consumer prices. An analysis of the summary statements of a sample of 285 non-financial corporations (both listed and not listed on the Athens Exchange)[14] over the period January-September 2004 shows that both gross profits and net pre-tax profits grew significantly (by 11.2% and 10.4% respectively). This increase in profits was greater than that in sales (6.7%), thus resulting, as previously noted, in a further increase in profit margins. The latter grew markedly in retail and wholesale trade, as well as in certain consumer goods industries (food, beverages, tobacco, furniture, publications).

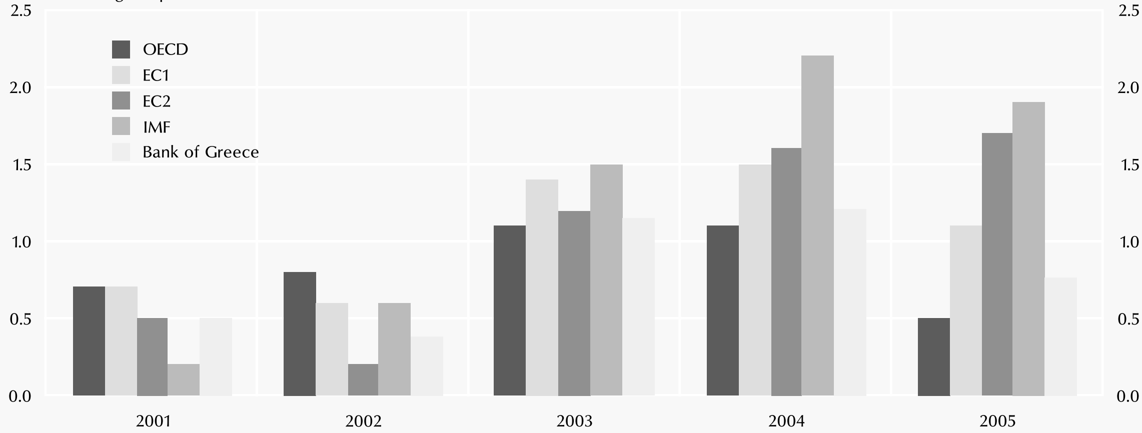
As for demand-induced inflationary pressures, the growth rate of private consumption remained high in 2004 (see Section 3 of this Chapter for more details). Furthermore, according to the latest estimates available (see Chart III.10),[15] the Greek economy's "output gap"[16] was positive in the four-year period 2001-2004 (i.e. actual output exceeded potential output) and the trend was upward. Therefore, excess demand has contributed to some degree to persistently high levels of inflation in recent years.[17] It should be noted that —based on other countries' experience in the past— increased inflationary pressures were expected to develop in 2004, especially in services, as a result of excess demand during the Olympic Games. However, such pressures did not arise, thanks to efforts by the Ministry of Development, the contribution of the social part-

14 The sample is quite representative, although it clearly refers mainly to larger enterprises.
15 Estimates from the European Commission (*Autumn 2004 Economic Forecasts*, October 2004), the OECD (*Economic Outlook*, December 2004), the International Monetary Fund (*Greece – Staff Report for the 2004 Article IV Consultation*, February 2005) and various departments of the Bank of Greece.
16 The "output gap" (see footnote 11 above) is not measurable directly. It is estimated by using various alternative methods. Estimates of potential output and the "output gap" are surrounded by a high degree of uncertainty. These factors must be taken into consideration when conclusions of analyses are considered. The *change* in the "output gap", which is measured in percentage points of GDP, is perhaps a more reliable indicator.
17 Estimates that the Greek economy's "output gap" has been positive over the last four years seem, at first sight, inconsistent with the fact that the unemployment rate remains high and the employment rate relatively low. This contradiction may indicate that the utilisation of labour force "reserves" with a view to increasing the country's potential output is impeded by labour and product market rigidities which lead to higher inflationary pressures and wider current account deficits. Moreover, in industry (which, however, accounts for only 11% of GDP), the degree of capacity utilisation (already slightly lower in 2003 at 76.5) fell further to 75.2 in 2004 (see Chart III.11), which implies that there is room for increasing capacity utilisation in this sector.

Chart III.10

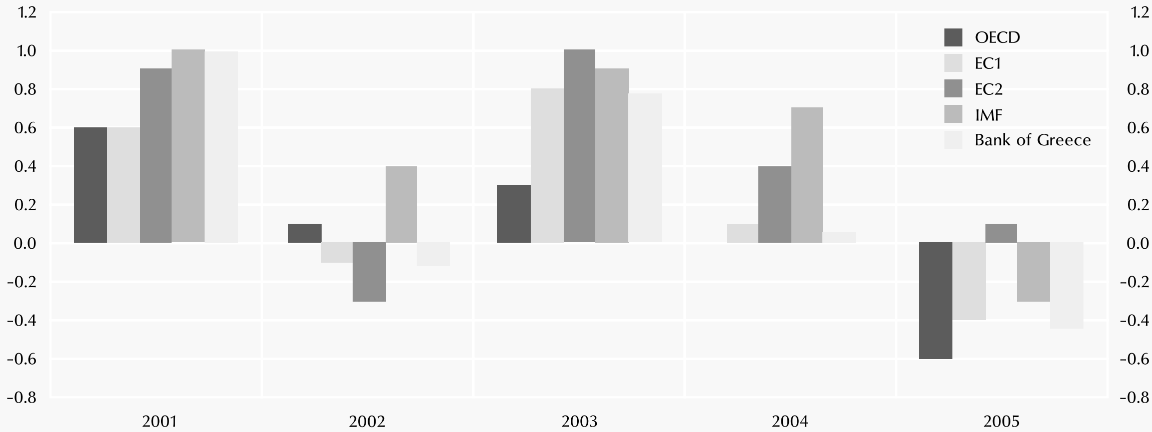
The output gap of the Greek economy

(Percentage of potential GDP)



Ghanges in the output gap of the Greek economy as a percentage of potential GDP

(Annual percentage changes)



EC1: European Commission estimate of the output gap on the basis of trend GDP.

EC2: European Commission estimate of the output gap on the basis of a production function.

Sources: OECD, *Economic Outlook,* December 2004. European Commission, *Autumn 2004 Economic Forecasts*. IMF, *Greece: Staff Report for the 2004 Article IV Consultation,* February 2004. Bank of Greece: Estimates of the Economic Research Department.

ners[18] and the smaller than expected number of foreign visitors.

Regarding production costs, the growth rate of unit labour costs[19] in the whole economy accelerated noticeably in 2004 and continued to exceed by a significant margin both the corresponding rate in the euro area (which was of the order of 0.5%[20]) and the level which is consistent with price stability, i.e. inflation below but close to 2%. Specifically, according to *revised* estimates,[21] unit labour costs in the whole economy rose by 4.2%

18 For more information concerning the agreement reached between the government on the one hand and producers and the social partners on the other, in order to ensure that the market would operate smoothly and prices remain stable during the Olympic and Paralympic Games, see the statements of the Minister of Development on 20 July 2004 and 15 September 2004.

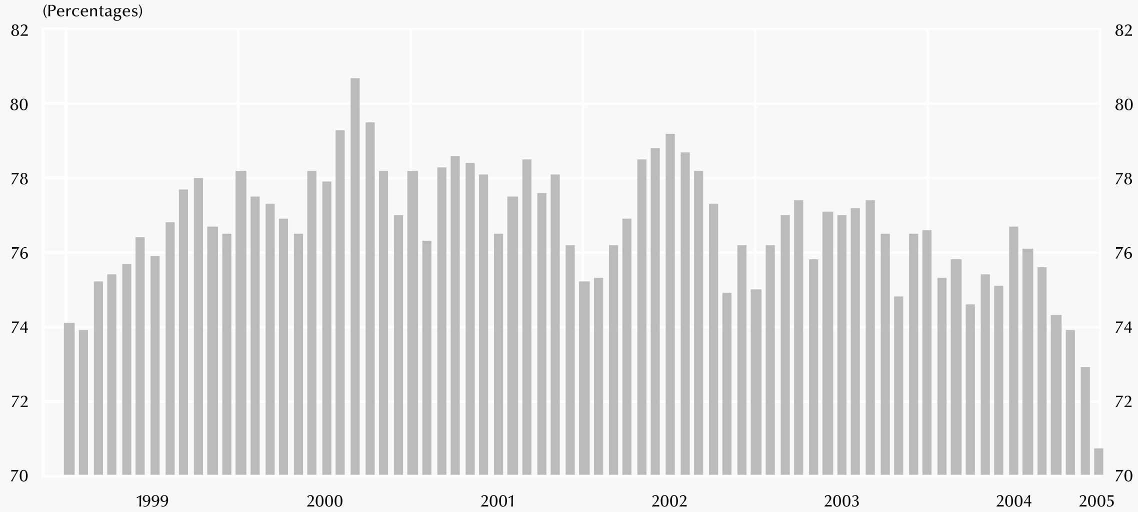
19 Obviously, the evolution of unit labour costs (at least in the business sector) is not simply an "autonomous" cost factor. It also reflects the impact of changes in demand, as excess demand affects firms' wage policies and the workers' bargaining power.

20 The average annual rate of growth of unit labour costs in the euro area was 0.5% in the first nine months of 2004.

21 The revised employment data announced by the NSSG in January 2005 have been taken into account.

Chart III.11

Industrial capacity utilisation rate (manufacturing)
(January 1999 - January 2005)
(Percentages)



Source: Foundation for Economic and Industrial Research (IOBE).

Table III.4

Employees' earnings, productivity and labour costs (2000-2005)

(Annual percentage changes)

	2000	2001	2002	2003	2004 (estimate)	2005 (forecast)
Average gross earnings *(nominal)*:						
– *whole economy*[11]	*6.1*	*4.8*	*6.6*	*5.3*	*6.5*	*5.4*
– central government [1]	7.1	5.5	7.3	5.9	8.2	6.0
– public enterprises	13.7	8.2	11.2	7.0	7.8	6.4
– banks	6.8[4]	6.4	2.9[6]	3.1[6]	6.6	5.4
– non-bank private sector	5.0	5.3	6.5	5.8	5.8	5.6
Minimum earnings	4.2	3.5	5.4	5.1	4.8	4.9
Net[2] income of an employee with average earnings						
(nominal)	8.1[5]	3.5	6.3[7]	6.0	4.9	...
(real)	4.7[5]	0.1	2.6[7]	2.4	1.9	...
Total compensation of employees (including employers' social security and other contributions)[11]	**9.0**	**8.4**	**9.2[8]**	**8.0[9]**	**8.2**	**6.1**
Compensation per employee	**5.9**	**4.9**	**6.0[8]**	**5.3[9]**	**6.9**	**5.2**
GDP[10]	**4.5**	**4.3**	**3.6**	**4.5**	**3.8**	**3.3**
Output per person-hour in manufacturing[11]	2.0	-0.6	0.6	1.2	0.9	...
Unit labour costs:[11]						
– *whole economy*	*4.3*	*3.9*	*5.4[8]*	*3.4[9]*	*4.2*	*2.7*
– business sector[3]	4.5	4.9	4.8[8]	3.6[9]	3.2	2.8
– manufacturing	3.4	6.1	5.3[8]	4.7[9]	4.8	...

1 Compensation per employee.
2 Gross earnings *less* employees' social security contributions *less* income tax.
3 The business sector comprises private and public enterprises and banks.
4 Excluding one major bank, where average earnings *decreased* by around 7.5% owing to the retirement of a large number of high-salaried employees (originating from a merged smaller bank), average earnings of bank employees rose by about 10%.
5 Including tax refunds (in January 2000) to wage earners (other than civil servants); also including the reduction (as from 1 September 2000) in social security contributions of minimum wage earners.
6 The relatively low rate of increase in average earnings of bank employees reflects mainly changes in the composition of personnel.
7 Including the abolition (as from 1 January 2002) of stamp duties (0.6% of gross earnings) paid by business sector employees.
8 Including the abolition (as from 1 January 2002) of stamp duties (0.6% of earnings) paid by business sector employers.
9 Including the increase (of 0.1% of gross earnings) in both employees' and employers' contribution to the Workers' Fund.
10 Revised NSSG estimates for the years 2000-2003 (September 2004). Bank of Greece estimates for 2004.
11 Revised estimates. Account was taken of the NSSG's revised data on the evolution of salaried employment in 2000-2003.
Sources: NSSG (2000-2003 GDP), Bank of Greece estimates and forecasts (for GDP in 2004-2005 and for the other annual aggregates in 2000-2005).

in 2004 (compared with 3.4% in 2003),[22] reflecting a faster rise in average pre-tax earnings to 6.5%, from 5.3% in 2003 (see Table III.4).[23] This acceleration was greater than the estimated acceleration of the increase in productivity (GDP per employee), which was expected to reach 2.6%, compared with 1.9% in 2003. By contrast, the annual rate of increase in unit labour costs in the business sector[24] is estimated to have slowed down slightly to 3.2%, from 3.6% in 2003.[25] The significant differential between the rate of change in unit labour costs in the economy as a whole and in the business sector is due to the large increase in personnel outlays in central government.

The outturn in unit labour costs in the business sector reflects, to start with, developments in earnings. Specifically, in the non-bank private sector, on the basis of the two-year (2004-2005) collective labour agreements signed in 2004, it is estimated that the average annual rate of increase in contractual wages (at branch level) was 5.0% (compared with 5.1% in 2003), with the corresponding figure for gross earnings being 5.8%. Particularly as concerns minimum wages (which are determined by the National General Collective Labour Agreement – NGCLA), the average annual increase for all NGCLA categories is put at 4.8%. Furthermore, the average annual contractual increase is estimated to be 6.3% in public utilities[26] and 5.1% in banks, while average gross earnings in these two sectors are estimated to have increased by 7.8% and 6.6% respectively.

In central government, taking into account the initial projections of the state budget for 2004, the introduction of new salary scales,[27] the available provisional estimates concerning wage bill developments in 2004 and the change in employment,[28] it is estimated that, while on the basis of the new salary scales the average annual increase was 6.4%, the average gross compensation of employees rose by 8.2%.[29]

22 The rates of change of unit labour costs in the Greek economy as a whole, which are included in the reports produced by the Bank of Greece, refer to the change in the ratio of total compensation of employees (at current prices) to GDP (at constant prices) or, expressed in a mathematically equivalent form, to the change in the ratio of "compensation per employee" to "GDP per employee". The NSSG and Eurostat have always used a different definition (change in the ratio of "total compensation of employees" to "GDP per employed person in general" – i.e. GDP is divided by the total number of employed persons, including the self-employed). This results in different rates being calculated. For its reports, the Bank of Greece prefers to measure the change in productivity on the basis of the change in the ratio of GDP to employees, as it considers that this is a better approximation of the change in labour productivity in branches of economic activity where employees work (see also *Monetary Policy 2002-2003*, Box 2, March 2003, pp. 47-48). It should also be noted that, since 1977, the Bank of Greece has published its own estimates concerning the increase in average earnings in the economy as a whole. These estimates are based on developments in four subsectors of the economy (central government, public utilities, banks and the non-bank private sector). The estimates take into account collective agreements, legislation (e.g. relating to the salaries of civil servants), state budget forecasts and figures on actual budget implementation, together with developments in salaried employment in each subsector. The estimates concerning these subsectors (summarised in Table III.4) are weighted and used to produce the estimate for the economy as a whole. This estimate is not always the same as the one produced by the national accounts department of the NSSG.

23 Compensation per employee, which includes employers' (social security and other) contributions to employees' social security funds and pension funds, along with central government outlays for pensions, is estimated to have increased by 6.9% in 2004, compared with 5.3% in 2003. In the euro area, this magnitude increased at an average annual rate of 2.0% in the first nine months of 2004, compared with 2.3% in 2003.

24 It includes public and private enterprises and banks.

25 Particularly as far as manufacturing is concerned, the rate of growth of unit labour costs is estimated to have reached 4.8% in 2004, almost the same as in 2003 (4.7%).

26 The two-year collective agreements provided for an average annual contractual increase of 6.9% for employees of the Hellenic Telecommunications Organisation (OTE) and 5.7% for Public Power Corporation (DEH) employees in 2004.

27 Law 3205/2003.

28 According to provisional estimates included in the Introductory Report on the 2005 Budget, the central government wage bill (excluding pensions) increased by 9.2% in 2004. If outlays for pensions are included, the increase was 10.5%. The number of civil servants rose at an annual rate of 0.9% in the first half of 2004.

29 The fact that the estimated rate of increase in compensation per civil servant in 2004 is considerably higher than the already high rate of increase stemming from the introduction of the new salary scales reflects: (a) the retroactive payment (pursuant to court decisions) of family allowances for the years 2001-2002 to both spouses when they are both civil servants, (b) the wages paid for additional or overtime employment during the parliamentary elections and the elections for the European Parliament, and (c) the payment of a special bonus to certain categories of personnel involved with security during the 2004 Olympic Games ("Olympic bonus"). Finally, the even higher rate of increase in government outlays when pensions are also taken into consideration is attributable to increased payments for pensions in implementation of the 2004 incomes policy and to the retroactive payment of part of the pay rises awarded for 2003.

2. Prospects for inflation in 2005

The assessment of the prospects for inflation in 2005 is based on estimates and assumptions concerning key determinants, such as the development of oil prices on the world market and exchange rates, developments in production costs, profit margins and demand, in conjunction with the productive capacity of the economy, as well as the impact of the macroeconomic and structural policies pursued. Most of these factors are expected to help in lowering inflation in the current year. However, for reasons which will be explained later in the analysis, it is forecast that:

— Core inflation will ultimately change very little, though the likelihood is that it will increase marginally during 2005.

— "Headline" inflation, as measured by the average annual rate of change in the HICP and the CPI, will increase by approximately 0.3 percentage point, mainly as a result of the technical assumption that weather conditions will be "normal" and that prices of fresh fruit and vegetables will therefore increase relative to the comparatively low levels seen in 2004.

In greater detail, it is expected that the increase in oil prices will continue to have an inflationary effect on price levels,[30] both *directly* (via increased prices for fuels contained in the consumer's "basket") and *indirectly* (affecting, with a time lag, the production costs of other goods and services). However, the total effect of rising oil prices on inflation will be less marked than in 2004. More specifically, it is not expected that increased oil prices will have any significant second-round effect in Greece, i.e. as a result of wage increases, given that in most cases wage increases for 2005 were determined in 2004 and are greater than the inflation rate. Also, based on the most recent forward prices, it can be assumed that average annual Brent crude oil prices on the world market will increase to around $44 per barrel in 2005 (from $38 in 2004), i.e. by 15.5-16%. However, based on the technical assumption that the exchange rate will remain stable at the level reached in the last ten days of January this year (€1 = $1.302), the average annual appreciation of the euro against the dollar will be 4.7% in 2005. Thus, the increase in the average annual price of crude oil in euro is expected to be limited to 10 – 10.5% approximately (from 21.5% in 2004), though this figure is, of course, still significant. This forecast is, however, characterised by a high degree of uncertainty, both as regards oil prices in dollar terms and the exchange rate of the dollar against the euro.

Based on the technical assumption that, for the whole of 2005, the exchange rate of the euro against all other currencies will remain at the same level as in the last ten days of January this year, it is expected that increases in the prices of the other products (excluding oil) imported into Greece from non-euro area countries[31] will continue to be limited. In the case of commodities (raw materials etc.) excluding oil, the prices of which in US dollars are expected to remain basically unchanged[32] or increase only slightly in 2005, the appreciation of the euro will result either in a fall in commodity prices in euro terms or in these prices remaining unchanged. At the same time, the appreciation of the euro will con-

30 For certain medium-term effects on supply, see Part 3 of this chapter.
31 Based on this technical assumption (which corresponds to that already noted with regard to the exchange rate of the euro against the US dollar), it is calculated that the average appreciation of the exchange rate of the euro weighted on the basis of Greece's external trade will be 0.5% in 2005 (almost as much as in 2004).
32 See also: Eurosystem staff macroeconomic projections for the euro area (ECB, *Monthly Bulletin*, December 2004).

tribute to a small drop in inflation in the euro area (see Chapter II.2), resulting in the continuation of the slowdown of the (already low) rate of increase in the prices of imported goods and services from euro area countries.

Furthermore, based on certain data and assumptions, it is estimated that in 2005 the rate of growth of unit labour costs may fall noticeably in the economy as a whole (to 2.7% from 4.2% in 2004) and to a lesser degree in the business sector (to 2.8% from 3.2%).[33] This forecast reflects the estimate that the rate of increase in average earnings in the whole economy will decelerate (mainly because of wage restraint in central government) by approximately one percentage point (i.e. to 5.4%). A slowdown is also expected, albeit to a lesser degree, in the rate of increase in productivity (GDP per employee), to 2.4% in 2005 from 2.6% in 2004. The forecast that productivity growth will fall slightly is based on the estimate that GDP growth (see Section 3 of this chapter) will decelerate slightly more in 2005 than employment growth. However, the possibility cannot be ruled out that the deceleration in employment growth will be about the same as the acceleration in GDP growth (see also Section 4 of this chapter). If this comes true, the increase in productivity will be greater (roughly equal to that of 2004) and the rate of increase in unit labour costs will fall still further (to 2.5%).

Concerning average earnings in 2005, it is estimated that the average compensation of central government employees will rise by 6% (compared with 8.2% in 2004).[34] As a rule, in the non-bank private sector, banks and public enterprises, increases were determined by the two-year collective agreements signed last year and are roughly the same as the increases awarded for 2004.[35] In addition, if account is taken of the forecast slowdown in the growth rate of GDP (see Section 3 of this chapter), the high rate of unemployment and the voluntary early retirement plans in certain enterprises, the positive differential between the increase in actual (gross) earnings paid and that in contractual earnings (i.e. wage drift) may be limited this year. It is therefore estimated that the average increase in gross earnings is likely to be 5.6% in the non-bank sector, 6.4% in public enterprises and 5.4% in banks. Hence, average earnings in the economy as a whole will rise by 5.4%, as already noted.[36]

Inflationary pressures on the demand side are expected to be limited in comparison with 2004, since the growth rate of private consumer demand will decelerate, although it will still be high (see Section 3 of this chapter), while excess demand will weaken. According to the available forecasts,[37] the "output gap" will remain positive, but will nonetheless fall in 2005 (see Chart III.10).[38] Current fiscal policy, which aims to cut back the general government deficit as a percentage of GDP, will also play a role in reducing inflationary

33 According to the European Commission, the rate of increase in unit labour costs in the euro area is forecast to rise, but will remain low (1.2%).

34 According to the 2005 Budget, the total increase in the wage bill excluding pensions will reach 6.5% (compared with 9.2% in 2004), while outlays for salaries and pensions will increase by 5.9% (compared with 10.5% in 2003). If the increase in the number of civil servants is limited (in the order of 0.5%), the average compensation of civil servants will increase by 6%. As always, this percentage includes all other charges included in wage costs apart from the increase in the regular salaries of civil servants, which, according to government announcements on 14 February 2005, will be in the order of 3% (the increase in basic salaries will be 3.6%).

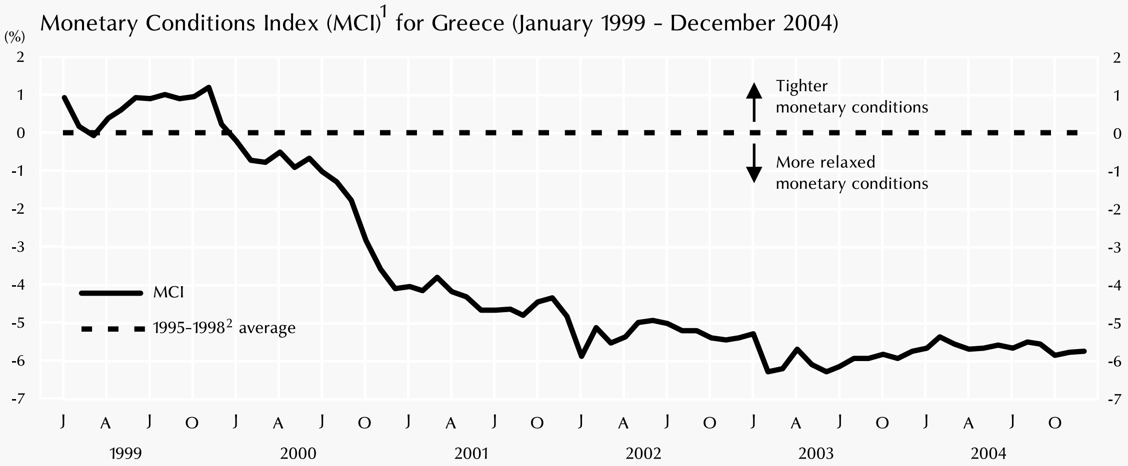
35 Specifically, the NGCLA provides for an average annual increase of 4.7% for the unskilled blue-collar and white-collar workers with previous employment and 5.6% for those without previous employment, while the average increase for all categories covered by the agreement is estimated at 4.9%. At a branch level, the contractual increases in the private sector are of the order of 5%. The average annual increase in contractual earnings is 4.9% for bank personnel, 5.5% for Hellenic Telecommunications Organisation (OTE) employees and 6.3% for the Public Power Corporation's (DEH) personnel.

36 Compensation per employee will increase by 5.2%.

37 See footnote 15 above.

38 To between +0.5 and +1.9, from between +1.1 and +2.2 in 2004.

Chart III.12
Monetary Conditions Index (MCI)[1] for Greece (January 1999 - December 2004)



1 The Monetary Conditions Index (MCI) is defined as:
MCI=0.25 (E(t)/E* - 1) + 0.75 (R(t) - R*), where E(t): real effective exchange rate based on the CPI, E*: average real effective exchange rate for 1995-1998, R(t): real interest rate (3-month Athibor minus CPI inflation until December 2000; thereafter 3-month Euribor minus CPI inflation), R*: average real interest rate for 1995-1998 (see note 2).
2 Excluding the period of serious market turmoil from October 1997 to February 1998.
Sources: Bank of Greece and IMF.

pressures. Although monetary conditions are still relaxed on the whole, they are becoming comparatively tighter, given that in recent months the real exchange rate has continued to appreciate on an annual basis, whereas real interest rates[39] remain negative, but their change is rather negligible (see the Monetary Conditions Index in Chart III.12).

The intensification of controls to ensure adherence to market regulations is expected to have a downward effect on inflation, as is the more active involvement of the Competition Commission and the upgrading of its role (see also the Appendix to this chapter). It should also be noted that the government had announced (in June 2004) its policy to limit the increase in public utility rates in 2004 and 2005. In fact, it is calculated that, in 2004, rates for public utilities (provided by both public and private enterprises) and certain fees set by the State[40] increased at an average annual rate of 3% (after excluding telecommunications rates, which are still on a downward path owing to relatively competitive conditions in the market) and contributed to an annual rise of just 0.16 percentage point in the general CPI. However, it is considered possible that the corresponding rises in rates in 2005 will be greater (in the order of 5-5.5% on average), reflecting an increase in various cost factors. In this case, the increase may add 0.30 percentage point to the annual rise in the CPI.

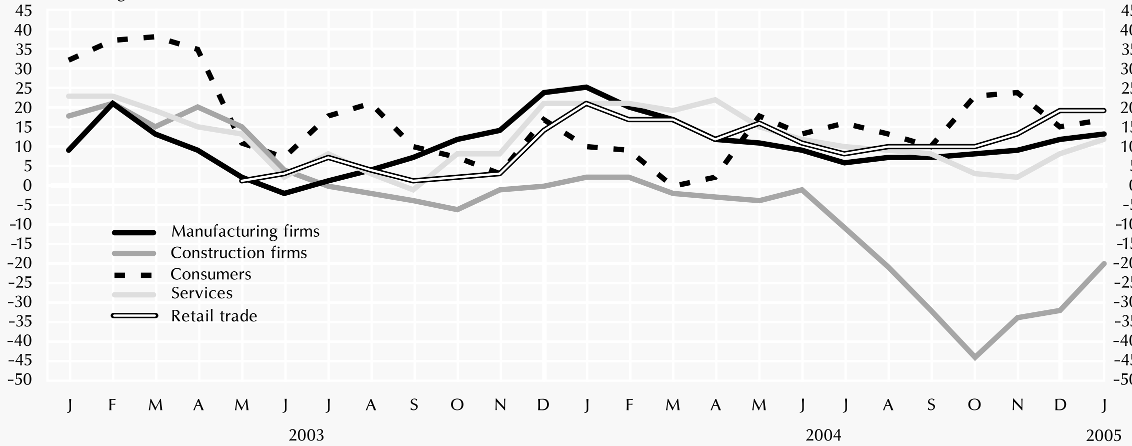
As for short-term inflation prospects, the latest business surveys by IOBE (December 2004 and January 2005) recorded an increase, compared with the immediately preceding months, in the percentage of firms in manufacturing, retail trade and services (excluding retail trade and banking) which forecast a rise in the prices of their products

39 The (three-month) Euribor money market rate, deflated by the annual change in the Greek CPI.
40 Comprising the rates applied by the Public Power Corporation (DEH), the Hellenic Post Office (ELTA), the Hellenic Railways Organisation (OSE), the Water Supply and Sewerage Company (EYDAP) and other water supply companies, Olympic Airlines and other private airlines, hospitals and private clinics, and also public transport fares, National Radio and Television Network (ERT) fees, municipal fees, tolls and road taxes. All these together in 2004 represented 5.8% of the "consumer's basket". The rates applied by the Hellenic Telecommunications Organisation (OTE) and private mobile telephony companies (2.4% of the "basket" in 2004) are excluded.

Chart III.13

Inflation expectations[1] of consumers and business firms (January 2003 - January 2005)

(Percentage balances)



1 The responses of business firms concern the prospect, in the next 3-4 months, of price increases for the goods they produce, while consumers' responses concern the prospect of a faster increase in consumer prices in the next 12 months. The data for consumers are seasonally adjusted.

Sources: IOBE and European Commission, *Business and consumer survey results*.

over the coming 3-4 months. In addition, the percentage of consumers who predict increased inflation over the next twelve months (as recorded in a survey carried out on behalf of the European Commission – see Chart III.13) remains high. By contrast, construction firms continue to forecast a drop in their prices (which, however, do not affect the level of consumer prices).

The impact of the aforementioned factors can be summed up as follows:

— On the one hand, the direct effect of increased oil prices on inflation (after taking account of the appreciation of the euro) will be less than it was in 2004.

— Moreover, the slowdown in the rate of increase in unit labour costs as well as in demand, efforts to reduce the public deficit, certain structural policy measures and the more intensive supervision of the market may also all help to reduce inflation. Of course, the rate of increase in demand will remain relatively high (and the "output gap" positive). Also, the rate of increase in unit labour costs will continue to be significantly higher than in the euro area.

— On the other hand, the anti-inflationary effect of the appreciation of the euro will, based on the aforementioned technical assumptions, be less marked than in 2004.

— In addition, the significant acceleration in 2004 of the rise in the wholesale prices of domestic industrial products (excluding fuel) for home consumption has not been fully passed on to the retail prices of consumer goods.[41] Consequently, inflationary pressures that have built up at the wholesale level may affect consumer prices in 2005. For the same reasons, part of the indirect effect on the prices of goods and services of sharp oil price rises in 2004 is likely to become noticeable —with a greater lag than is usual— in 2005.

41 The rate of increase in consumer goods prices (excluding fuel and fresh fruit and vegetables) accelerated less rapidly in 2004 than did the rate of increase in the wholesale prices of domestic industrial goods. This was a reflection of the slowdown in the rate of increase in the prices of imported products.

It should also be remembered that the increase in public utility rates and certain fees set by the State may be greater in 2005 than in 2004.

— Finally, the shorter than usual period of winter sales this year (1-28 February, compared with 15 January to 28 February in 2004) does not just explain the temporary rise in the annual inflation rate by about one percentage point in January, but also adds almost 0.1 percentage point to the average annual inflation rate for 2005 (as well as to core inflation).[42]

On the basis of the foregoing analysis, it is forecast that core inflation in 2005 will on average be roughly the same as in 2004. It is also possible that there will be a marginal increase in the last quarter of this year compared with the fourth quarter of 2004 (3.2%). It is also forecast that headline inflation, as measured on the basis of the HICP, in the fourth quarter of 2005 will practically be at the same level as in the last quarter of 2004 (3.2%); the average annual level, however, will increase slightly (to 3.3% from 3.0%). Account must be taken of the fact that, while the average annual increase in retail fuel prices in 2005 will be less than in 2004 and the annual rate of change in these prices will be negative in the final months of the current year, the prices of fresh fruit and vegetables will rise in 2005 in comparison with the relatively low prices in 2004 (of course based on the "technical" assumption that weather conditions this year will be "normal").

This forecast involves a considerable degree of uncertainty surrounding factors such as crude oil prices, exchange rates and the development of productivity (and therefore unit labour costs). If, for example, the price of oil rises more than forecast or if the upward trend in the value of the euro against the dollar is reversed, then inflation is likely to reach a higher level than currently forecast. Should the rise in productivity ultimately be faster than forecast, inflation may fall to a lower level.

3. Economic activity: developments in 2004 and prospects for 2005

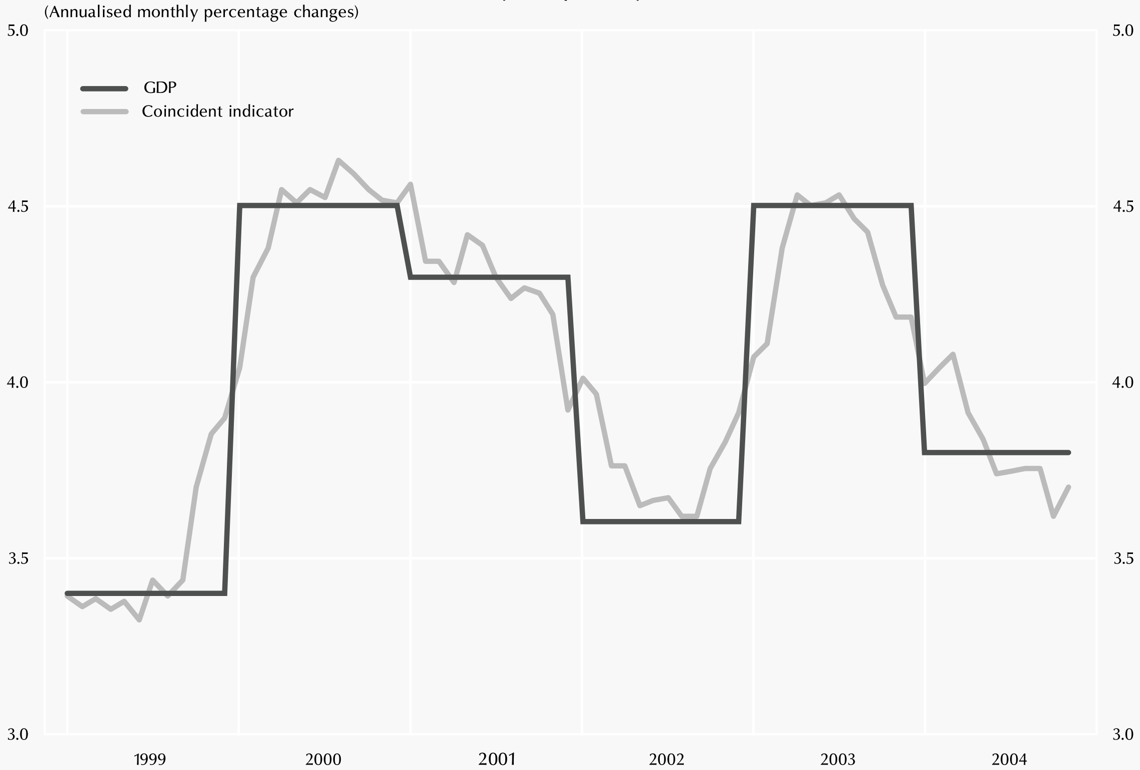
GDP growth remained high in 2004, though it decelerated, mainly because the completion of the investment projects associated with the Olympic Games led to lower growth of gross fixed capital formation than in 2003. On the basis of the NSSG's *flash* estimates (14 February 2005) for the fourth quarter of 2004 (also released by Eurostat on 15 February 2005), which will be revised, the average annual GDP growth rate was 3.9% in 2004, against 4.5% in 2003.[43] Moreover, the rise in the coincident indicator of economic activity, which is compiled by the Bank of Greece and summarises current developments (see Chart III.14), slowed gradually and almost continuously from April 2004 and stood at 3.7% in November 2004 (from an average 4.2% in the last quarter of 2003).[44] Other indicators (compiled by the European Commission and the OECD) provide a similar picture.[45] *Taking into account all the available data, the Bank of Greece estimates that GDP grew by 3.8% in 2004.*

42 This reflects the fact that the sales period in 2005 will be two weeks shorter than in 2004.
43 In May 2004, the Ministry of Economy and Finance estimated that GDP will grow by 3.7% in 2004 and 3.9% in 2005 and those estimates were maintained both in the Introductory Report on the 2005 Budget (November 2004) and in the Updated Stability and Growth Programme released in December 2004.
44 Annualised monthly rates.
45 The economic sentiment indicator for Greece (compiled by the European Commission, based exclusively on business and consumer survey results and incorporating, *inter alia*, information on future developments), after rising from 103.5 in December 2003 to 115.5 in April 2004, showed a considerable and almost continuous decline thereafter, to reach 91.5 in December. (This fall reflected the increasingly deteriorating assessments and forecasts of construction firms and consumers, as well as the fact that manufacturing firms' forecasts turned negative). Moreover, the assessments and forecasts of retail trade and services firms (services exclude banks and retail trade) remained positive, although they did display a marked decline. However, in January 2005 the economic sentiment indicator recovered slightly to 94.2, mainly reflecting the improving assessments and forecasts of retail trade and services firms. The OECD Composite Leading Indicator for Greece also shows a noticeable decline compared with the first months of 2004.

Chart III.14

The coincident indicator of economic activity compiled by the Bank of Greece

(Annualised monthly percentage changes)



Sources: Bank of Greece (coincident indicator, as well as GDP for 2004) and NSSG (GDP for 1999-2003).

On the demand side, GDP growth in 2004 (see Table III.5) was mainly driven by the strong rise in private consumption and the rebound in exports of services (which is mainly accounted for by the large increase in shipping activity and the rise in travel receipts). The increase in total gross fixed capital formation also contributed to GDP growth, though it slowed down considerably in comparison with 2003, as a result of both the completion of the public and private investment projects associated with the Olympic Games and the halt in private residential investment.

According to available short-term indicators, certain components of consumption (see Tables III.6 and III.7) rose fast (at a rate similar to that at 2003), as evidenced by the increase in retail sales volume (excluding cars) at an annual rate of 4.8% in the first eleven months of 2004 (compared with an average 4.6% for 2003 as a whole) and the impressive recovery in passenger car sales. New passenger car registrations rose by 15.7% in 2004 (after declining by 2.7% in 2003), although in the last quarter of 2004 their annual growth rate slowed significantly[46] (see Chart III.15).[47]

Overall, according to Bank of Greece estimates, in 2004 private consumption grew almost as much as in 2003 (when it had risen by 4.4%,

46 The growth in sales is partly confirmed by the 24.8% rise in payments for passenger car imports in 2004, which however may reflect increased imports of passenger cars used as taxis or for rental during the Olympic Games. There has been a rising trend in new passenger car registrations since the last quarter of 2003, which may to some extent be related to the abolition of restrictions on consumer credit in June 2003.

47 It should be recalled that expenditure for the purchase of passenger cars has a 7% share in consumer expenditure for goods, which in turn accounts for about 50% of total private consumption (goods and services).

Table III.5
Demand and gross domestic product (2002-2004)
(At constant market prices of year 1995, annual percentage changes)

	2002	2003 (estimate)	2004 (estimate under revision)
Final consumption			
Private consumption	3.0	4.4	(3.6)
Public consumption	5.3	-2.5	(5.5)
Gross fixed capital formation	5.7	13.7	(5.8)
Dwellings	8.8	7.3	(-6.5)
Other constructions	0.7	13.2	(12.6)
Equipment	6.9	18.3	(6.5)
Other fixed investment	21.0	3.4	(2.0)
Stocks and statistical discrepancy *(percentage of GDP)*	0.4	0.1	(0.0)
Domestic final demand	4.2	5.3	(4.3)
Exports of goods and services	-7.7	1.0	(7.3)
Exports of goods	-7.1	4.2	(-10.0)
Exports of services	-8.1	-1.3	(20.0)
Imports of goods and services	-2.9	4.8	(8.3)
Imports of goods	3.2	6.6	(7.5)
Imports of services	-26.5	-5.3	(13.0)
Gross domestic product at market prices	3.6	4.5	(3.7)

Sources: NSSG/National Accounts (September 2004) for 2002 and 2003. For 2004: Ministry of Economy and Finance, Revised Stability and Growth Programme (December 2004)– *the figures in parentheses are estimates (under revision) up to 21 March 2005. On Bank of Greece estimates see the main text.*

Table III.6
Indicators of consumer demand (2003-2005)
(Annual percentage changes)

	2003	2004	2005 (available period)
Volume of retail sales[1]	4.6	4.8 (Jan.-Nov.)	
Food-beverages-tobacco	5.4	7.5 (» »)	
Clothing-footwear	1.6	1.5 (» »)	
Furniture-household equipment	4.0	4.4 (» »)	
Books-newspapers-office equipment	7.5	5.3 (» »)	
Retail trade business expectations indicator	9.3	2.8	–5.7 (Jan.)
New passenger car registrations	–2.7	15.7	4.7 (Jan.)
Piraeus Port Authority (OLP) passengers	6.3	–5.4 (Jan.-Nov.)	
Tax revenue from mobile telephony (monthly flat fees)	16.9	13.0	
Outstanding balance of total consumer credit extended by banks	27.2 (Dec.)	37.4 (Dec.)	

1 Revised retail sales volume index (2000=100) excluding VAT.
Sources: NSSG-Eurostat (retail sales), IOBE (expectations), NSSG (cars), OLP, Ministry of Economy and Finance (tax revenue from mobile telephony) and Bank of Greece (consumer credit).

according to the NSSG). Households' real disposable income is estimated to have grown slower than in 2003, but faster than private consumption, which suggests an increase in households' average propensity to save. In this respect, account should be taken of the 3.5% growth of employees' real average pre-tax earnings, increased transfers to economically disadvantaged groups (pursuant to legislation passed in 2003 and 2004 and implemented in 2004),[48] measures to reduce the tax burden (which, however, offset only a part of the "fiscal drag"[49]), as well as a rise in employment (though smaller than in 2003 – see Section 4 of this chapter). The increase in private consumption at almost the same rate as in 2003 (despite the slowdown in the growth of disposable income and the increase in the saving rate) was also supported by the growth in the outstanding balance of consumer loans, which remained high and accelerated (to an annual rate of 37.4% in December 2004, compared with 27.2% in December 2003). Besides, it is estimated that the cumulative rise in the market value of households' assets continued to have a positive effect on private consumption. However, this effect was smaller than in 2003, given that house price inflation (houses are households' main assets) slowed to an annual rate of 2.2% in the first nine months of 2004 (from 6.2% in the corresponding period of 2003, see Table III.8).[50] The increase in the market value of households' assets also reflects, to some extent, the rebound in equity prices on the Athens Exchange.[51]

As regards private consumption, favourable financing conditions in recent years have allowed households greater flexibility with regard to the timing of their consumption decisions. Although the overriding importance of disposable income should not be overlooked, credit deregulation has made possible a better smoothing of the private consumption pattern over time, with a growing share of the population depending less on current income. At first sight, this might be expected to have favourable effects on the stability of GDP growth in the short run. Consumption patterns in Greece are gradually becoming similar to those found in other European countries and consumption tends to be more sensitive to interest rate changes and —more generally— to monetary and credit conditions, which have a direct effect on households' borrowing and savings and an indirect effect on the "current value" of their assets. Of course, to the extent that GDP growth is mainly the result of increases in private consumption, with the latter depending importantly on credit expansion, high growth rates may not be sustainable in the long run if households' debt increases to a level that cannot be serviced. For this reason, sustainable growth requires a substantial improvement in competitiveness, which will be achieved, among other things, through an increase in investment; this will make possible a rise in net exports, which may thus become an important driving force of economic growth. Moreover, the observed increase in the potential growth rate of private consumption in the

T a b l e III.7

Retail sales *value* index (2004)

(Percentage changes over corresponding period of previous year)

Categories	2004 (Jan.-Nov.)
1. Big food stores	8.8
2. Department stores	7.2
3. Food-beverages-tobacco	5.5
4. Pharmaceuticals-cosmetics	6.4
5. Clothing-footwear	5.3
6. Furniture-electrical appliances-household equipment	4.7
7. Books-stationery-other goods	8.1
8. Retail sales not in stores	2.5
General retail sales *value* index	6.5

Source: NSSG.

48 According to Ministry of Economy and Finance estimates on a national accounts basis (Dec. 2004), current transfers to the private sector (mostly households) rose by about 17% in 2004.
49 I.e. the increase in the tax burden resulting from the nominal increase in incomes owing to inflation combined with the progressivity of the tax scale.
50 The growth of dwelling prices has come to a halt in Athens, but continues in other urban centres.
51 The average annual level of stock prices rose by 27.3% in 2004, compared with a decline of 11.2% in 2003.

Chart III.15

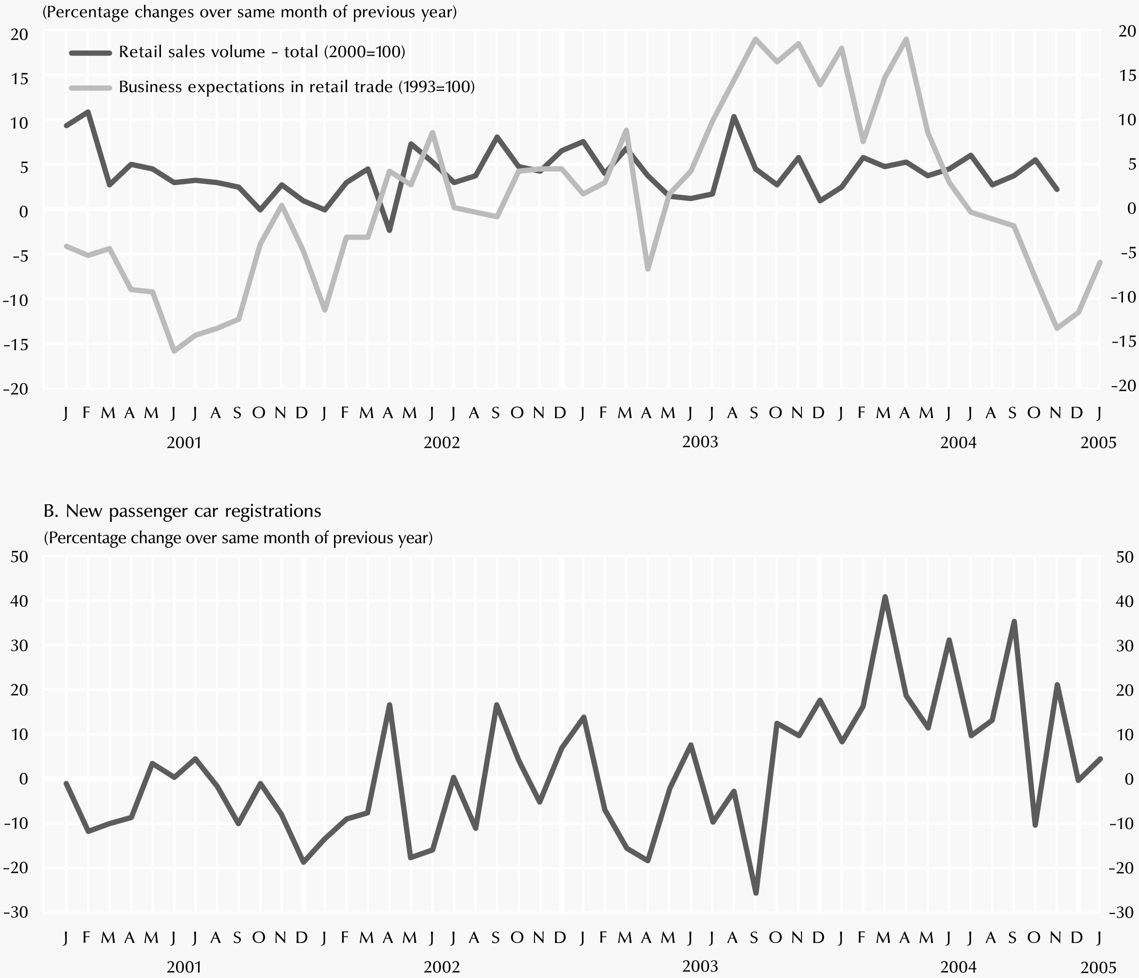
Consumer demand (January 2001 - January 2005)

A. Retail sales volume and retail trade business expectations

(Percentage changes over same month of previous year)

B. New passenger car registrations

(Percentage change over same month of previous year)



Sources: NSSG - Eurostat (retail sales), NSSG (cars) and Foundation for Economic and Industrial Research - IOBE (expectations). The revised retail sales index is calculated excluding VAT. The business expectations index is based on firms' estimates of sales and stocks, as well as on their forecasts of business activity over the next six months.

medium term is due, *inter alia*, to the very important cumulative growth of the population because of the inflow of immigrants.

Data on government budget implementation released by the Ministry of Economy and Finance indicate a considerable increase in government consumption. Moreover, in the Introductory Report on the 2005 Budget it is estimated that, on a national accounts basis, government consumption rose by 5.5% at constant prices in 2004.

According to Bank of Greece estimates in 2004, total gross fixed capital formation (see also Table III.9) rose by some 4.5% at constant prices (compared with 13.7% in 2003 according to the NSSG).

Specifically, general government investment, as estimated by the Introductory Report on the 2005 Budget, rose by 9.4% at constant prices (compared with 11.7% in 2003 according to the NSSG). Bank of Greece data show that disbursements out of the Public Investment Budget (at

T a b l e III.8

Dwelling price index

Period	Urban areas-total			Athens			Other urban areas		
	Index	Percentage changes		Index	Percentage changes		Index	Percentage changes	
	1997=100	Over previous period	Over corre-sponding period of previous year	1997=100	Over previous period	Over corre-sponding period of previous year	1993 Q4=100	Over previous period	Over corre-sponding period of previous year
1994	76.1	. . .	. . .	73.4	9.5	9.5	106.0	. . .	. . .
1995	82.6	8.5	8.5	80.1	9.2	9.2	114.3	7.8	7.8
1996	91.2	10.5	10.5	88.9	11.0	11.0	125.7	10.0	10.0
1997	100.0	9.7	9.7	100.0	12.5	12.5	134.7	7.1	7.1
1998	114.4	14.4	14.4	115.5	15.5	15.5	152.6	13.3	13.3
1999	124.5	8.9	8.9	129.6	12.2	12.2	161.5	5.8	5.8
2000	137.6	10.5	10.5	149.1	15.1	15.1	171.2	6.0	6.0
2001	157.7	14.6	14.6	175.4	17.6	17.6	190.6	11.3	11.3
2002	178.2	13.0	13.0	203.8	16.2	16.2	208.8	9.5	9.5
2003	188.4	5.7	5.7	211.9	4.0	4.0	225.2	7.9	7.9
2002 I	171.5	4.4	13.9	193.6	5.8	16.8	203.9	3.0	10.7
II	178.9	4.3	14.4	208.0	7.4	19.4	205.3	0.7	8.8
III	179.4	0.3	12.4	205.4	–1.3	14.9	209.9	2.3	9.7
IV	183.1	2.0	11.5	208.2	1.4	13.8	215.9	2.8	9.0
2003 I	187.2	2.3	9.2	214.6	3.1	10.8	219.0	1.4	7.4
II	186.9	–0.2	4.5	210.6	–1.8	1.3	223.0	1.8	8.6
III	188.6	0.9	5.1	210.6	0.0	2.6	227.1	1.9	8.2
IV	190.8	1.2	4.2	211.5	0.4	1.6	231.7	2.0	7.3
2004 I	190.7	0.0	1.8	209.7	–0.9	–2.3	233.8	0.9	6.8
II	191.1	0.2	2.2	209.4	–0.2	–0.6	235.3	0.6	5.5
III	193.4	1.2	2.6	211.1	0.8	0.2	239.1	1.6	5.3
2003 July	. . .	. . .	. . .	208.6	0.5	1.9	. . .	. . .	. . .
Aug.	. . .	. . .	. . .	211.9	1.6	4.1	. . .	. . .	. . .
Sept.	. . .	. . .	. . .	211.5	–0.2	1.7	. . .	. . .	. . .
Oct.	. . .	. . .	. . .	210.7	–0.4	2.5	. . .	. . .	. . .
Nov.	. . .	. . .	. . .	211.2	0.3	–0.1	. . .	. . .	. . .
Dec.	. . .	. . .	. . .	212.7	0.7	2.5	. . .	. . .	. . .
2004 Jan.	. . .	. . .	. . .	212.7	0.0	0.2	. . .	. . .	. . .
Feb.	. . .	. . .	. . .	207.1	–2.6	–2.4	. . .	. . .	. . .
March . .	. . .	. . .	. . .	209.5	1.1	–4.5	. . .	. . .	. . .
Apr.	. . .	. . .	. . .	208.0	–0.7	–2.6	. . .	. . .	. . .
May	. . .	. . .	. . .	211.5	1.7	0.3	. . .	. . .	. . .
June	. . .	. . .	. . .	208.5	–1.4	0.4	. . .	. . .	. . .
July	. . .	. . .	. . .	208.8	0.1	0.1	. . .	. . .	. . .
Aug.	. . .	. . .	. . .	212.4	1.7	0.3	. . .	. . .	. . .
Sept.	. . .	. . .	. . .	212.1	–0.1	0.3	. . .	. . .	. . .

Sources: For the other urban areas: Bank of Greece (quarterly data). For Athens: calculations based on data from "Danos and Associates" (1993-97) and "Property Ltd" (monthly data for 1997-04). For the total of urban areas: weighted index based on the housing stock in Athens and other urban areas.

current prices) increased by 11.7% in 2004, compared with 19.6% in 2003.

As regards private residential investment, its rise came to a halt in 2004 according to Bank of Greece estimates (compared with a 7.3% growth in 2003 according to the NSSG). The volume of private construction activity on the basis of permits issued, which is a leading indicator, had already fallen considerably in the fourth quarter of 2003 (average annual rate: –13.5%), and decreased at an average annual 4.1% during the first eleven

T a b l e III.9
Indicators of investment demand (2003-2005)
(Annual percentage changes)[1]

	2003	2004	2005 (available period)
Capital goods output	0.8	–0.3	
Investment expenditure (at current prices) of private industrial firms [2]	–8.0[3]	–32.3[4]	–2.4[4]
Capacity utilisation rate in the capital goods industry	(78.9)	(78.6)	(72.8) (Jan.)
Outstanding amount of loans to non-financial corporations with a maturity of over one year	20.1 (Dec.)	18.2 (Dec.)	
Disbursements out of the public investment budget	19.6	11.7	–76.6 (Jan.)
Volume of private construction activity (on the basis of permits issued)	1.5	–4.1 (Jan.-Nov.)	
Cement production	3.6	–2.3	
Construction business expectations indicator	0.8	–28.9	–43.6 (Jan.)
Outstanding balance of total bank credit to housing	25.0 (Dec.)	24.8 (Dec.)	

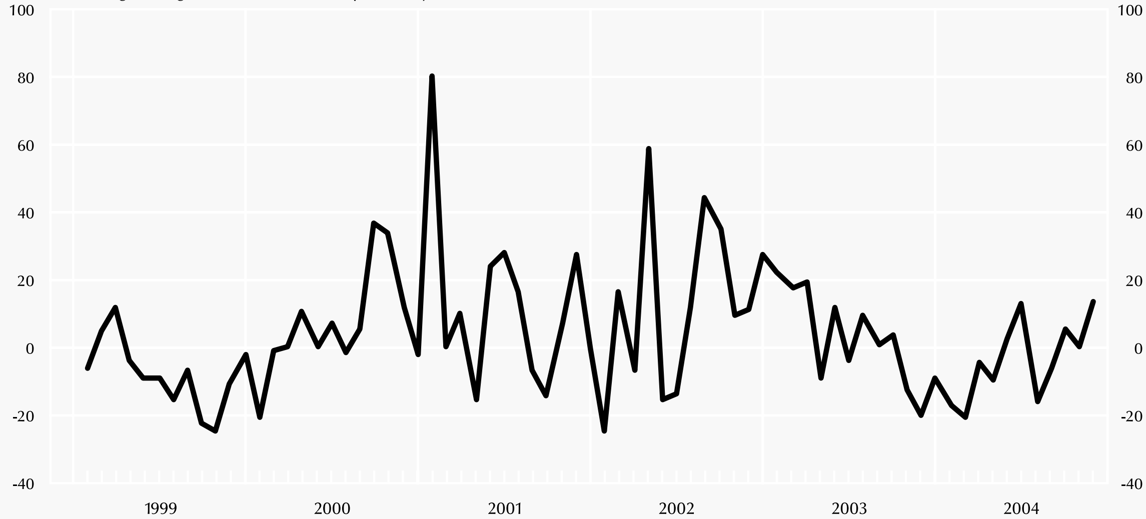
1 With the exception of capacity utilisation, which is expressed in percentages.
2 Estimates of firms participating in the IOBE investment survey.
3 Estimate of the March-April 2004 survey.
4 Estimate or forecast of the October-November 2004 survey.
Sources: NSSG (capital goods output, volume of private construction activity, cement production), IOBE (investment expenditure, capacity utilisation rate, business expectations indicator), Bank of Greece (loans to non-financial corporations, disbursements out of the public investment budget, housing loans).

months of 2004 – see Chart III.16.[52] However, the annual growth of the outstanding balance of housing loans remained high (at 24.8% in December 2004, compared with 25.0% in December 2003). This reflects, on the one hand, the time lag between the issuance of a building permit and the execution of the project concerned and, on the other hand, the fact that housing loans are also used to finance the purchase of existing (old or newly built) dwellings, as well as to undertake repairs.[53]

Finally, according to Bank of Greece estimates, the growth rate of investment by public and private enterprises decelerated substantially. As mentioned in the Introductory Report on the 2005 Budget, public enterprises' investment rose by 9% (at current prices) in 2004, against an increase of 28% in 2003. Moreover, private business investment in the telecommunications, hotel, domestic maritime transport and other services sectors is estimated to have grown considerably in 2003 and in the early months of 2004 (in anticipation of the Olympic Games), but its average growth rate inevitably dropped for 2004 as a whole. In addition, industrial firms' investment declined.[54]

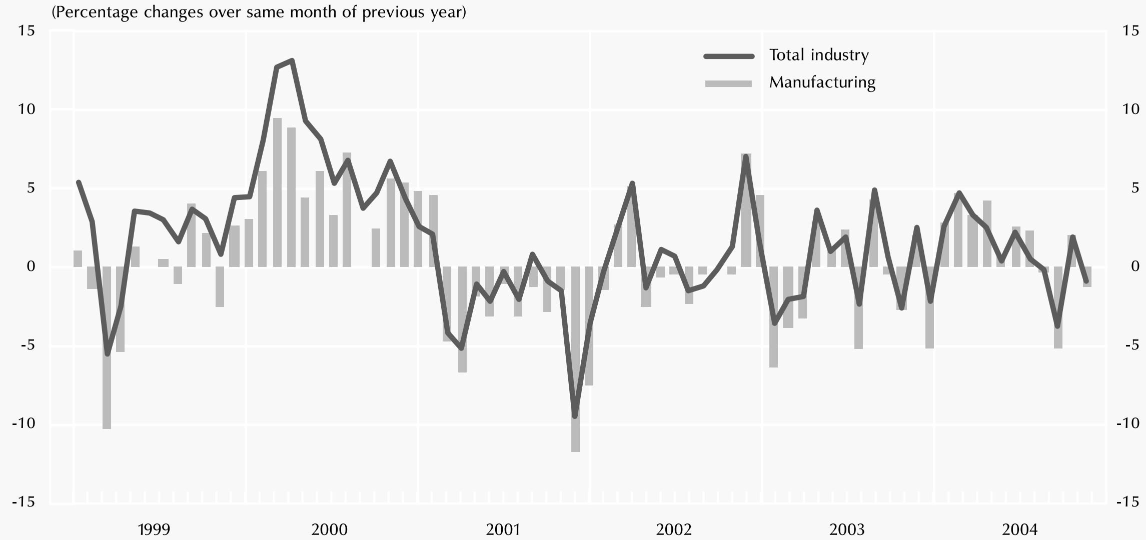
52 The estimate that private residential investment remained stagnant in 2004 takes account of the time lag between the issuance of a building permit and the execution of the project concerned. Characteristically, in the first nine months of *2003* (i.e. before the volume of construction activity on the basis of permits issued started to decline), this indicator was rising at an average annual rate of 7.5%.
53 It should also be noted that, according to the IOBE business survey of the construction sector, firms' assessments concerning their house-building business were negative only in February, March and September 2004, though their estimates of business prospects were negative, as were their forecasts about employment.
54 According to estimates of private industrial firms participating in the IOBE investment survey for October-November 2004, investment expenditure fell by 32.3% at current prices.

Chart III.16
Volume of new buildings and extensions on the basis of permits issued (January 1999 - November 2004)
(Percentage change over same month of previous year)



Source: NSSG.

Chart III.17
Industrial production (January 1999 - December 2004)
(Percentage changes over same month of previous year)



Source: NSSG, revised series, 2000 = 100.

The change in the real external balance on a *national accounts basis*,[55] according to estimates of the Bank of Greece, had a negative contribution to GDP growth in 2004 (1.2 percentage points), roughly equal to that in 2003. More specifically, it is estimated that exports of goods and services rose by almost 7% in 2004, compared with a very small increase in 2003 (1.0%, according to the NSSG), and that imports of goods and services grew by about 8.5% (compared with 4.8% in 2003, according

55 The real external balance is the difference between exports and imports of goods and services (at constant prices).

Chart III.18
Output and business expectations in manufacturing (January 2001 - January 2005)

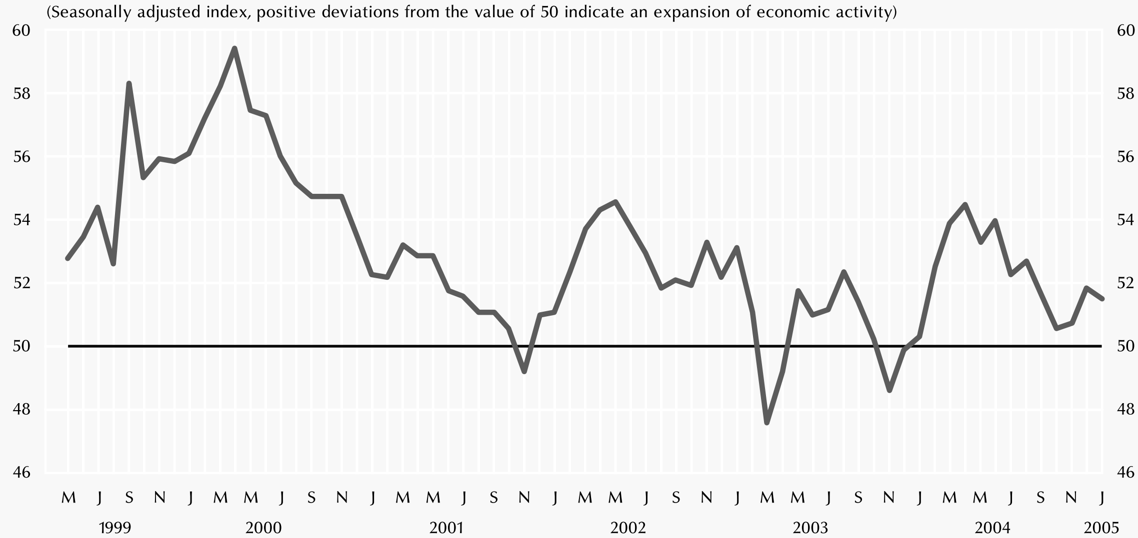
Sources: NSSG (output) and IOBE (expectations). The index of business expectations is based on business firms' estimates of total demand and stocks, and on output forecasts for the next 3-4 months.

to NSSG). (For further analysis see Section 5 of this chapter.)

On the supply side, as already mentioned, construction activity rose at a slower pace, while retail trade business kept increasing fast. Moreover, activity in the telecommunications sector continued to rise strongly.[56] Overall, total industrial output[57] grew at an average annual rate of 0.9% in 2004 (compared with 0.3% in 2003[58]) and manufacturing output rebounded (it also increased by 0.9%, after declining by 0.4% in 2003 as a whole – see Charts III.17 and III.18). These developments are confirmed by the Purchasing Managers' Index (PMI), which implies that manufacturing output rose continuously throughout 2004 (see Chart III.19). Finally, in the agricultural sector, gross value added at constant prices recovered and rose by 1.3%, according to

56 Tax revenue from mobile telephony (flat monthly fee per connection) rose at an average annual rate of 13.0% in 2004.
57 Comprising mining-quarrying, manufacturing and electricity, as well as natural gas and water distribution.
58 NSSG new revised index.

Chart III.19
Purchasing Managers' Index (PMI) for manufacturing (May 1999 - January 2005)
(Seasonally adjusted index, positive deviations from the value of 50 indicate an expansion of economic activity)



Sources: Hellenic Purchasing Institute and NTC Research.

Eurostat's[59] first estimates, after declining for four years in succession (NSSG estimates).

* * *

As regards prospects for economic activity in 2005, the GDP growth rate is forecast to slow to around 3.3%. In particular, it is estimated that some of the factors that supported fast economic growth in recent years will also contribute to GDP growth in 2005. Increased private consumption will continue to be the main driving force. Additionally, developments in the global economy are expected to be favourable in general and to have a positive effect on the exports of goods, shipping services and tourism. On the downside, projects associated with the Olympic Games have been completed; the need for fiscal adjustment is leading to a curtailment of public investment expenditure; the stagnation of private residential investment is already in evidence since 2004. For these reasons, total investment is not expected to have a significant contribution to GDP growth. The rate of increase in government consumption is projected to moderate notably, partly reflecting the need for fiscal adjustment. Thus, a decline in the growth rate of economic activity should be expected in 2005. Naturally, economic growth will largely depend on the efforts to ensure macroeconomic stability (fiscal as well as price stability) and to improve international competitiveness, which fell significantly in the 2001-2004 period. If these efforts are successful, the Greek economy will benefit from the ongoing recovery of the global economy. Moreover, entrepreneurship will be encouraged and investors' confidence will be enhanced, boosting private business investment, which is also favoured by the increase in profitability over the last two years. This calls, in addition, for the implementation of the new tax and growth-supporting legislative provisions and the fast promotion of further structural reforms in order to modernise the public sector, stimulate competition and encourage innovation. Besides, private and public invest-

59 Statistics in Focus-Agriculture and Fisheries, No. 38/2004, December 2004.

ment in infrastructure projects, particularly in the regions, should continue to increase strongly, in order to underpin high growth in domestic demand. Given the fiscal constraints, such an investment policy requires a more effective utilisation of resources from the Third Community Support Framework (CSF III).

Expected developments in the international environment[60] should have a positive effect on Greek exports of goods and services. Apart from the observed high growth rates in maritime transport activity, it is expected that the effect of the increased publicity, during 2004, for Greece as a tourist destination will show in 2005. Indeed, certain indications point to an increase in foreign tourist bookings for this year's tourist period.[61]

By contrast, the rise in international oil prices to a high level may be of a more permanent nature.[62] This could have a lagged negative effect on investment projects, with a significant indirect impact on economic activity.

Turning to domestic factors, the overall fiscal policy stance is restrictive, as reflected mainly in the projected significant decline in public investment at constant prices and the reduction in some items of consumption expenditure. However, although the projected deceleration in the growth rate of the total wage bill as well as of compensation per employee in central government is indeed substantial compared with 2004 (when the corresponding rates of increase were particularly high due to the special reasons mentioned in Section 1 of this chapter), it does not constitute a restrictive measure, since *compensation per employee in central government* is expected —according to the Budget— to rise in 2005 by about as much as in *2003* and, in any case, noticeably more than inflation. This, combined with the wage increases for private sector employees (which had already been agreed upon last year and are essentially similar to those for 2004), is one of the main factors which will support the rise in private consumption in 2005. Moreover, the government seeks to offset the planned reduction in public investment (at constant prices) by providing more incentives for private investment (through the tax and development laws[63]) and promoting the execution of big public projects by concession agreements to be passed by Parliament, while a general institutional framework allowing for the public-private partnerships is being prepared. The question is, however, whether —despite the positive effect of the above factors— the (aforementioned) almost continuous deterioration of confidence indicators in recent months will adversely affect investment decisions.

On the basis of those facts and assumptions (including the speedy implementation of the measures enacted and the promotion of those announced), the GDP growth rate in Greece is projected (as mentioned above) to fall to about 3.3% in 2005, still standing considerably higher than the growth rate of the euro area as a whole. Specifically, private consumption should increase by more than 3.5%, though less than 4%. Moreover, it is estimated that the growth rate of households' real disposable income will continue to decelerate and will actually be lower than the growth rate of private consumption. This suggests that households' saving rate will drop and that con-

60 See Chapter II.1-2 on the projected growth rate of the global and the European economy and the world trade volume, and Section 2 of this chapter on assumptions and forecasts concerning the development of oil prices and exchange rates.
61 Moreover, according to the IOBE business and consumer survey in the services sector, forecasts of hoteliers, restaurant owners and travel agents about demand developments in the coming months clearly improved in December 2004 and January 2005.
62 See Chapter II.1. Also see OECD, "Oil prices: developments, drivers, economic consequences and policy responses", *Economic Outlook*, December 2004.
63 Passed on 30 November 2004 and 14 December 2004, respectively.

sumption will continue to be supported by credit expansion. Government consumption will increase by 1.5% on a national accounts basis, according to the Introductory Report on the Budget, while, on the basis of Bank of Greece estimates, the growth rate of total investment is expected to be very low (around 1%), reflecting the significant decline in general government investment (which could fall by as much as 17%, according to the Introductory Report on the Budget) and a small rise in housing investment. By contrast, business investment may increase (if the effects of the aforementioned favourable factors prevail over those of the unfavourable ones).[64] Overall, domestic demand will remain the main factor contributing to GDP growth, though this contribution is expected to fall to 3.2 percentage points in 2005 (against 4.9 percentage points in 2004). The contribution of the external sector, which was negative in 2004 (–1.2 percentage points), is expected to be neutral (zero) in 2005, reflecting forecasts that, while exports of goods and services will increase about as much as in 2004 (by some 7%), imports of goods and services will grow markedly less, i.e. by about 4.5% (compared with some 8.5% in 2004).

4. Employment: developments in 2004 and prospects for 2005

The substantial growth of GDP in 2004 and the holding of the Olympic Games naturally contributed to a rise in employment. It is not possible to obtain accurate estimates on the size of the change and on the sectors affected, as comparable data from the Labour Force Survey are not available (see Chart III.20). However, it is estimated that the increase took place mainly in the first half of the year, when employment rose in most sectors of economic activity. By contrast, employment in construction fell in the second half of 2004, while employment in trade and services kept rising.[65]

Available OAED data show that job creation in the first eight months of 2004 was significantly higher than in the corresponding period in 2003 (117,961 new jobs, compared with 77,148).[66] However, *between September and November* a decline in net job creation was recorded, which was more than double that in the corresponding quarter of 2003. This decline was only partly seasonal (owing to the end of the summer period) and is mostly attributable to lower activity after the end of the Olympic Games in sectors associated with the Games. Thus, *during the eleven months from January to November 2004*, job creation was marginally *lower* than in the corresponding period of 2003 (47,735 new jobs, compared with 48,275).

As regards developments by branch of economic activity (see also Table 6 in the Statistical Appendix), employment in services (excluding retail trade and banks) for most months in 2004 was higher relative to 2003 —on the basis of the relevant business survey conducted by IOBE— reflecting, *inter alia*, increased employment in hotels, restaurants and tourist agencies, i.e. industries associated with the holding of the Olympic Games.

64 However, according to the IOBE investment survey (October-November 2004), private industrial firms forecast a 2.4% drop (at current prices) in their investment expenditure in 2005.

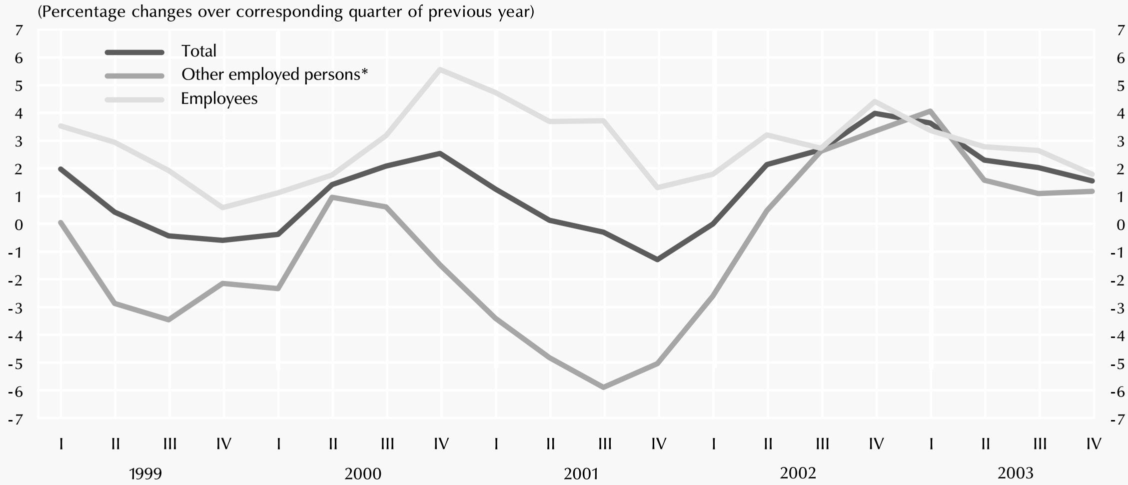
65 The estimates concerning developments in employment are based on Manpower Employment Organisation (OAED) data on employment flows, the IOBE and the Hellenic Purchasing Institute-NTC Research (PMI) business and consumer surveys, the NSSG survey on employment in retail trade, Ministry of Economy and Finance data on employment in the public sector, as well as balance sheets of companies listed on the Athens Exchange. The usual source of data on changes in employment, i.e. the Labour Force Survey (LFS) of the NSSG, cannot serve this purpose at the current juncture, as the fact that the survey is conducted on a new sample and by a new methodology from the first quarter of 2004 makes intertemporal comparisons unreliable. Changes in the LFS have been presented in the recent press releases of the NSSG, as well as in a communication of the NSSG Press and Public Relations Office (8 July 2004).

66 OAED data should be treated with caution because they do not provide a comprehensive picture of employment, as they neither cover the self-employed nor fully record voluntary quits.

Chart III.20

Employment (1999 - 2003)

(Percentage changes over corresponding quarter of previous year)



* Other employed persons= Self-employed with staff (employers)+Self-employed without staff + Assistants in family businesses.

Source: New revised data for 1998 - 2003, published in January 2005. *No changes are given for 2004, as data are not fully comparable, due to a change in the survey sample.*

The average annual growth rate of employment in retail trade, according to the new index for this industry,[67] was 3.8% for the nine months from January to September 2004. The annual rate of change is estimated to have remained positive, although possibly lower, in the last quarter of 2004.

Employment in banks at the end of the year is estimated to be lower than at the end of 2003, owing to voluntary early retirement programmes implemented by some big banks.

There is no evidence that employment in manufacturing changed significantly compared with 2003, while employment in construction is estimated to have decreased considerably in the second half of the year —after the completion of projects associated with the Olympic Games— compared with the corresponding period in 2003.

Employment in central government[68] grew at an average annual rate of 0.9% in the first half of 2004. By contrast, employment in public enterprises fell by an average annual rate of 2.1% during the first nine months of 2004.

Despite the rise in employment, unemployment remained high and stood at 10.8% in the *first half of 2004*, according to LFS data (see Chart III.21).[69] These data show that a very large proportion of the unemployed (53.1%) are long-term unemployed, i.e.

67 The "Retail Trade Employees Index" compiled by NSSG includes the total number of persons employed in a firm, irrespective of their employment status or skills (owners, partners, family members, managers, salespersons, auxiliary personnel) and of whether they are temporarily and/or seasonally employed, are full-time or part-time employees and receive or do not receive remuneration.

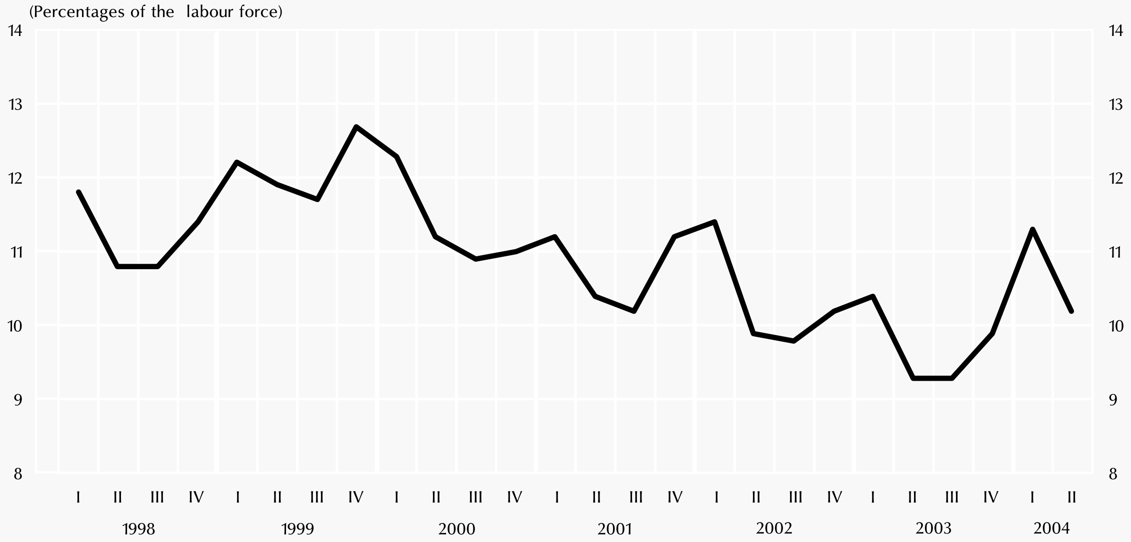
68 Comprising the personnel of ministries, regional governments, municipalities, hospitals and security forces.

69 For the reasons referred to above, LFS data are not suitable for intertemporal comparisons. This also applies to OAED data on the number of the registered unemployed, as the number of persons registered with OAED is particularly affected by the fact that persons until recently registered as economically non-active may register as unemployed in order to participate in subsidised programmes; actually, some of those persons often report that they do not wish to get a job. According to data released since October 2004 by the Employment Observatory (an OAED subsidiary), around 8% of registered unemployed persons do not wish to work. In addition, since October 2004 data on registered unemployed persons also include those seasonally unemployed, thus making comparisons with previous years difficult.

Chart III.21

Total unemployment rate (1998 - 2004)

(Percentages of the labour force)

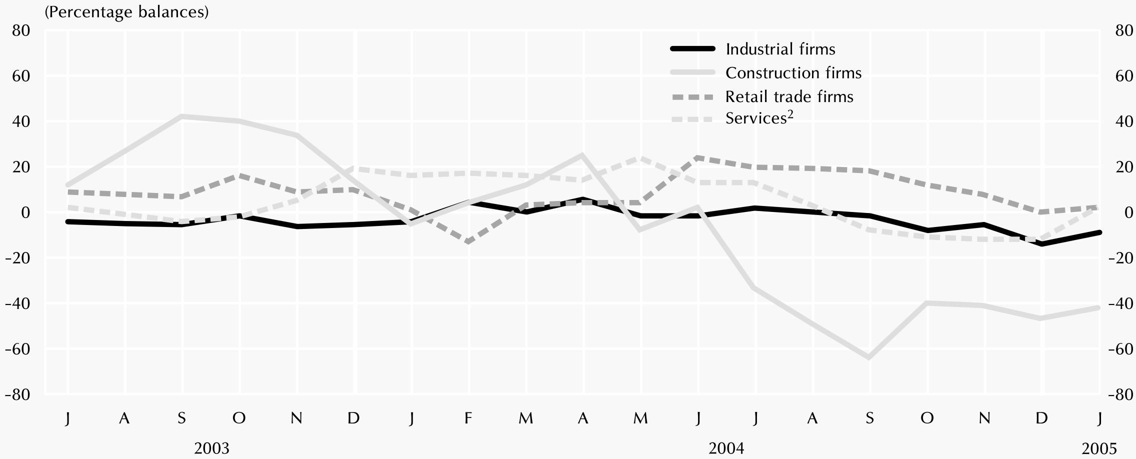


Source: NSSG, Labour Force Surveys. New revised data for 1998 - 2004, published in January 2005.

Chart III.22

Business and consumer forecasts[1] for employment (July 2003 - January 2005)

(Percentage balances)



1 Firms were asked to assess the prospect of an increase in their number of employees over the coming period.
2 Excluding banks and retail trade firms.

Source: IOBE, Business Surveys.

persons unemployed for a period longer than a year. The high unemployment rates of women (16.5%) and the young, i.e. those between 15 and 24 years of age (27.7%), are also a matter of concern.

As regards the outlook for employment, the Ministry of Economy and Finance, in its Updated Stability and Growth Programme (released in December, but expected to be further revised) forecast that employment in 2005 will grow by 1.5% and that the unemployment rate will fall by 0.6 percentage point. Given that, as mentioned in the Programme, the recruitment policy in the public sector will be "extremely restrictive", these

Table III.10
Business expectations for employment
(Weighted percentage balances)

	January 2005	1998-2004 average	Maximum	Minimum
Industry	–11	–1	14	–17
Construction	–42	26	60	–64
Services	2	3	38	–37
Retail trade	2	13	56	–13

Source: IOBE business surveys.

forecasts suggest that a significant rise is anticipated in employment in the private sector. Moreover, it should be noted that certain banks, but also the Hellenic Telecommunications Organisation (OTE) (and other public enterprises), are already implementing or plan to implement "voluntary early retirement" programmes, which will have a downward effect on employment.

Enterprises themselves appear to be less optimistic about the medium-term outlook for employment (see Chart III.22). The latest available data from the IOBE surveys (January 2005) show that employment is expected to fall in industry and construction. Only in retail trade and services is it the case that the percentage of firms forecasting a rise in employment exceeds (marginally) that of firms forecasting a decline (see Table III.10).

However, employment may develop more favourably, if account is taken of the positive effects which will stem from: the implementation of the recently taken economic policy measures (provisions included in the tax and development laws); the promotion of public-private partnerships; the fact that the aim is for a more effective absorption of CSF III funds; and the simplification of procedures for business start-ups in manufacturing.[70]

The emphasis put on the "personalised approach" for the unemployed, through the upgrading and enhancement of the capacity of the Employment Promotion Centres (KPAs), is expected to contribute to a decline in unemployment and a shortening of its duration.[71]

An overview of the Greek labour market shows that significant challenges remain, such as the low employment rate (59.2% in the first half of 2004) and high unemployment, in particular among the young and women. Dealing with these challenges requires both short-term policy measures such as those mentioned above (though businesses do not seem to have responded to them yet) and measures which will bear fruit over a longer time-horizon, such as a comprehensive treatment of the weaknesses of the educational system, which has already started. This comprehensive treatment is important, as it can contribute to both an increase in labour productivity and the better matching of labour supply and labour demand (along with

70 A relevant draft law was released in January this year.
71 The National Action Plan on Employment submitted to Parliament in autumn 2004 puts particular emphasis on those measures. Moreover, data from the Employment Observatory (Employment Observatory – Research & Information SA) for the March-November 2004 period indicate that the rate of registered unemployed persons who enjoyed a personalised approach increased during 2004.

the excess labour supply, there are indications[72] of labour market tightness with respect to certain top professionals). At any rate, the new tax law provides incentives to businesses to deal with the training requirements for their personnel; expenditure for personnel training can be deducted from the firms' gross income.[73]

5. Developments in the balance of payments in 2004 and the outlook for 2005

5.1 Current account balance

In the 2000-2003 period, the current account deficit (on the basis of the balance of payments statistics compiled by the Bank of Greece) widened to 6.2% of GDP on average, compared with 3.4% in the preceding five-year period (1995-1999). However, in 2004 the deficit narrowed appreciably, but remained relatively high (3.9% of GDP). As noted in previous Reports of the Bank of Greece, the high current account deficit observed in recent years may, to some extent, be considered normal in an economy in the process of convergence. From the standpoint of rational intertemporal allocation of resources, the widening of the current account deficit allows a country to fund increased investment —in the expectation of higher returns— or to smooth out consumption over time.[74] Indeed, total gross fixed capital formation rose from 22.7% of GDP in 1999 to 25.7% in 2003 and 2004. Furthermore, private investment increased from 19.2% of GDP in 1999[75] to 21.8% both in 2003[76] and 2004. In the same period, overall saving grew, but at a slower pace (from 16.8% of GDP in 1999 to 17.5% in 2003 and 18.5% in 2004), and was not enough to finance investment. Besides, the fact that the current account deficit widened in the 2000-2003 period and —despite its fall— remained relatively high in 2004 reflects (i) the different cyclical position of the Greek economy in relation to Greece's major EU trading partners; and (ii) structural weaknesses of the economy and competitiveness losses. Therefore, the current account position signals a need for further reforms aimed at increasing productivity and boosting competitiveness, as pointed out repeatedly.

In 2004 as a whole, the current account deficit reached €6,411 million, improving substantially (by €2,235 million) over 2003 (see Chart III.23 and Table 7 in the Statistical Appendix). This development is a result of: (i) mainly a large increase in the services surplus, notably shipping receipts; (ii) secondarily, a rise in the transfers surplus; and (iii) finally, a small decline in the income account deficit, which, taken together, more than offset the considerable widening of the trade deficit.

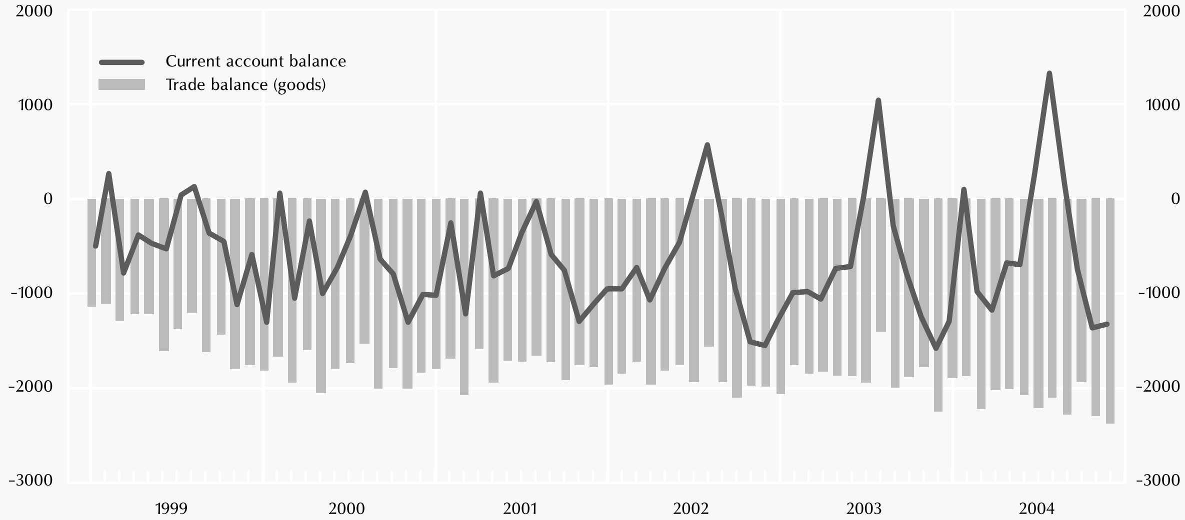
The relative stagnancy of goods imports in the 2001-2003 period (despite the fast growth of domestic economic activity), as shown by Bank of Greece data, gave way in 2004 to a considerable increase, which is partly attributable to the completion of facilities and infrastructure projects associated with the Olympic Games (as well as to goods imports in preparation for the Olympic Games, e.g. means of transport). This led to a widening of the non-oil trade deficit, as the large increase in the import bill more than offset the rise in export receipts in absolute terms. Thus, the growth of the non-oil trade deficit, in conjunction with the increase in the net oil import bill, pushed up the overall trade deficit.

72 See Federation of Greek Industries (SEB), *Survey on corporate needs for top professionals during the three-year period 2005-2007*, June 2004.
73 Law 3296/2004, Art. 9.
74 See M. Bussiere, M. Fratzscher and G.J. Mueller, "Current account dynamics in OECD and EU acceding countries – an intertemporal approach", ECB Working Papers, February 2004.
75 18.5% in the euro area.
76 17.2% in the euro area.

Chart III.23

Trade balance and current account balance (January 1999 - December 2004)

(Million euro)



Source: Bank of Greece.

The substantial widening of the services surplus is mainly accounted for by a large increase in net transport receipts, which stemmed from a rise in sea transport freight charges and in world sea trade volume. The spectacular increase in freight charges, which peaked in February 2004, continued in the fourth quarter of the year and came to a halt in December 2004. However, increased demand for sea transport of raw materials and semi-manufactured goods, fuelled by the recovery of the US economy and the strong growth rate of the Chinese economy, keeps freight charges high and is expected to remain buoyant. The current account balance was also affected favourably by a rise in the transfers surplus, mainly as a result of higher net EU transfers to general government.

Regarding the outlook for 2005, on the basis of estimated developments in domestic economic activity and the key aggregates of the world economy (see Chapter II and Section 3 of this chapter) which affect the current account balance of Greece, the current account deficit should remain virtually unchanged in nominal terms in 2005 and drop slightly as a percentage of GDP (to around 3.6-3.7%, compared with 3.9% in 2004).

Trade balance

Underlying the deterioration of the trade deficit in 2004 were a substantial increase in imports (for the reasons mentioned earlier) and a further decline in the price competitiveness of Greek products (which was influenced by a further rise in relative prices and the appreciation of the euro). Specifically, competitiveness dropped by around 6% in 2004, as measured by relative unit labour costs, and by almost 2%, as measured by relative consumer prices.

The trend in non-oil exports observed at the beginning of 2004 continued throughout the year. Specifically, non-oil export receipts showed a remarkable rise (of €1,276 or 13.0%) in comparison with 2003. *It should be pointed out, however, that this increase stems almost exclusively from sales (exports) of used ships as a part of a move towards commercial fleet renewal. Other export* *receipts rose minimally*, as a net result of two opposing effects: on the one hand the acceleration of the growth rate of world trade, which affected exports favourably, and, on the other hand, the deterioration of the price competitiveness of Greek exports, which had an almost equal unfavourable impact.[77] Besides, the non-oil import bill rose considerably (by €3,629 million or 12.8%), after remaining relatively stagnant in 2003.[78] The growth of imports had been expected, as already mentioned. These developments caused the non-oil trade deficit to widen by €2,353 million.

As regards the oil balance, the net oil import bill increased by €439 million owing to the steep rise in world crude oil prices. Thus, the overall trade deficit grew by €2,792 million or 12.3%.

According to Bank of Greece provisional data on the breakdown of non-oil exports and imports by product category (see Table III.11), 2004 saw an increase in export receipts from certain products —notably metallurgical products, means of transport (mainly used ships) and chemicals-plastics. By contrast, export receipts from agricultural products and machinery-appliances declined. On the import side, an increase was observed in the import bill for all the categories of products other than capital goods and consumer durables. Means of transport (comprising passenger cars and all other means of transport) had the largest contribution to the overall rise in the import bill.

Regarding the geographical breakdown of exports, according to the latest available disaggregated NSSG data for the first ten months of 2004 (see Table III.12), the proportion of exports to the EU-15 remained unchanged from 2003, while the share of exports to the new Member States declined. The proportion of exports to non-EU OECD countries also remained virtually unchanged, while the share of exports to the Commonwealth of Independent States narrowed. By contrast, a considerable increase is shown by exports to the Balkan, North Africa, Middle East and Asia countries. Changes are also observed in the geographical breakdown of imports. Specifically, the share of imports from the EU (notably the euro area), the Balkan, North Africa and Middle East countries, South-Eastern Asia and China rose, while the proportion of imports from the Commonwealth of Independent States declined.

Services balance

In 2004 the services surplus grew substantially (by 34.4%) over 2003, to reach €15,467 million. This rise is accounted for by a very large increase (of 63.1%) in net transport receipts (especially from sea transport), reflecting the high growth rate of world trade and the large increase in freight charges in the international market, which peaked at the beginning of 2004 and continued to be high in the next months.[79] The services surplus was also boosted by a €678 million (or 9.2%) rise in net travel receipts, which is largely attributable to the successful organ-

77 According to NSSG provisional data, non-oil export values were stagnant in the first eleven months of 2004 (actually, they declined slightly, by 0.2%) and there was a small increase (of 0.2%) in total goods exports. Taking into account the NSSG estimates for December 2004, total goods export values rose by 2.1% for 2004 as a whole. The discrepancies between the Bank of Greece and the NSSG trade statistics arise for many reasons, the chief one being that the former mainly relate to receipts and payments through the domestic banking system, while the latter are based on the one hand on customs data (for transactions with non-EU countries) and, on the other hand, on tax data (INTRASTAT) (for intra-EU transactions) and remain provisional for a long time.

78 According to NSSG, non-oil import values rose at an average annual rate of 13.3% in the first eleven months of 2004 (and total goods import values increased by 11.0%). Taking into account the NSSG estimates for December 2004, total goods import values rose by 9.7% for 2004 as a whole.

79 It should be noted that the average daily receipts of oil tankers, which had been $27,963 in 2001, $16,362 in 2002 and $29,351 in 2003, reached $44,012 in 2004. The corresponding figures for dry cargo vessels were $8,064 in 2001, $7,133 in 2002, $14,379 in 2003 and $27,661 in 2004.

Table III.11
Breakdown of Greece's non-oil external trade by product category

A. Export receipts

	Percentage share of each product category in total export receipts			Percentage change in export receipts	
	2002	2003	2004*	2003/2002	2004/2003*
Agricultural products	19.3	22.0	17.1	20.0	–12.3
Chemicals, plastics	11.0	12.4	11.6	19.3	5.7
Manufacturing (excluding metallurgy)	19.2	20.1	17.8	10.8	0.1
Metallurgy	8.6	7.9	9.7	–3.3	38.7
Machinery, appliances	5.4	7.3	5.5	42.2	–14.9
Means of transport	0.7	3.7	13.7	445.1	323.2
Ships	*0.4*	*3.0*	*12.4*	*702.7*	*369.8*
Unclassified goods[1]	35.8	26.6	24.6	–21.4	4.4
Total	100.0	100.0	100.0	5.6	13.0
Total (excl. ships)				*2.9*	*2.0*

B. Import bill

	Percentage share of each product category in total import bill			Percentage change in import bill	
	2002	2003	2004*	2003/2002	2004/2003*
Agricultural products	14.7	14.4	13.7	–2.6	7.7
Chemicals, plastics	16.7	15.8	14.2	–5.2	1.1
Manufacturing (excluding metallurgy)	21.9	21.9	20.7	0.1	6.3
Metallurgy	8.1	8.8	9.2	8.5	18.0
Machinery, appliances	21.4	21.2	19.3	–1.4	2.5
Consumer durables	3.5	3.6	3.2	1.7	–0.9
Capital goods	13.0	13.2	11.7	1.6	0.0
Computers	2.3	1.9	2.0	–16.1	15.9
Fixed-voice and mobile telephony	2.6	2.4	2.4	–7.6	10.6
Means of transport	12.8	15.0	18.4	16.7	38.1
Passenger cars	6.2	7.1	7.9	14.2	24.8
Other goods	0.4	0.3	0.4	–13.6	36.7
Unclassified goods[1]	4.0	2.5	4.2	–37.2	84.8
Total	100.0	100.0	100.0	–0.3	12.8

1 Products for which no code number has been reported.
* Provisional data.
Source: Bank of Greece.

isation of the Olympic Games in Greece. Finally, the "other" services deficit narrowed substantially (to €149 million, from €499 million in 2003).

Income account

The income account deficit declined slightly in 2004 over 2003 owing to an increase in interest, dividend and profit receipts, while the respective payments remained virtually unchanged. It should be noted that the income account deficit is explained by the fact that payments include interest payments on Greek government bonds, which weigh considerably on the balance, owing to the substantial funds invested in such securities by non-residents.

Table III.12
Breakdown of Greece's external trade by geographical area

A. Exports

	Percentage share in the value of total exports						Percentage change in the value of exports			
	2000	2001*	2002*	2003*	2003* Jan.-Oct.	2004* Jan.-Oct.	2001/00	2002/01	2003/02	2004/03
European Union (15)	47.3	42.0	43.5	46.7	48.1	48.1	–18.9	–3.3	16.4	–1.3
Euro area	38.5	32.3	35.2	37.8	38.6	38.2	–23.4	1.6	16.6	–2.5
New Member States	7.6	9.5	8.8	8.5	8.3	7.4	14.9	–13.5	4.4	–12.8
Other OECD countries[1]	13.8	12.9	12.3	14.3	13.8	13.7	–15.1	–10.6	25.9	–2.4
USA	5.4	5.5	5.3	6.6	6.1	5.3	–7.7	–9.3	33.1	–14.1
Balkan countries[2]	14.7	18.4	16.6	16.4	16.1	17.2	13.9	–15.6	6.9	5.2
Commonwealth of Independent States	3.2	4.3	4.3	3.5	3.2	2.9	22.2	–5.8	–10.5	–11.1
Northern Africa & Middle East countries[3]	6.8	6.7	7.1	5.5	5.2	6.4	–10.4	–1.2	–16.0	21.1
China & Southeastern Asia	1.5	1.9	2.1	1.6	1.5	1.8	15.4	4.9	–20.1	14.5
Other countries	5.1	4.5	5.2	3.6	3.7	2.6	–19.7	8.6	–25.1	–32.2
Total	100.0	100.0	100.0	100.0	100.0	100.0	–8.6	–6.7	8.5	–1.4

B. Imports

	Percentage share in the value of total imports						Percentage change in the value of imports			
	2000	2001*	2002*	2003*	2003* Jan.-Oct.	2004* Jan.-Oct.	2001/00	2002/01	2003/02	2004/03
European Union (15)	61.0	54.5	52.2	54.5	54.1	55.5	–21.6	–0.5	25.6	8.4
Euro area	52.0	47.3	46.3	48.3	47.8	53.2	–20.2	1.6	25.5	17.6
New Member States	1.8	2.0	2.0	1.8	1.8	1.9	–2.2	4.0	9.1	14.5
Other OECD countries[1]	13.9	13.8	17.9	18.9	19.0	16.2	–13.0	35.1	26.9	–9.9
USA	3.2	3.5	4.7	5.0	5.5	5.0	–5.3	40.3	28.2	–3.0
Balkan countries[2]	2.8	3.6	2.7	2.7	2.8	3.1	14.0	–21.2	17.7	17.2
Commonwealth of Independent States	4.2	6.8	9.3	7.3	7.3	5.9	44.2	42.5	–6.1	–13.7
Northern Africa & Middle East countries[3]	9.8	10.4	7.0	7.2	7.5	8.1	–6.3	–30.6	24.0	14.6
China & Southeastern Asia	4.0	5.2	5.0	4.7	4.7	5.2	12.7	1.0	12.4	16.8
Other countries	2.6	3.7	3.8	2.8	2.9	4.1	25.0	7.7	–11.3	48.2
Total	100.0	100.0	100.0	100.0	100.0	100.0	–12.3	3.9	20.1	5.7

1 The OECD Member States not included in any other category.
2 Albania, Bulgaria, Romania and former Yugoslavia countries (Bosnia, Croatia, FYROM and New Yugoslavia).
3 Greece's major trading partners in Northern Africa and the Middle East.
* Provisional data.
Source: NSSG.

Transfers balance

The transfers surplus grew by €927 million in 2004, to reach 6,015 million. This is almost exclusively accounted for by a considerable increase (of €1,169 or 21.7%) in general government receipts (mainly EU transfers), while general government payments (mainly to the EU) only rose by €117 million and the net payments of the "other" sectors (mainly emigrants' remittances) declined by €125 million.

Underlying the appreciable increase in net transfers to general government (mainly from the EU) in 2004 was an acceleration in the rate of absorption of resources from the Structural Funds under the Third Community Support Framework (CSF III),[80] taking into account that receipts (under the Common Agricultural Policy – CAP) from the Guarantees Section of the European Agricultural Guidance and Guarantee Fund (EAGGF) remained almost unchanged from 2003. A further increase in transfers is expected in the next months, as in December 2004 the European Commission approved the "interim review" of CSF III (2000-2006). At the same time, the necessary organisational and institutional improvements were implemented and steps were taken to simplify the relevant procedures, with a view to utilising the Community resources faster and more effectively.

5.2 Financial account

In 2004, financial investment, i.e. the sum of direct investment, portfolio investment and "other" investment, showed a net inflow of €5,223 million, compared with a net inflow of €5,255 million in 2003.[81] This reflects a net inflow of €13,727 million under portfolio investment (€12,334 million in 2003) and €600 million under direct investment (€545 million in 2003), which, however, were largely offset by a net outflow of €9,104 million under "other" investment (€7,624 in 2003).

Foreign investors' purchases of Greek government bonds continue to be the main source of the substantial net inflows under portfolio investment. Specifically, non-residents' investment in Greek bonds rose from €18.8 billion in 2003 to €21.6 billion in 2004. Besides, residents also made substantial investments (of €10.3 billion) in foreign bonds, which were higher than in 2003 (€8.3 billion). As already mentioned in the *Monetary Policy Interim Report*, October 2004, a considerable share of residents' investment in foreign bonds pertains to euro area bonds purchased by the Bank of Greece, which reduced its reserve assets by a corresponding amount. Considerable investments were also made by domestic credit institutions and private individuals.

Net inflows under direct investment reached €600 million in 2004, as non-residents' investment in Greece (€1,088 in 2004, up from €586 million in 2003) exceeded residents' investment abroad (€489 million in 2004, compared with €41 million in 2003). It should be pointed out that inflows for direct investment in Greece, albeit relatively low, recovered further in 2004, despite the declining path of foreign direct investment globally. The most important direct investments by non-residents in Greece were the following acquisitions: (i) of Panafon S.A. by Vodafone (which was partly effected in 2003 and completed in January and February 2004); (ii) of Geniki Bank by Société Générale (in March); (iii) of "Delta Singular Outsourcing Services" (a subsidiary of "Delta Singular Informatics") by the US company "First Data" (in July); and (iv) of "Kotsovolos S.A." by "Dixons" (in September). Finally, a substantial inflow is accounted for by the increase in the participation of ''Paneuropean Oil S.A." in the capital of ''Hellenic Petroleum S.A." (in August). Regarding residents' investment abroad, the most important developments were the acquisition of a mobile telephony company in Uzbekistan by "Germanos S.A." (in September) and the acquisition of the Bulgarian bank "UBB" by the National Bank of Greece (in July).

80 By end-December 2004, around 32% of the government expenditure resources under CSF III had been absorbed, which (expenditure), as is known, includes the total national and Community contribution (Ministry of Economy and Finance, January 2005).

81 The net inflow under financial investment, together with the change in reserve assets and errors and omissions, by definition fully covers the current account deficit. See Table 7 of the Statistical Appendix.

Under "other" investment, a net outflow of €9,104 million reflects a €6,216 increase in residents' foreign assets, as well as a €2,888 decrease in residents' foreign liabilities. The rise in assets in 2004 is exclusively accounted for by an increase in residents' (mainly credit institutions') investment in deposits and repos (€6.3 billion, compared with €4.1 billion in 2003), while the decline in liabilities was a result of outflows of €2.2 billion for loan repayment and —to a lesser extent— a €0.8 billion drop in non-residents' deposits and repos. It should be noted that 2003 had seen a €3.9 billion decline in liabilities out of loan repayment.

Finally, at end-2004, Greece's reserve assets came to €2.0 billion, compared with €4.6 billion at end-2003. It should be recalled that, since the first months of 2003, the Bank of Greece has started to diversify its portfolio, by reducing its non-euro area currency holdings, which are included in reserve assets, and by increasing its higher-yield (mainly euro-denominated assets) – most notably bonds issued by euro area Member States, which are not included in reserve assets (as already mentioned, the relevant investments are recorded under residents' portfolio investment). Given that there is less need to maintain high foreign currency reserves, by the above diversification the Bank of Greece has improved the return on its investments. As noted repeatedly, since Greece joined the euro area in January 2001, reserve assets, as defined by the European Central Bank, include only monetary gold, the reserve position in the IMF, special drawing rights, and Bank of Greece claims in foreign currency on residents of non-euro area countries. Conversely, reserve assets do not include claims in euro on residents of non-euro area countries, claims in foreign currency and in euro on residents of euro area countries, and the Bank of Greece participation in the capital and the reserve assets of the ECB.

Appendix to Chapter III

Structural reforms and competition in product markets

1. Introduction

The Bank of Greece and international organisations (OECD, IMF, European Commission) have repeatedly stressed the need to promote competition in product markets in Greece.[1] The lack of competition is evidenced, *inter alia*, by: (a) the extent of regulations in the economy and the constrained competition in some branches of economic activity, (b) the limited liberalisation of utilities and (c) the extent of agreements and harmonised practices between companies.

2. Regulatory environment

The OECD, the World Bank and independent researchers have —on the basis of both objective measures and subjective evaluations derived from opinion surveys— constructed indicators to measure the pervasiveness of regulations in a number of developed economies. According to the OECD evaluation (see Table III.A1), Ireland has the least regulated environment in the euro area, as the economic and administrative regulations governing its economy are limited, there are only a few barriers to entrepreneurship, and the economy is outward-looking. According to the OECD, Greece is among those countries that —despite having made considerable progress in improving the business environment in the period 1998-2003— are characterised, together with France and Italy, by the most restrictive product market regulations, mainly due to the pervasiveness of state controls, the nature and extent of economic regulations (e.g. price controls, use of command and control regulations etc.) and red tape.

In 2001, the OECD stressed the need to reform and modernise the regulatory environment in Greece to make it market-friendly and pro-competitive.[2] According to the OECD, the reform process should include the evaluation and codification of laws to combat regulatory inflation with a view to increasing transparency and reducing uncertainty.

The Ministry of Development acknowledges the need to simplify bureaucratic procedures. To this effect, on 25 January 2005 and following public consultation it presented a bill on simplifying licensing procedures for manufacturing enterprises. The bill provides for, *inter alia*, a faster issuance of licences for the establishment and operation of manufacturing enterprises, the prolongation of the validity of existing licences and the exemption of handicraft firms from the need to obtain a licence.[3] Furthermore, the Ministry of the Interior, Public Administration and Decentralisation announced that it will proceed to the further reduction of red tape (e.g. by simplifying the procedures necessary for signature validation).

3. Limited deregulation of utilities

The acknowledgment of the shortcomings that arise from the involvement of the State in the production process, in conjunction with technological developments and the need to comply with EU directives, have contributed to the gradual modernisation of utilities in Greece over the last decade. The significance of utilities for an economy cannot be overstated; their output is an input to all economic sectors.

The modernisation of public enterprises in Greece included the adoption of financial criteria in their operation (e.g. through Law 2414/1996), the partial privatisa-

1 See e.g. P. Mylonas and G. Papaconstantinou, "Product Market Reform in Greece: Policy Priorities and Prospects" in Bank of Greece and The Brookings Institution *Greece's Economic Performance and Prospects* (2002), as well as the recent study by I. Mergos and N. Magginas "Tackling structural rigidities is necessary to maintain high growth rates", published in the Bulletin of the National Bank of Greece *Greece-Economic and Market Analysis* (November 2004-January 2005).
2 OECD, *Regulatory Reform in Greece*, 2001.
3 Law 2941/2001 simplified the licencing procedures for the establishment of sociétés anonymes.

Table III.A1: Extent of product market regulation in euro area Member States

Country	Overall indicator (1)	State control (2)	Barriers: Entrepreneur-ship (3)	Barriers: Trade and investment (4)	Economic regulation (5)	Administrative regulation (6)
Ireland	1.1	2.0	0.9	0.5	1.5	1.1
Finland	1.3	2.3	1.1	0.6	1.9	1.3
Austria	1.4	1.9	1.6	0.7	1.5	1.9
Belgium	1.4	2.4	1.6	0.3	1.8	1.9
Germany	1.4	2.2	1.6	0.6	1.8	1.9
Netherlands	1.4	1.9	1.6	0.7	1.6	1.9
Spain	1.6	2.7	1.6	0.7	2.1	2.0
Portugal	1.6	2.7	1.3	0.8	2.2	1.5
France	1.7	2.7	1.6	1.0	2.3	1.6
Greece	*1.8*[1]	*2.8*	*1.6*	*1.2*	*2.2*	*1.9*
Italy	1.9	3.2	1.4	1.1	2.6	1.6

1 According to OECD estimates, the value of the overall indicator of product market regulation was 2.8 in 1998, suggesting an improvement in the regulatory environment between 1998 and 2003.
Note: The overall indicator presented in the first column is a composite of the indicators presented in the next three columns (2-4). The regulations taken into consideration in the construction of the indicators presented in columns 2-4 can also be divided into economic and administrative regulations; the values of the relevant indicators are presented in the last two columns of the table. All indicators range from 0 to 6, reflecting increasing restrictiveness of regulatory provisions for competition. The data refer to the situation in 2003.
Source: OECD (2005), "Product Market Regulation in OECD Countries: 1998 to 2003", Working Paper No. 419 (P. Conway, V. Janod, G. Nicoletti).

tion of some enterprises (e.g. Public Power Corporation, Hellenic Telecommunications Organisation, Athens Water Supply and Sewerage company), the curtailment of the exclusive rights of others (e.g. Hellenic Post) and the deregulation, gradual or complete, of the sectors in which these companies belong. Despite the progress already made, there is still room for further improvement, since on the one hand not all EU directives have been transposed into national law and on the other hand some markets are not yet open to competition.

More specifically the following main shortcomings are observed in the sectors of electricity, telecommunications and postal services:

Electricity

Although the Greek electricity market was liberalised in February 2001, in effect it remains controlled by the Public Power Corporation (DEH). The shortcomings of the institutional framework[4] governing this market seem to be the main reason for the lack of competition.

While the basic law on the deregulation of the electricity market (Law 2773/1999) gave industrial and commercial consumers[5] the option of concluding supply contracts with producers/suppliers other than DEH and although a number of enterprises were accordingly licensed, no progress was made in the implementation of investment projects. The reason is that both the Regulatory Authority for Energy (RAE)[6] as well as the prospective investors and the banks called upon to finance the construction of the new plants thought that

4 The operating framework of the electricity market was initially set by Law 2773/1999, which had been based on Directive 1996/92/EC on the development of the single internal energy market. It was subsequently amended by Law 3175/2003, which partly meets the requirements of the new relevant EC Directive (2003/54).
5 Those consuming over 100 GWh per annum. They make up 34% of the overall market.
6 According to RAE's *Report* for January 2003-March 2004, the main obstacles to competition have to do with shortcomings of Law 2773/1999 and can be summarised as follows: (i) absence of an organised market and other mechanisms that would have enabled better business risk management, (ii) poor regulation and supervision of the market, which added to business uncertainty, (iii) failure to unbundle production and supply, (iv) limited right to select a supplier and (v) the non-liberalisation of the natural gas market.

Table III.A2: Licences granted to the private sector for the generation of electricity from thermal power stations and for electricity supply (February 2001-November 2004)

	Number of licences	Power in MW
Generation	11	4,095
Supply	9	2,343

Source: Regulatory Authority for Energy (RAE).

the existing institutional framework was inadequate, given that DEH retained the lion's share[7] of the market. The need to address this issue led to the enactment of Law 3175/2003, which brought about considerable changes in the operation of the electricity market[8] and gave additional motivation to suppliers, by allowing both those not owning production capacity to enter the market, as well as the resale of energy among suppliers. Moreover, the law increased the percentage of consumers who are free to purchase electricity from a supplier of their choice to 65% of the market, by including therein (as of 1 July 2004) all non-household consumers and provided that the market would be fully liberalised on 1 July 2007. The provisions of the new law were welcomed as a "positive step" by the parties concerned, but have actually remained ineffective, pending the approval[9] by the Ministry of Development of the new Power Exchange Code (PEC), which sets the first integrated framework for the operation of the new market. This should be followed by the start-up of investment projects for the construction of plants that have already received authorisation[10] and by a tender[11] for the integration of a capacity of 900MW into the system. In view of the acute problem of electricity supply in 2005 and 2006, the Ministry of Development has placed at the heart of its policy, *inter alia* the improvement of the electricity generation, transmission and distribution system in 2005 and the taking of measures to save energy and reduce consumption.

As for the deregulation of the electricity market, the Ministry of Development priorities are the approval of PEC and the fuller alignment of the legal framework with the provisions of Directive 2003/54/EC,[12] which have not been adequately, if at all, transposed into Greek law.

7 Although DEH operates as a société anonyme as of January 2001, it retains ownership of the electricity transmission system and remains responsible for the operation of the distribution system (low and medium-voltage customers). Moreover, about 65% of its output is generated using lignite, which is available to it free of charge, unlike natural gas which is used by private producers.

8 More specifically, Article 23, Section C, of Law 3175/2003 (i) establishes a mandatory daily market for the trade of electricity generated by the new private producers; the latter are not compelled to have concluded contracts with suppliers or end-consumers before entering the daily market; (ii) introduces a tendering procedure for the awarding (by HTSO) of capacity availability contracts in order to secure sufficient long-term capacity and reserves. (It should be recalled that the Hellenic Transmission System Operator —HTSO/DESMIE— is a société anonyme established by Presidential Decree 328/2000; pursuant to Law 2773/1999, HTSO has the responsibility of operating the electricity transmission system. Its role was further enhanced by Law 3175/2003, which confers upon it the task of operating the daily market.) Producers having concluded capacity availability contracts with HTSO are bound to guarantee the availability of a given amount of electricity from the new generation plants for a specified period of time in the future. In the first application of this arrangement, HTSO invited tenders for the integration into the system of a total capacity of 1,300 MW (900 MW initially, with a possibility of adding a further 400 MW by 1 July 2007). It should be noted that this measure only applies to private producers, as DEH is barred from tender participation.

9 This is expected to happen soon (the final draft was made public by RAE in September 2004).

10 A Hellenic Petroleum's plant (with a total generating capacity of 390 MW) is at the construction stage and is scheduled to start operating (initially at half capacity) in 2005. Moreover, following an HTSO tender for additional electricity reserves, a 160 MW gas-fired turbine was constructed and has been operating since summer 2004. Also, three other power plants (total generating capacity: 1200 MW) will possibly be integrated into the system in 2007. RAE's *Report* for January 2003-March 2004 states that this capacity should rather be integrated into the system in 2005, so as, along with a further 800 MW to be added between 2005 and 2008, to make it possible for Greece to obtain sufficient capacity and reserves by 2008.

11 Launched by HTSO.

12 It should be recalled that Member States ought to have completed alignment with this Directive by 1 July 2004.

Table III.A3: Indicators of market penetration by providers other than OTE in the fixed-voice and mobile telephony, 2003

	Market shares of alternative providers (%)*	Number of licensed providers	Number of licensed providers (OTE excluded) for development of fixed network
Fixed-voice telephony	9.3 / 15.8 / 24.2	13	2
Mobile telephony	59	4	**

Notes: *For fixed-voice telephony, the figures refer to the market shares of alternative providers in local, long-distance and international calls respectively.
** The supply of the mobile telephony services has been based on the development of new infrastructure networks.
Source: European Commission (see footnote 22) and EETT (2003) *Annual Report*.

Telecommunications

The deregulation of the telecommunications market and the strengthening of competition in terms of both prices and services, particularly in the sector of mobile telephony, have contributed to a drastic reduction in the prices of telecommunication services[13] and, therefore, to a weakening of inflationary pressures.

Specifically, the Greek mobile telephony market is characterised by competitive conditions,[14] high level of development,[15] considerable private investments and technologically upgraded services,[16] while it helps increase employment[17] and business turnover in the market for mobile telephone sets.[18]

As regards the fixed telephony market, the entry of companies competing against the public enterprise that formerly operated as a state monopoly had positive effects both on prices[19] and on services.[20] Nevertheless, the fixed telephony market is still far from competitive, as indicated by the market share[21] based on retail sales revenue (see Table III.A3). The delay seen in the deregulation of the fixed telephony market influences, among other things, the development of the market for broadband networks,[22] with a considerable impact on the use of the Internet and on the expansion of electronic trade and the digital content market. If this lag persists, the economy as a whole and telecommunication companies in particular will have to bear an additional technological "opportunity cost". A greater effort will therefore be necessary to reduce the "digital distance" between Greece and the advanced economies.

13 The telephony services sub-index of the HICP fell by 15.6% between January 2002 and December 2004.
14 The existence of competition is evidenced by the changes in market shares, the fact that none of the four operators occupies a dominant position (as the largest one holds a share of 41%) and the business strategies of the operators.
15 The mobile telephony penetration rate exceeds 90% of the total population.
16 As indicated by the commercial use of advanced data transmission services.
17 According to a survey conducted by ALBA students on behalf of a mobile telephony company, the total number of employees in the mobile telephony sector exceeded 28,000 in 2003 (*Imerisia*, 20 November 2004, special edition).
18 It is estimated (according to a relevant study by Stat Bank, *Imerisia*, 4-5 December 2004) that 2.5 million mobile telephones were sold in 2004, worth roughly €350 million.
19 The prices of fixed telephony services affect to a large extent the price index of telephony services, because fixed telephony costs account for 72% of total telephony service costs.
20 Under pressure from its competitors (among other factors), OTE has provided subscribers with a number of digital services (caller ID, three-party conference call, voice mail etc.), as well as alternative options of call debit in relation to user profile, the country called, the time and the day of the call etc. There is evidence that the development of a competitive mobile telephony market has contributed to the emergence of a much more demanding telecom services user and consequently has upgraded commercial practices and, in some cases, the technical specifications of fixed telephony operators, while it has shortened the time of operator response.
21 Even if we take into account that, during 2004, the market shares of the alternative fixed telephony operators increased or that the market share of OTE in long-distance and international calls is considerably lower than in local calls, the situation does not change significantly.
22 According to a Communication from the European Commission entitled "European Electronic Communications Regulation and Markets 2004" (COM(2004) 759, 2 Dec. 2004), the broadband penetration rate does not exceed 0.24% of the total population compared with an average of 7.6% in the EU-15.

Table III.A4: Number of licensed postal operators and employment therein

	1999	2000	2001	2002	2003	2004
Operators	152	174	224	262	295	266
Number of employees	19,373	20,407	21,027	20,706	21,065	. . .

Sources: EETT (2004) Greek express delivery market (Table 4.1), EETT website (www.eett.gr) and National Statistical Service of Greece, National Accounts, 1999-2003.

Table III.A5: ELTA transit time performance and targets for domestic mail

	2002 (1st half)	2003 (1st half)	2004 (1st half)	ELTA target for 2004
Percentage of items delivered one and three days after posting day (T)				
T+1	48.7	58.8	66.1	85.0
T+3	90.9	94.9	95.6	95.0
Average delivery time in working days				
	1.9	1.6	1.5	–

Sources: EETT announcement on the quality of the USP service and Annex I of Ministerial Decision 79293 (Government Gazette B 1588/29 December 2000).

The National Telecommunications and Post Commission (EETT),[23] an independent regulatory authority, is making strong efforts to establish sound competitive conditions in telecommunication markets. The Commission's interventions, however, are hampered by the fact that Greece has failed so far to adjust national law to the European Union's new regulatory framework[24] for telecommunications.[25] Regarding the promotion of competitive conditions, an important matter is the creation of an environment that will encourage private entrepreneurship, so that the protection of new investments against a variety of risks will not have inhibitory effects. It will thus be possible to offer new and higher-quality services to meet demand.

Postal services

The postal market is a further example of a sector in which the deregulation of one segment of the market —the express delivery services— has led to both an increase in the number of firms active in the market (see Table III. A4) and an intensification of competition. In the remaining segments of the postal market, however, competition is still limited, since, apart from the Hellenic Post (ELTA), only two companies are currently authorised to operate within the "universal service" remit.[26] The scope of services reserved for ELTA has been gradually restricted and ELTA now retains, under certain conditions,

23 Under Law 2867/2000, EETT applies competition laws in the telecommunications market and arbitrates for the settlement of disputes in the respective markets (telecommunication services providers, public sector organisations and users).
24 Includes Directives about access, licensing procedure, universal services and competition.
25 The European Commission has already referred Greece (and four other countries) to the European Court of Justice in connection with this matter.
26 The "universal postal service" includes the following minimum facilities: the clearance, sorting, transport and distribution of postal items up to 2 kilograms; the clearance, sorting, transport and distribution of postal packages up to 20 kilograms as well as the services for registered and insured items. These services cover both national and cross-border services. A detailed account of these services is provided in Law 2668/1998. ELTA has been designated as Universal Service Provider (USP) and is required to permanently provide postal services of specified quality and at affordable prices to all users of postal services in Greece. Furthermore, certain services have been reserved for ELTA as the USP. Reserved services are limited to the clearance, sorting, transport and delivery of items (up to 100 grams) of domestic and cross-border mail, provided that certain conditions pertaining to the transportation charge for the service are met. The services reserved for the USP are detailed in Law 3185/2003. Two companies are currently authorised to operate within the provision of the universal postal service remit, excluding those services reserved for ELTA.

Table III.A6: Percentage of items delivered one day after posting, 2003 (%)

Greece	Italy	Portugal
62.9	87.0	91.6

Note: The percentage for Greece refers to the whole of 2003 and thus differs from that presented in Table III.A5, which refers only to the first half of the year.
Source: WIK-Consult (2004), "Main developments in the European Postal Sector", Appendix C, Table 40.

a monopoly only in the delivery of mail weighing less than 100 grams. EU Directive 39/2002 provides for a further restriction of reserved services from 2006 onwards.

In anticipation of this further deregulation, ELTA is being modernised and is improving its services. However, despite the quality improvement that has taken place in the last few years, certain quality indicators lag behind both the targets initially set (see Table III.A5) and the respective indicators for other European Union (EU) countries (see Table III.A6). This deviation in performance may be the reason for the relatively limited, compared to other EU countries, use of postal services in Greece.[27]

4. Agreements and harmonised practices between companies

In its latest *Selected Issues* paper on Greece, the IMF states that product markets in Greece are not sufficiently competitive and that the efforts to enhance the operation of the Hellenic Competition Commission (EA) have been obstructed by difficulties in hiring qualified personnel and by the limited number of investigations initiated by EA itself.[28] According to the OECD, the lack of competition can also be deduced from the existence of agreements between companies on prices and shop-opening hours.[29]

EA is accused of devoting most of its resources to reviewing merger and acquisition applications[30] rather than investigating day-to-day issues, such as prices and shop-opening hours.[31]

Indicative of the limited role of EA is the fact that, in a number of instances, agreements between firms or the abuse of a dominant position went on unimpeded for a while before the EA's intervention.[32]

27 The importance of the quality of services for the development of the postal market is also emphasised by the National Regulatory Authority, i.e. the National Telecommunications and Post Commission (EETT), in its decision 187/9 October 2000 modifying the proposal of the Ministry of Transport and Communications regarding quality standards and their monitoring: "The quality of the services provided is one of the most important factors in the development of the USP and the market as a whole". The intensity of the use of postal services, measured either through the *per capita* domestic letter volume or the domestic letter volume per €1,000 of GDP, is lower than in other European Union countries, even those of Southern Europe. In 2002 the *per capita* volume of domestic letters was 47.0 in Greece, compared with 103.3 in Italy, while the volume of domestic letter post per €1,000 of GDP was 3.5 in Greece compared with 4.7 in Italy.

28 IMF, *Greece-Selected Issues*, February 2005.

29 The government support to the "Gentlemen's agreement" between firms to restrain price increases during the period that preceded Greece's entry into the euro area is considered as an example of government intervention and harmonised practice. OECD, *Economic surveys-Greece*, 2002, p. 157.

30 Review of merger cases according to Article 4b of Law 703/1977.

31 More than half of the decisions of EA in the period 2000-2004 concerned reviews of merger applications, i.e. possible violations of Article 4b of Law 703/1977. According to the Deputy Minister of Development (Interview to *Oikonomikos Taxydromos* on 26 May 2004), EA had until recently around 300 pending cases, most of which pertained to day-to-day issues.

32 Certain indicative examples that concern cases of abuse of dominant positions or horizontal agreements and had an impact on a large number of consumers are the following: (a) The abuse for 8 years by a soft-drink manufacturer of its dominant position through unjustified discriminatory behaviour towards its non-exclusive dealers as well as through offers to certain wholesellers in order to achieve certain sales targets. EA decided that these offers could not be justified on the basis of economies of scale and were putting pressure on wholesellers to sell solely the products of this company (EA decision 207/III/2002/25 January 2002). (b) The horizontal agreement of three airline companies to proceed simultaneously to an increase in their tariffs and a reduction in the commissions paid to travel agents. The complaint was made by travel agent associations and around 20 months later the EA decided (EA decision 249/III/2003) that this was indeed a case of agreement, asked for it to stop and announced that there would be a fine in case the violation continued or were repeated. (c) The complaint by a chain store against the harmonised pricing behaviour followed by an industrial branch (EA decision 206/III/2002). (d) Prompted by the increase in food prices in the last few years and following complaints about concerted behaviour, EA has been investigating since autumn 2004 the existence or otherwise of agreements between certain chain stores and their suppliers to hinder sales below cost by other competitor chain stores.

The government, acknowledging the need for better supervision of competitive conditions in the market, made public in November 2004 a new bill, which is aimed at modernising EA and enhancing its role.[33] The new bill provides for:

— The upgrading of EA as an institution, by assigning more responsibilities and monitoring powers to it. The Chairman of EA will be selected by the Cabinet and not, as up to now, by the Minister of Development and his/her appointment will take place following a hearing by the Special Parliamentary Committee on Institutions and Transparency.

— The adaptation of Greek law to Council Regulation (EC) No. 1/2003/16 December 2002 ("on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty").

— The reinstatement of Article 2a of Law 703/1977, which had been repealed by Law 2837/2000. Article 2a prohibits the abuse of economic dependence. It gives the opportunity to small firms with a relationship of "economic dependence" to another firm to appeal to EA in case of abuse (e.g. imposition of arbitrary trading terms, exercise of discriminatory behaviour, sudden and unjustified termination of long-term contracts). Until recently, in such instances small enterprises had to rely on a judicial process, which turned out to be very time-consuming.

— The speeding up of the review process.

— The systematic recording of the structure of all markets, which will enhance prudential supervision and permit intervention in time to prevent the abuse of dominant positions and the distortion of market competition.

33 "Amendment and supplementation of Law 703/1977 "on control of monopolies and oligopolies and the protection of free competition" as currently in force".

IV. Money, credit and capital markets in Greece

1. Monetary developments in Greece

After mid-2004, the annual growth rate of the Greek contribution to euro area M3[1] (excluding currency in circulation) gradually accelerated, as did the corresponding rate for the euro area. However, throughout 2004 this growth rate was higher in Greece than in the euro area. These developments reflect the historically low level of interest rates (and thus the relatively low opportunity cost of holding money), the faster growth of nominal GDP in Greece compared with the euro area, as well as the different rates of substitution of assets not included in M3 with M3 assets. At the same time, credit expansion also accelerated considerably in Greece, as central government borrowing requirements were much higher in 2004 than in 2003.

The composition of M3 changed in the course of 2004. Specifically, the growth rate of short-term (overnight) deposits strengthened considerably, while the rate of increase in time deposits with an agreed maturity of up to two years fell substantially. An even greater drop was recorded in the rate of change in investment in money market fund shares/units (which turned from positive to negative in the last quarter of the year), while the rate of decline in investment in repos weakened considerably.

In more detail, the annual growth rate of the deposits that, according to the definition of the ECB, are included in M3 remained relatively stable

1 The Greek M3, as well as that of any other euro area country (see the Glossary for the definitions of monetary aggregates), can no longer be calculated accurately, as quantities of euro banknotes and coins put in circulation by one euro area country may be held by residents of other euro area countries (and/or residents of third countries). Therefore, due to the technical problems with the calculation of currency in circulation in each euro area country, developments are discussed with respect not to the Greek M3 but only to its key components (excluding currency in circulation).

T a b l e I V.1

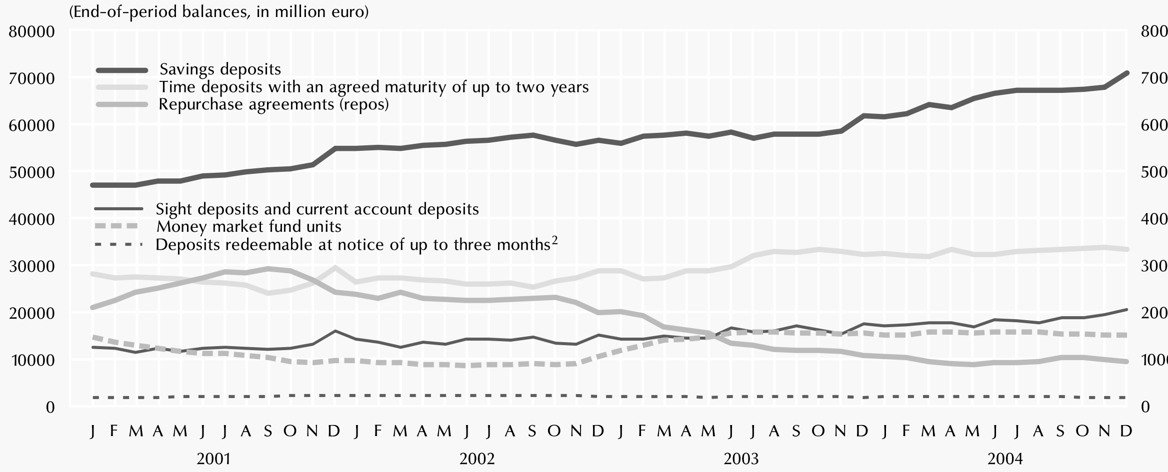
Greek contribution to the key monetary aggregates of the euro area

(Not seasonally adjusted data)

	Outstanding balances on 31.12.04 (million euro)	Annual percentage changes[1]							
		2001	2002	2003	2004				
		Q4[2]	Q4[2]	Q4[2]	Q1[2]	Q2[2]	Q3[2]	Q4[2]	December[3]
1. Overnight deposits	91,695	11.1	8.9	6.8	11.7	13.4	15.5	16.8	15.5
1.1 Sight deposits and current account deposits	20,697	5.3	5.7	17.7	19.3	18.0	11.8	19.1	17.8
1.2 Savings deposits	70,998	12.5	9.8	4.1	9.7	12.2	16.5	16.1	14.7
2. Time deposits with an agreed maturity of up to 2 years	33,408	–9.3	10.1	29.3	19.9	14.8	5.1	5.3	6.0
3. Deposits redeemable at notice of up to 3 months[4]	1,939	19.7	8.1	1.5	2.8	1.6	3.9	2.8	0.3
4. Total deposits (1+2+3)	**127,042**	**5.1**	**9.3**	**12.2**	**13.4**	**13.1**	**11.8**	**12.6**	**11.8**
5. Repurchase agreements (repos)	9,529	38.3	–19.0	–47.7	–45.9	–41.3	–23.8	–12.6	–12.1
6. Money market fund units	15,227	–38.4	–3.7	68.0	24.6	7.5	0.1	–1.9	–2.9
7. Bank bonds with a maturity of up to 2 years[5]	466	. . .	. . .	. . .	. . .	. . .	. . .	. . .	. . .

1 Annual rates of change in the corresponding index, which is compiled on the basis of outstanding stocks for December 2001 and cumulative monthly flows, adjusted for exchange rate variations, reclassifications etc.
2 The quarterly average is derived from monthly averages (which are calculated as arithmetic means of two successive end-of-month figures) and is not the three-month average of end-of-month annual growth rates (see the "Technical Notes" in the ECB *Monthly Bulletin*).
3 Annual rates of change on the basis of the corresponding index at the end of the month.
4 Including savings deposits in currencies other than the euro.
5 Rates of change are not shown because, owing to the low calculation base, they are very high.
Sources: Bank of Greece and ECB.

Chart IV.1
Deposits, repurchase agreements and money market fund units in Greece[1] (January 2001 - December 2004)
(End-of-period balances, in million euro)



1 These aggregates concern deposits, repos and money market fund units which, according to the ECB definition, are included in M3 and therefore constitute the Greek contribution to the corresponding euro area aggregates.
2 Including savings deposits in currencies other than the euro.
Source: Bank of Greece.

(fourth quarter of 2004: 12.6%, fourth quarter of 2003: 12.2%, see Table IV.1). Indicatively, the growth rate of savings deposits (which account for the largest part of overnight deposits)[2] accelerated considerably in the previous year (fourth quarter of 2004: 16.1%, fourth quarter of 2003: 4.1%). The fast growth of savings deposits is associated with the continuing decline in repos, as well as with a fall in government paper yields in 2004, i.e. with developments that boosted demand for more liquid assets, while the interest rate on savings deposits increased slightly (by 8 basis points). As mentioned above, a factor that contributed to these developments in savings deposits was the relatively low opportunity cost of holding money, which turned savers towards more liquid deposits. The same factor also led to a considerable deceleration in the annual growth rate of time deposits with an agreed maturity of up to two years in 2004 (fourth quarter of 2004: 5.3%, fourth quarter of 2003: 29.3%).

Among the other main components of M3, placements in repos dropped further in 2004 (see Chart IV.1), although their annual rate of decline slowed down significantly (fourth quarter of 2004: –12.7%, third quarter of 2004: –23.8%, fourth quarter of 2003: –47.7%). Apart from the taxation of repo yields,[3] this development is also associated with the extensive restructuring of credit institution portfolios (in the form of reduced holdings of Greek government securities and correspondingly increased loans to the private sector, which bring higher interest income). Finally, holdings of money market fund shares/units decreased in the last four months of 2004, so that their strong positive growth rate gradually turned negative (fourth quarter of 2004:

2 Savings deposits (as already mentioned in previous Bank of Greece *Annual Reports* and *Monetary Policy Reports*) are broadly similar to current account deposits, since they are redeemable on demand (without penalty) and enable depositors to effect payments to third parties (e.g. standing payment orders and fund transfers through cards). Thus, they are included in overnight deposits along with sight deposits and current account deposits.
3 It should be noted that in January 2005 the tax rate on repo yields (such taxation was imposed anew in January 2002) was raised from 7.5% to 10%, while the tax rate on deposit yields was cut from 15% to 10% as the tax rate on interest income from deposits and repos was equalised with the one applicable on bond interest income (see Introductory Report on the 2005 Budget).

–1.9%, fourth quarter of 2003: 68.0%). This development is associated with a drop in bond yields (which represent a sizeable share of money market mutual fund portfolios), while the interest rate on savings deposits increased slightly in 2004 as mentioned above. It should also be noted that the periods in which households and enterprises choose to invest in money market fund shares/units are usually those of relatively high uncertainty, mainly in the stock markets. Therefore, the deceleration in the growth rate of these mutual funds implies a somewhat reduced uncertainty and a gradual normalisation of savers' investment patterns.

2. Credit expansion

The annual growth rate of credit extended by Monetary Financial Institutions (MFIs) to the whole economy strengthened considerably in the course of 2004 (fourth quarter of 2004: 8.6%, fourth quarter of 2003: 3.2%). This acceleration reflects developments in the outstanding balance of domestic MFI credit to general government,[4] which continued to decrease, albeit at a much slower pace than in the previous year (–5.6% in the fourth quarter of 2004, compared with –15.9% in the fourth quarter of 2003). It should be noted, on the one hand, that this development reflects the continued decline in MFI holdings of Greek government paper and, on the other hand, that capital inflows from abroad for investments in government paper were significantly higher than the central government net borrowing requirement, which increased in 2004 (2004: €15,605 million, 2003: €10,526 million). By contrast, credit expansion to enterprises and households declined slightly, remaining nonetheless at a relatively high level (fourth quarter of 2004: 16.1%, fourth quarter of 2003: 17.1%, see Table IV.2).[5]

Bank lending to enterprises and households

The annual rate of increase in outstanding bank loans to enterprises decelerated in the course of 2004 (fourth quarter of 2004: 8.6%, fourth quarter of 2003: 11.0%). This development is associated with the increased issuance of corporate bonds since the last quarter of 2003. These bond issues have been absorbed by credit institutions (see the Appendix to this Chapter). Thus, the sum total of MFI claims on enterprises (loans and bonds) increased at an annual rate of 12.3% in December 2004, compared with 13.9% in December 2003, i.e. at a rate which remains well above nominal GDP growth (around 8%).

According to data that have become available since September 2002, the average monthly level of new loans to non-financial corporations[6] rose by 21% in 2004, compared with 2003. Almost all new loans concern loans with a floating interest rate or an initial rate fixation of up to one year, while more than 60% of new loans are large loans, i.e. over €1 million.

In 2004, credit expansion to trade and agriculture accelerated significantly, while it decelerated for industry, the "other" sectors (mainly construction firms) and tourism – even though the rate of credit expansion to tourist enterprises remains high (see Table IV.3).

In particular, the annual growth rate of loans to industry followed a downward course in 2004

4 Domestic MFI financing to general government comprises loans to government and total government paper held by the central bank, credit institutions and money market funds.
5 During 2004, credit expansion to the private sector in the euro area accelerated, though it stood at far lower levels than in Greece (December 2004: 7.0%, December 2003: 5.5%).
6 New loans comprise only loans of a specific amount and with a defined maturity and not credit lines or debit balances on current accounts, which represent one-third of total loans to non-financial corporations.

Table IV.2
Total credit expansion in Greece
(Annual percentage changes)

	2001	2002	2003	2004				
	Q4[1]	Q4[1]	Q4[1]	Q1[1]	Q2[1]	Q3[1]	Q4[1]	December[2]
1. Total credit expansion	8.9	7.1	3.2	3.8	8.6	9.3	8.6	7.7
2. Credit expansion to general government	–2.4	–5.2	–15.9	–15.5	–6.2	–2.8	–5.6	–8.0
3. Credit expansion to enterprises and households	23.2	18.3	17.1	16.9	17.4	15.7	16.1	15.8
3.1. Credit expansion to enterprises	16.7	11.4	11.0	10.9	10.5	8.2	8.6	7.5
3.2. Credit expansion to households	40.0	33.1	28.2	27.5	28.9	28.2	28.0	28.5
3.2.1 Housing loans	36.7	35.4	27.1	24.5	24.7	22.9	23.8	24.8
3.2.2 Consumer loans	44.3	27.4	24.8	29.2	34.5	38.2	37.9	37.4

1 The quarterly average is derived from monthly averages (which are calculated as arithmetic means of two successive end-of-month figures) and is not the three-month average of end-of-month annual growth rates (see the "Technical Notes" in the ECB *Monthly Bulletin*).
2 Annual rate of change at the end of the month.
Source: Bank of Greece.

(fourth quarter of 2004: 1.1%, fourth quarter of 2003: 10.4%). This deceleration is partly attributable to the increased funding of industrial firms through alternative sources of financing, particularly through corporate bond issuance but also through the Athex in the form of share capital increases.[7] Taking into account the additional — compared with the previous year— funds raised through these alternative sources of financing, the rate of credit expansion in December stood at 1.4% (compared with –1.2% if these funds are not taken into account).

A notable slowdown was recorded in credit expansion to the "other" sectors (fourth quarter of 2004: 11.7%, fourth quarter of 2003: 26.5%) and, to a lesser extent, to tourism (fourth quarter of 2004: 17.6%, fourth quarter of 2003: 24.4%). These developments are associated with the decrease in the borrowing requirements of construction companies (which are included in the "other" sectors) and tourist enterprises, following completion of investment projects related to the Olympic Games. Moreover, construction companies and tourist enterprises had a significant recourse to bond issuance (€329 million), while the capital they raised through the Athex increased (2004: €87 million, 2003: €8 million). Taking into account the additional —compared with the previous year— funds raised through these alternative sources of financing, the rate of total credit expansion in December was 12.1% for the "other" sectors and 22.9% for tourism (compared with 11.0% and 15.8% respectively, if these funds are not taken into account).

Among the sectors that contributed to faster credit expansion, the most notable developments concern trade, where the annual growth rate of loans stood at 12.7% in the fourth quarter of 2004, compared with 4.0% in the fourth quarter

7 According to data reported by industrial firms listed on the Athex, in 2004 these firms issued corporate bonds amounting to €605 million, compared with €210 million in 2003. Furthermore, in 2004 industrial firms raised through the Athex funds totalling €102 million, compared with €80 million in 2003.

Table IV.3

Breakdown of credit to enterprises and households in Greece

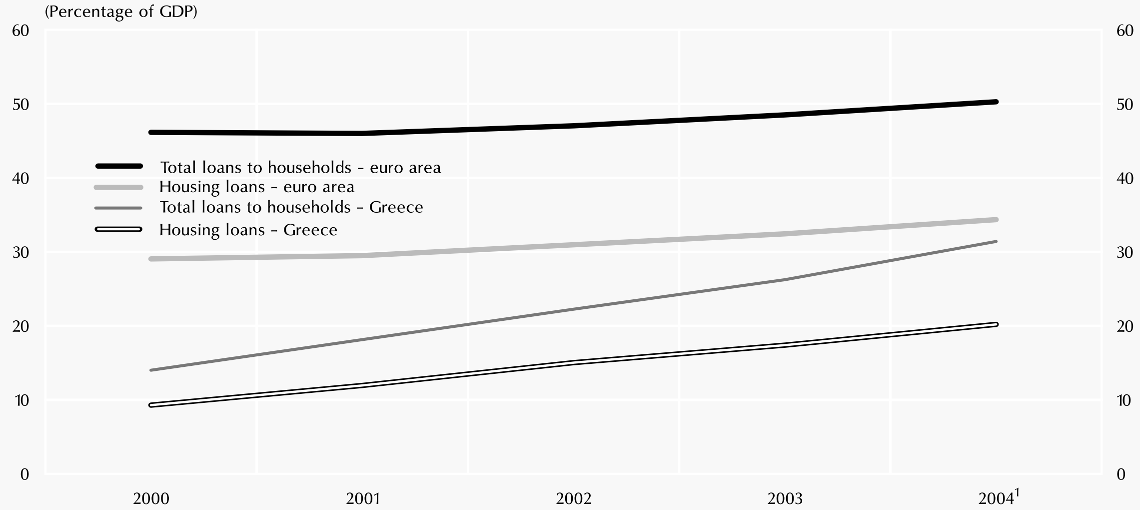
	Outstanding balances on 31.12.04 (million euro)	Annual percentage changes							
		2001	2002	2003	2004				
		Q4[1]	Q4[1]	Q4[1]	Q1[1]	Q2[1]	Q3[1]	Q4[1]	December[2]
A. Enterprises	**65,566**	**16.7**	**11.4**	**11.0**	**10.9**	**10.5**	**8.2**	**8.6**	**7.5**
1. Agriculture	3,248	–2.6	–14.0	3.3	2.6	5.5	9.1	7.8	5.4
2. Industry[3]	15,676	10.2	11.5	10.4	10.2	7.5	1.8	1.1	–1.2
3. Trade	18,821	20.3	7.8	4.0	4.5	7.6	10.2	12.7	14.0
4. Tourism	4,040	14.2	33.7	24.4	18.6	19.4	18.9	17.6	15.8
5. Shipping	4,495	7.8	5.5	2.3	4.0	7.0	4.0	3.0	4.1
6. Non-monetary financial institutions	2,693	141.8	72.5	–3.2	–2.2	6.0	2.9	9.5	–2.7
7. Other	16,593	24.6	14.3	26.5	25.6	18.5	12.6	11.7	11.0
B. Households	**51,636**	**40.0**	**33.1**	**28.2**	**27.5**	**28.9**	**28.2**	**28.0**	**28.5**
1. Housing loans	33,127	36.7	35.4	27.1	24.5	24.7	22.9	23.8	24.8
2. Consumer loans	17,054	44.3	27.4	24.8	29.2	34.5	38.2	37.9	37.4
– Credit cards	7,665	62.1	37.1	27.8	24.8	23.3	23.0	23.4	23.2
– Other consumer[4] loans	9,389	31.8	19.2	21.8	33.9	46.9	54.9	53.1	51.7
3. Other	1,455	165.5	62.6	135.7	119.2	87.5	47.6	18.8	15.9
TOTAL	**117,202**	**23.2**	**18.3**	**17.1**	**16.9**	**17.4**	**15.7**	**16.1**	**15.8**

1 The quarterly average is derived from monthly averages (which are calculated as arithmetic means of two successive end-of-month figures) and is not the three-month average of end-of-month annual growth rates (see the "Technical Notes" in the ECB *Monthly Bulletin*).
2 Annual rate of change at the end of the month.
3 Comprising manufacturing and mining/quarrying.
4 Including personal loans and loans against supporting documents.
Source: Bank of Greece.

Chart IV.2

Bank loans to households

(Percentage of GDP)



1 Estimates for the 2004 GDP.

Sources: Bank of Greece and ECB for outstanding loans, Ministry of Economy and Finance and Eurostat for GDP.

of 2003. Thus, the share of this sector in total credit expansion to enterprises rose to 50% in 2004, from 14% in 2003.

Credit expansion to households remained at high levels in 2004 (fourth quarter of 2004: 28.0%, fourth quarter of 2003: 28.2%, see Table IV.3). This development reflects, on the one hand, the slowdown in the growth rate of housing loans and, on the other hand, the significant acceleration of the growth rate of consumer loans following the abolition of borrowing ceilings in June 2003. It is estimated that total loans to households as a percentage of GDP rose to 31.4% in December 2004 (December 2003: 26.3%), thus tending to approach gradually the corresponding euro area average (December 2004: 50.3%, December 2003: 48.5%, see Chart IV.2).

In more detail, the annual growth rate of housing loans fell to 23.8% in the last quarter of 2004 from 27.1% in the last quarter of 2003. To some extent, this deceleration is due to the securitisation of housing loans by two credit institutions, in November 2003 and June 2004 respectively (see the Appendix to this Chapter). Taking the securitised loans into consideration, the slowdown in the growth rate of housing loans is marginal, as this rate comes to 26.8% for the fourth quarter of 2004.

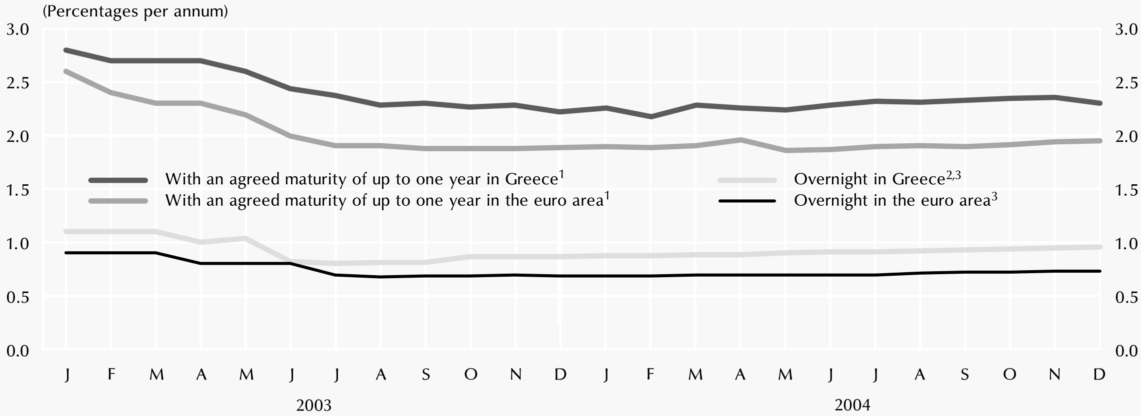
According to data on new loans, the monthly level of new housing loans in 2004 was on average €670 million, i.e. 36% higher than in 2003 (€492 million), confirming the strong potential of housing credit. It should be pointed out, however, that the share of loans with an initial rate fixation of up to one year or with a floating rate increased,[8] accounting on average for 83% of all new housing loans in 2004, compared with 71% in 2003. The outstanding balance of housing loans as a percentage of GDP stood at 20.1% in December 2004, i.e. at a significantly lower level than in the euro area (34.3%).

The outstanding balance of consumer loans to households displayed a high and accelerating rate

8 This loan category has lower interest rates than loans with an initial rate fixation of over one year.

Chart IV.3

Bank interest rates on new deposits from households in Greece and in the euro area
(January 2003 - December 2004)
(Percentages per annum)



1 Monthly average rate.
2 The interest rate on savings deposits is used, as these deposits represent the bulk of overnight deposits and their interest rate is almost the same as the overnight rate.
3 Interest rate at the end of the month.

Sources: Bank of Greece and ECB.

of increase (fourth quarter of 2004: 37.9%, fourth quarter of 2003: 24.8%). Moreover, the restructuring of household borrowing, which had started following the removal of consumer credit restrictions in June 2003, continued in 2004. Thus, despite the high annual growth rate of loans through credit cards (fourth quarter of 2004: 23.4%), their share in total consumer loans fell to 45% in December 2004 from 50% in December 2003.

3. Bank interest rates

Interest rates on bank deposits[9] exhibited minor changes in the course of 2004, as ECB rates have remained unchanged since June 2003. Somewhat greater changes were recorded in bank loan interest rates, which declined overall in 2004.

The average rate on household overnight deposits showed a small increase (of 9 basis points) in 2004 (December 2004: 0.96%, see Chart IV.3), i.e. almost equal to the increase recorded in the rate on savings deposits (December 2004: 0.94%), which account for the greatest part (92%) of overnight deposits. The relatively low interest rate on overnight deposits is associated with the historically low level of ECB rates and the high degree of liquidity of these deposits, as well as with the operating cost of services offered by banks through such deposit accounts (standing payment orders and bill payments through cards, cheque processing). It should be noted that the interest rates applied by banks to these deposit account categories (savings, current account, sight/demand) also vary according to the level of the account balance and are very low or zero for low account balances.[10]

In the course of the previous year, the interest rate on new repos remained virtually unchanged

9 Since the beginning of 2003, bank interest rates on deposits and loans throughout the euro area are recorded using a common methodology (see *Monetary Policy* 2003-2004, Box 2, March 2004).
10 As mentioned above, on 1 January 2005, the tax rate on deposit interest was reduced to 10% from 15%, while the corresponding rate on repo yields rose to 10% from 7%. Thus, a common tax rate was set for these investments.

Table IV.4

Bank interest rates on new deposits and loans in the euro area and Greece

(Percentages per annum)

A. Deposits

	December 2003	December 2004	Change Dec. 2004/Dec. 2003
A.1. Overnight from households[1]			
Weighted average interest rate in the euro area	0.69	0.73	0.04
Maximum interest rate	1.20	1.17	–0.03
Minimum interest rate	0.07	0.12	0.05
Interest rate in Greece	0.87	0.96	0.09
A.2. With an agreed maturity of up to one year, from households[2]			
Weighted average interest rate in the euro area	1.89	1.95	0.06
Maximum interest rate	2.38	2.35	–0.03
Minimum interest rate	1.47	1.49	0.02
Interest rate in Greece	2.22	2.30	0.08

B. Loans with a floating rate or an initial rate fixation of up to one year[2]

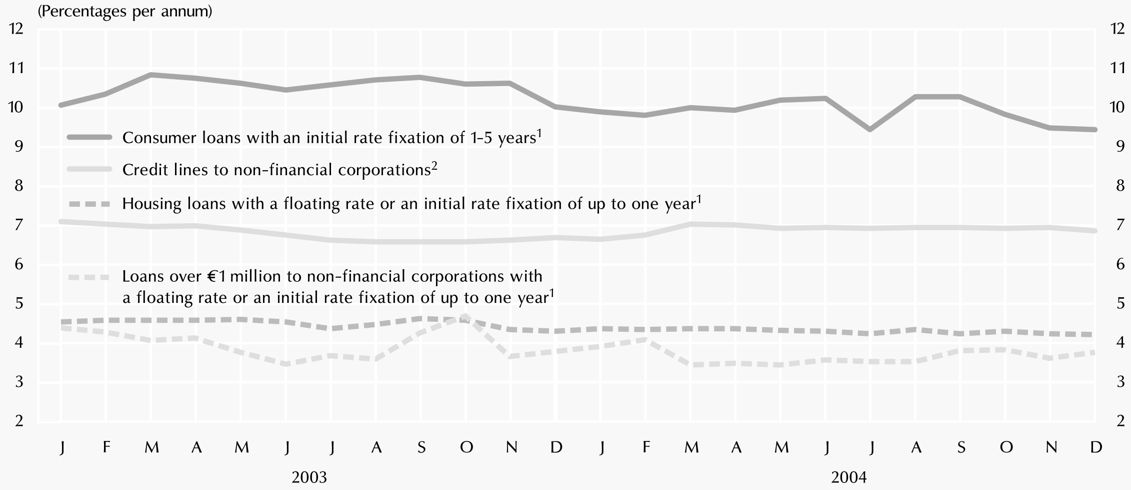
	December 2003	December 2004	Change Dec. 2004/Dec. 2003
B.1. Loans up to €1 million to non-financial corporations			
Weighted average interest rate in the euro area	4.03	3.98	–0.05
Maximum interest rate	5.63	5.52	–0.11
Minimum interest rate	2.78	3.48	0.70
Interest rate in Greece	5.13	5.04	–0.09
B.2. Loans of more than €1 million to non-financial corporations			
Weighted average interest rate in the euro area	3.12	3.05	–0.07
Maximum interest rate	4.33	4.09	–0.24
Minimum interest rate	2.88	2.67	–0.21
Interest rate in Greece	3.78	3.77	–0.01
B.3. Housing loans			
Weighted average interest rate in the euro area	3.62	3.43	–0.19
Maximum interest rate	4.63	4.37	–0.26
Minimum interest rate	3.29	3.10	–0.19
Interest rate in Greece	4.31	4.21	–0.01
B.4. Consumer loans			
Weighted average interest rate in the euro area	7.64	7.24	–0.40
Maximum interest rate	10.87	10.96	0.09
Minimum interest rate	5.02	4.73	–0.29
Interest rate in Greece	9.60	8.58	–1.02

C. Loans with an initial rate fixation of 1-5 years[2]

	December 2003	December 2004	Change Dec. 2004/Dec. 2003
C.1. Consumer loans			
Weighted average interest rate in the euro area	6.54	6.60	0.06
Maximum interest rate	10.03	10.59	0.56
Minimum interest rate	4.34	4.25	–0.09
Interest rate in Greece	10.03	9.45	–0.58

1 Interest rate at the end of the month.
2 Monthly average rate.
Sources: ECB and euro area NCBs.

Chart IV.4
Interest rates on new bank lending in Greece (January 2003 - December 2004)
(Percentages per annum)



1 Monthly average rate.
2 Interest rate at the end of the month.
Source: Bank of Greece.

(December 2004: 2.01%), while a small increase (of 8 basis points) was recorded in the interest rate on new deposits with an agreed maturity of up to one year (December 2004: 2.30%).

With regard to the above categories of deposits, the interest rate differential between Greece and the euro area remained positive in the course of 2004, as euro area interest rates on these deposits also showed no significant change (see Table IV.4). By contrast, the Greek interest rate on new repos stood broadly at the same level as the average repo rate in the euro area (2.02%). In general, no significant yield differentials were observed across euro area repo markets due to the homogeneity of the products and the typically large amounts involved in transactions in the repo market.

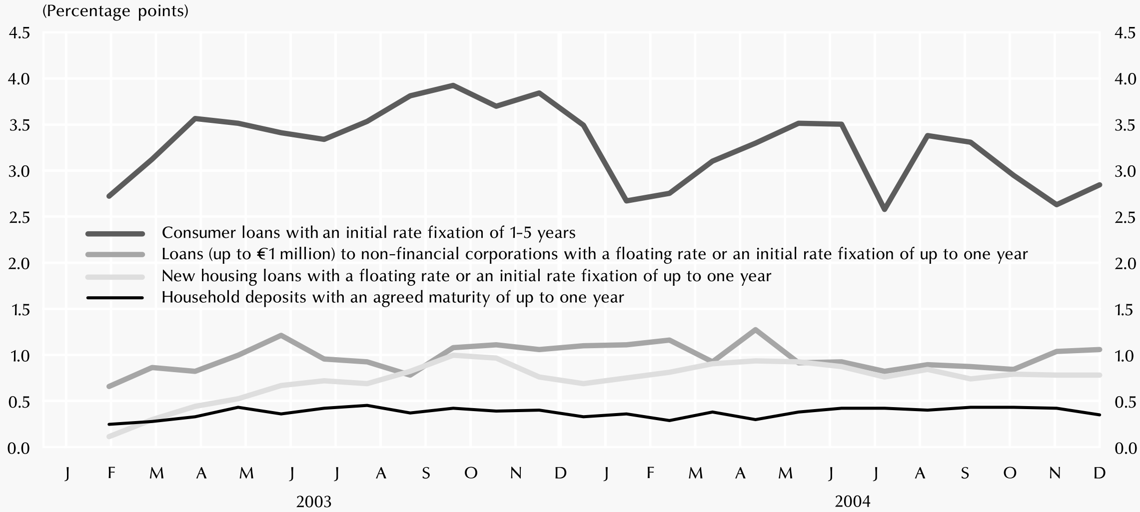
The level of bank lending rates depends on the collateral offered, the credit risk involved and the maturity of the loan. In general, interest rates are higher for loans without a defined maturity and lower for housing loans and large corporate loans with a floating rate or an initial rate fixation of up to one year. As regards the evolution of interest rates in the course of 2004, it should be noted that those on new consumer loans (regardless of their maturity) registered a larger decline, those on new housing loans displayed a smaller decrease (see Chart IV.4), while those on corporate loans showed marginal changes. Specifically, the average rate on all new consumer loans (with a defined maturity) dropped by 50 basis points in 2004 (December 2004: 9.36%). The rate on new consumer loans with an initial rate fixation of over one and up to five years, which account for about 43% of consumer loans with a defined maturity, fluctuated in the course of the previous year and in December it stood at 9.45%,[11] i.e. 58 basis points lower than in December 2003. As the corresponding euro area rate increased marginally in the previous year, the differential between the two rates narrowed (to 2.85 percentage points in

11 It should be pointed out that the interest rate on the other, equally significant, type of consumer loans, i.e. loans with a floating rate or an initial rate fixation of up to one year —which account for 42% of consumer loans with a defined maturity— displayed the largest decline (by 1.02 percentage points) in 2004.

Chart IV.5

Interest rates on new bank deposits and loans: differentials between Greece and the euro area (January 2003 - December 2004)

(Percentage points)



Sources: Bank of Greece and ECB.

December 2004, down from 3.49 percentage points in December 2003, see Chart IV.5). This differential remains high, reflecting to a certain extent the increased uncertainty faced by banks in Greece with regard to doubtful loans and the extent to which they will be repaid. More specifically, given that restrictions on consumer credit have been only recently abolished, available data do not cover a sufficiently long time span to allow for an adequate assessment of credit risks. Moreover, difficulties have arisen regarding the prompt updating of the "Tiresias S.A." database.

The interest rate on consumer loans without a defined maturity —the most important type of consumer loans— displayed a relatively large decline in 2004 (of 67 basis points, to 13.41% in December). As the corresponding euro area rate decreased less (by 18 basis points), the differential between the two rates narrowed further, to 3.90 percentage points in December 2004, from 4.39 percentage points in December 2003. This relatively wide differential between Greek and euro area rates on loans without a defined maturity is mainly due to the large share of loans through credit cards in the total of loans without a defined maturity, as well as to the high rate on loans through credit cards in Greece (December of 2004: 14.29%), which mainly reflects their higher risk premium and operating costs for banks.

The weighted average interest rate on all new housing loans recorded an upward movement in the first quarter of 2004 and, after some fluctuations, stood in December at a slightly lower level than at the end of 2003 (December 2004: 4.37%, December 2003: 4.53%). The interest rate on new housing loans with a floating rate or an initial rate fixation of up to one year —which account for 83% of total housing loans— came to 4.21% in December 2004, i.e. it was a little lower than in December 2003 (4.31%). As the corresponding euro area rate on housing loans decreased by 19 basis points in 2004 (see Table IV.4), the differential between the two rates widened slightly (to 78 basis points in December 2004 from 69 basis points in December 2003). It should be pointed out that differentials between Greek and euro area rates on housing loans are associated with the fact that the time required for the liquidation of real estate serving as loan collateral is longer in Greece. Moreover, these differentials should be viewed against the aforementioned background of uncertainty surrounding credit risk measurement and, hence, the cost of doubtful loans.

Turning to interest rates on loans to non-financial corporations, the rate on loans without a defined maturity[12] —which account for around one-third of the outstanding amount of loans to corporations— increased in 2004 by 19 basis points (December 2004: 6.97%). However, this rise is due to statistical reasons.[13] As the corresponding euro area rate dropped in the course of 2004, the differential between the two rates widened, to 1.71 percentage points in December 2004 from 1.20 percentage points in December 2003. This significant interest rate differential reflects the fact that the above loan category is not homogeneous across euro area countries as regards loan collateral and other loan terms.[14] Nevertheless, the Greek rate is not the highest in the euro area. In 2004, a small decline (of 9 basis points) was recorded in Greek interest rates on corporate loans with a floating rate or an initial rate fixation of up to one year for loans up to €1 million, while interest rates on same-type loans over €1 million remained virtually unchanged.

The spread between the weighted average interest rate on total new bank loans and the corresponding rate on deposits remained roughly unchanged in 2004 (December 2004: 4.84 percentage points, December 2003: 4.89 percentage points), as both the average lending rate and the average deposit rate remained broadly stable. Specifically, average deposit and lending rates stood at 1.18% and 6.02% respectively in December 2004. However, it should be pointed out that the average interest rate depends not only on changes in the rates on individual categories of loans and deposits but also on each category's share in total deposits or loans. The continuous increase in the share of consumer loans in total loans leads to an increase in the average lending rate, which therefore does not fully reflect the general fall of interest rates in individual loan categories.

The average interest rate on the outstanding amounts of euro-denominated loans, which affects the operating income of banks, showed a small decline in 2004. Specifically, a decrease was recorded in the interest rate on the most important type of consumer loans (with a maturity of up to one year), as well as in the interest rate on the largest category of housing loans (with a maturity of over five years). Moreover, in the previous year the interest rate on short-term loans to non-financial corporations (which constitute the most significant type of corporate loans) remained virtually unchanged, while a decline was recorded mainly in the interest rate on long-term corporate loans.

4. Capital markets

4.1 The bond market

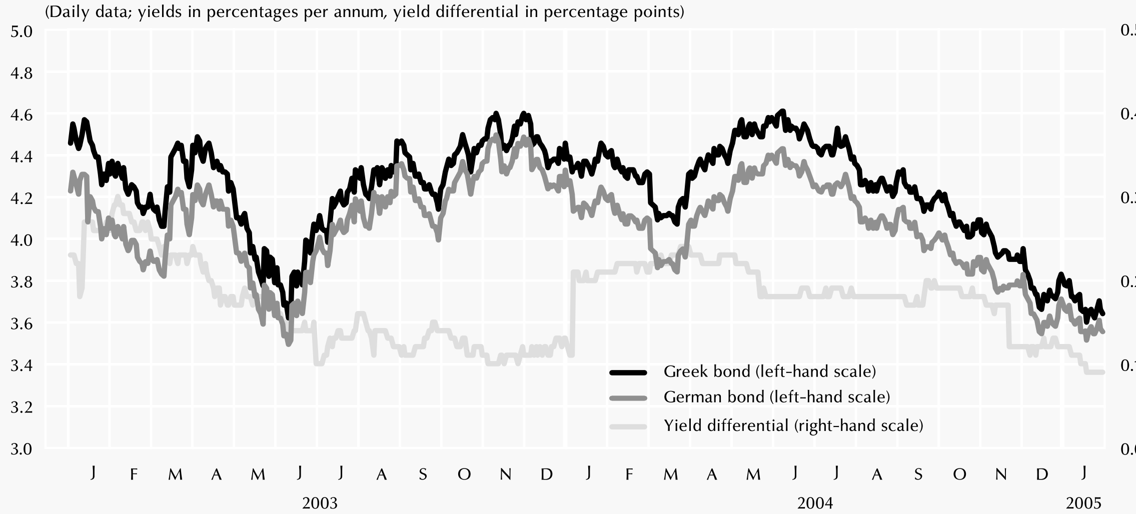
Greek government bond yields declined substantially in 2004, reflecting similar developments in the yields of comparable securities in the euro

12 The most significant sub-category of these loans are loans through credit lines, whose interest rate displayed a similar increase.
13 In February and March 2004 a bank reclassified certain low-rate corporate loans from the category of credit lines to the category of loans with a defined maturity, thereby raising the average interest rate of loans through credit lines.
14 In some euro area countries like France and the Netherlands, these loans are fully covered by collateral, which contributes to a low interest rate.

Chart IV.6

Yields on the 10-year Greek and German government bonds
(January 2003 - January 2005)

(Daily data; yields in percentages per annum, yield differential in percentage points)



Sources: Bank of Greece and Bloomberg.

area,[15] while transactions in these securities on the secondary market rose markedly.

In more detail, Greek government bond yields in the Electronic Secondary Market for Securities (HDAT) followed a downward path during the first three months of 2004, which however reversed in the second quarter of the year (see Charts IV.6 and IV.7). This reversal is attributable to the upward revision of market estimates about the growth rate of the world economy, as well as to expectations of an increase in US interest rates.[16] Thereafter and until the end of December, the demand for government bonds strengthened anew, with their yields falling significantly. Underlying this development were investors' concerns about the impact of higher oil prices on economic activity and of the ongoing appreciation of the euro on euro area exports and economic growth. Bond yields kept falling in January 2005 (see Chart IV.6). Moreover, it should be noted that volatility in HDAT and the euro area bond market declined significantly[17] during 2004.

The yield on the ten-year Greek government bond stood at 3.80% at the end of December 2004, i.e. 62 basis points lower than at the end of December 2003. The yield recorded a peak (4.61%) on 14 and 15 June and a trough (3.66%) on 16 December. The yield differential between the Greek ten-year bond and the comparable German bond was 13 basis points at end-December 2004,[18] i.e. roughly

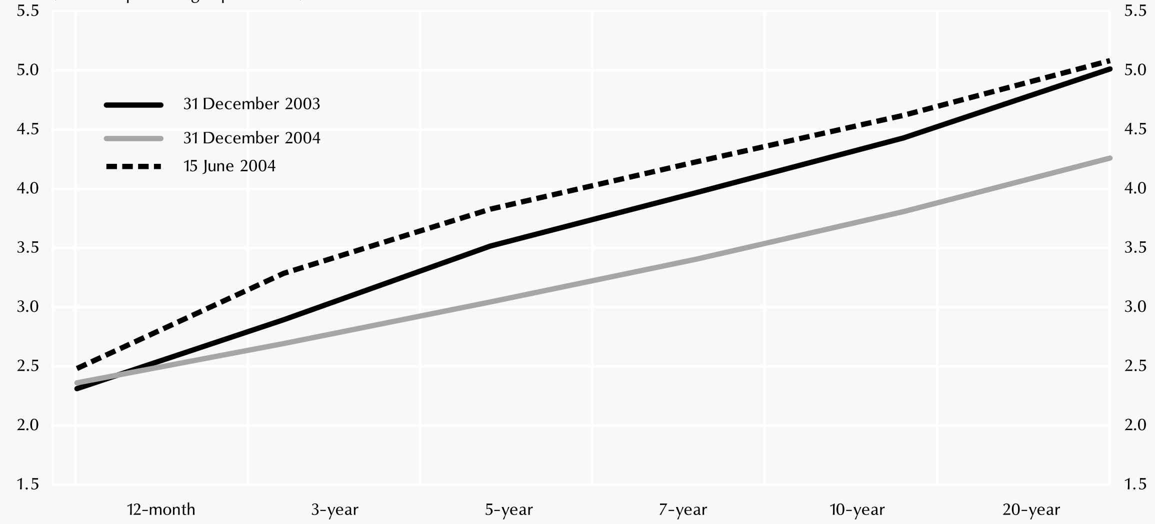
15 For developments in euro area and US bond markets see Chapter II.3.3.

16 These expectations came true on 30 June 2004, when the US Federal Reserve raised, for the first time in recent years, its target for the federal funds rate by 25 basis points.

17 Volatility in international bond markets, as measured by the implied volatility in the prices of options of futures contracts on ten-year government bonds, recorded a marked decline in 2004 and generally fell below the average level of the last five years. For further analysis see ECB, *Monthly Bulletin*, December 2004.

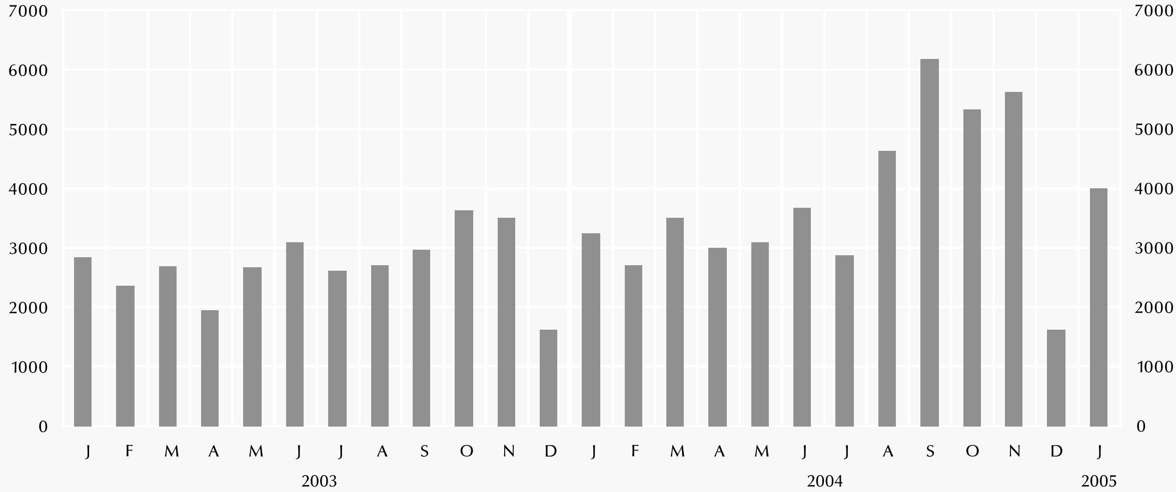
18 By mid-January 2004 this differential widened significantly to 21 basis points, due to the issuance of a new Greek reference bond with a maturity 5.5 months longer than that of the corresponding German bond. From the beginning of June to the end of November, the differential narrowed and came to 18 basis points on average. The significant further decline of this differential to 12 basis points from the end of November is due to the fact that a new German reference bond was issued on 24 November 2004, maturing on 4 January 2015, i.e. 7.5 months after the comparable Greek bond. If both bonds theoretically had the same maturity date, the yield differential would reach 21 basis points at the end of December 2004.

Chart IV.7
Greek government paper yield curves
(Yields in percentages per annum)



Source: Bank of Greece.

Chart IV.8
Average daily value of transactions in the Electronic Secondary Market for Securities (HDAT) (January 2003 - January 2005)
(Million euro)



Source: Bank of Greece.

unchanged from end-December 2003 (see Chart IV.6). The downgrading of Greece's long-term credit quality (from A+ to A) by the international rating agencies Standard & Poor's and Fitch (on 17 November and 16 December, respectively) due to the fiscal data revision is estimated to have had almost no effect on this differential.

Between end-December 2003 and end-December 2004, Greek government bond yields declined across the maturity spectrum, with the excep-

Table IV.5
Greek government paper issuance

Type of security	January - December 2003 Million euro	2003 Percentage of total		2004 Million euro	2004 Percentage of total	
Treasury bills	*1,737*	*4.8*		*2,493*	*5.7*	
Bonds[1]	*34,784*	*95.2*	*100.0*	*40,868*	*94.3*	*100.0*
1-year	2,569		7.4	7,183		17.5
3-year	7,828		22.5	8,663		21.2
5-year	9,002		25.9	12,352		30.3
7-year	191		0.5	96		0.2
10-year	9,757		28.1	9,692		23.7
12-year	–		–	384		0.9
15-year	649		1.9	–		–
20-year	3,541		10.2	242		0.7
23-year	1,247		3.5	2,256		5.5
Total	**36,521**	**100.0**		**43,361**	**100.0**	

1 By initial maturity as regards the reopening of past issues.
Source: Ministry of Economy and Finance.

tion of bonds with a twelve-month maturity, whose yields showed a small rise. The most marked reductions were seen in long-term (20-year and 10-year) bonds. The government bond yield curve shifted downwards (see Chart IV.7) and its slope flattened in the section corresponding to maturities of 12 months to 10 years, as evidenced by the yield spread between the ten-year bond and the 12-month Treasury bill, which narrowed by 67 basis points in 2004. It should be noted that in mid-June 2004 the yield curve had clearly shifted upwards compared with the end of 2003, because yields rose appreciably in the second quarter of 2004, as mentioned above (see Chart IV.7).

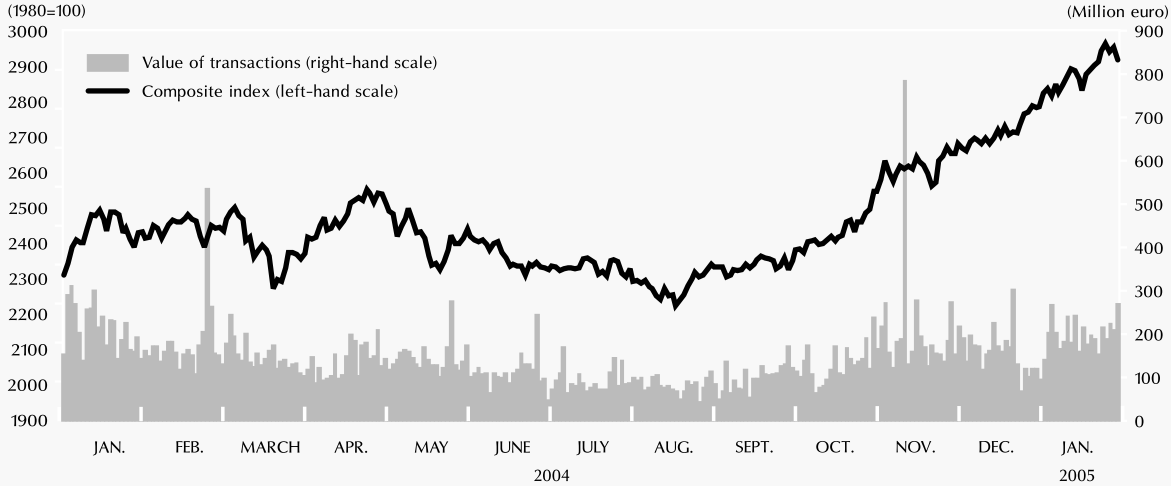
The average daily value of transactions in HDAT grew by 39% to €3.8 billion in 2004, compared with the previous year[19] (see Chart IV.8). This strong rise in turnover enhanced significantly the liquidity and efficiency of the secondary market, as indicated by the further narrowing of the bid-ask spread. This spread stood at 6.1 basis points in December 2004, compared with 8.2 basis points in December 2003 and 9.4 basis points in December 2002. Investors showed a preference for ten-year bonds, which accounted for approximately 61% of the total value of transactions in 2004.

In the primary market for Greek government securities, the total amount of funds raised in 2004 increased by 19% to €43.4 billion,[20] compared with 2003 (see Table IV.5). A significant part of the total bond issues concerned syndicated loans (new issues and reopenings of past issues)[21] and, to a lesser extent, issues by auction procedures (new ones and reopenings). The high coverage ratio of the auctioned issues[22] reflects the continued strong attractiveness of Greek government bonds for domestic and foreign investors.

19 The corresponding growth in 2003 against 2002 was 19%.
20 It should be noted that in 2004 redemptions of Greek government securities reached €25.5 billion.
21 Out of these issues, an amount of €2.3 billion concerned the reopening of the 23-year bond issue linked to the Harmonised Index of Consumer Prices (excluding tobacco) of the euro area.
22 According to available data, during the January-September 2004 period, investment demand for Greek government securities was more than four times as high as supply.

Chart IV.9

Athens Exchange: composite share price index and value of transactions
(January 2004 - January 2005)
(Daily data)



Source: Athens Exchange.

It should be noted that, out of bonds with a maturity of up to one year (representing 18% of the total value of bond issues), an amount of €1.1 billion concerned Special Savings Bonds issued in February 2004, while €6.1 billion were issues of euro commercial paper.[23] Moreover, 3- and 5-year bond issues totalled an amount of €21 billion and had a share of 51%, while the remaining 31% of total bond issues was allocated among 7-, 10-, 12-, 20- and 23-year bond issues. Finally, Treasury bill issues remained low in 2004 and accounted for about 6% of the total value of issues. The weighted average maturity of Greek government securities issued in 2004 declined compared with 2003.[24]

4.2 Stock market developments

The composite share price index of the Athens Exchange (Athex) registered an overall increase in 2004, rising stronger from the end of August (see Chart IV.9). Specifically, share prices in the Greek stock market, in line with similar developments mainly in the stock markets of the euro area,[25] rose between the beginning of 2004 and early March. This rise reflected a sizeable recovery in corporate profitability in 2003 (35%) and a significant decline in stock market uncertainty.[26] However, thereafter, Athex stock prices followed a broadly downward path until the end of August 2004, owing to investors' concerns about the potential impact of rising oil prices on economic activity and corporate profitability. In the following four months, stock prices recovered appreciably, mainly due to the continuous improvement in corporate prof-

23 These are short-term financing instruments and are sold to Primary Dealers. Apart from asset management purposes, they serve to improve liquidity and lower borrowing costs for the government.

24 According to the latest available data, the weighted average maturity of Greek government paper issued during the January-September 2004 period fell to 6.85 years, from 7.22 years in 2003.

25 The ASE composite share price index recorded in 2004 the third best performance compared with the other euro area stock markets. Note that the correlation of performances of stock price indicators in euro area stock markets grows continuously in recent years, due to the increasing integration of these markets, which however remains relatively low. For further analysis, see Baele *et al.*, "Measuring financial integration in the euro area", ECB, Occasional Paper No. 14, April 2004.

26 About this issue, see ECB, *Monthly Bulletin*, November 2004.

Table IV.6
Fund raising through the Athens Exchange

Branches	January - December			
	Number of firms		Funds raised (million euro)[1]	
	2003	2004*	2003	2004*
Listed companies	35	33	317.0	397.2
Newly listed companies	13	10	61.0	79.4
Total	**48**	**43**	**378.0**	**476.6**
– Banks	4	4	105.8	185.2
– Investment	2	1	3.0	13.2
– Insurance	2	1	35.0	3.0
– Holding	1	2	0.3	11.8
– Industrial	17	12	80.4	102.5
– Construction	1	2	7.5	41.0
– Commercial	5	5	36.3	37.7
– Telecommunications	3	2	3.0	10.0
– Information technology	12	9	38.6	24.3
– Other	1	2	8.1	47.9

1 Share capital increase through public subscription and private investment. Subscriptions to new capital are entered on the last day of the subscription period.
* Provisional data.
Sources: Athens Exchange and Bank of Greece.

itability,[27] as well as the positive climate in international stock markets. Stock prices continued to increase in January 2005 (see Chart IV.9).

In more detail, between end-December 2003 and end-December 2004, the composite share price index of the Athex rose by 23.1%.[28] A peak of 2,788.7 points was recorded on 29 December and a trough of 2,227.3 points on 20 August. The composite index thus substantially outpaced both the broad Dow Jones EURO STOXX index in the euro area[29] (rise of 10.0%) and the Standard and Poor's 500 index in the United States (9.0%).[30]

The average daily value of transactions on the Athex reached €141 million in 2004, i.e. about the same level as in 2003. Participation of foreign institutional investors in transactions on the Athex was particularly high in the period under review.[31] The total amount of funds raised from the stock market,[32] though increasing slightly compared with the two previous years, remained at low levels.[33] In particular, the amount of funds raised rose to €477 million in 2004,[34] from €378 million in 2003, and concerned 43 companies (2003: 48 companies), of which 10 were newly listed and raised €79 million (2003: 13 companies, €61 million, see Table IV.6).

The stock market performance of the banking sector was better than that of the market as a

27 Pre-tax earnings of companies with shares listed on the Athens Exchange rose by 6% during the January-September 2004 period compared with the corresponding period in 2003. On a consolidated basis, the corresponding increase was 10%.
28 The average level of this index in 2004 was 28% higher than in 2003.
29 For this index, see Chapter II, footnote 22, and for a detailed discussion of stock market developments in the euro area, see Chapter II.3.4.
30 Note that, in terms of euro, this index rose by 1.0%.
31 According to Central Depository of Securities data, at the end of December 2004 foreign investors accounted for 36% of the Athex market capitalisation in shares, where the 24% of this percentage refers to institutional investors.
32 Through capital increases.
33 Funds raised in 2004 accounted for almost 7% of the annual average amount raised in the 1998-2000 period.
34 In addition, €15 million were raised in 2004 through secondary public offerings, compared with €1,523 million in 2003 which mostly regarded shares of public enterprises.

whole.[35] This development was largely due to the fact that during 2004 the profitability of commercial banks continued the recovery under way since 2003, following the significant decline observed in 2000-2002. Specifically, in the January-September 2004 period, pre-tax profits of Greek banks with Athex-listed shares rose by some 14.5%[36] relative to the corresponding period of 2003,[37] compared with a 34% increase in 2003. The improved profitability of banks in the January-September 2004 period stemmed mainly from the increase in net interest income as well as income from commission fees and securities, all of which rose faster than operating costs.[38]

35 The stock price index of the banking sector rose by 44.3% between end-December 2003 and end-December 2004.
36 Excluding Geniki Bank, which recorded substantially increased provisions for loan losses following its acquisition by Société Générale. Including Geniki Bank, profitability rose by 4.5%. As regards Greek commercial banks with Athex-listed shares (i.e. excluding the Bank of Cyprus), the corresponding increase was 2.5%, while for the five largest banks the increase was 19.2%.
37 Total net pre-tax profits of the financial sector rose by about 7.2% in the January-September 2004 period, in comparison with the corresponding period in 2003.
38 For a detailed discussion, see Bank of Greece, *Monetary Policy, Interim Report*, October 2004, Appendix to Chapter V.

Appendix to Chapter IV

New forms of financing the economy

Modernising the Greek financial system and improving its efficiency, particularly in the context of increasing integration in the European market, requires the introduction and development of new, alternative methods of funding non-financial corporations and banks. The enactment of a new law[1] concerning corporate bonds and the securitisation of receivables has been a relatively recent development in this direction. The text below provides an overview of these alternative forms of financing.

1. Corporate bonds

The financing of enterprises through corporate bond issues has gained considerable and growing importance in euro area countries, especially following the introduction of the single currency. This trend is related to increasing market integration in the context of the monetary union, which allows businesses to have access to a more homogeneous European capital market. Moreover, it reflects the aim of enterprises to become more flexible in raising funds by using alternative forms of financing. In addition, investors, in the current low interest rate environment, search for placements bearing higher yields, such as those usually offered by corporate bonds. As a result, in December 2004, the outstanding balance of corporate bonds issued by euro area firms amounted to 36% of the loans granted to them by euro area MFIs, compared with 19% in December 1998. Approximately two thirds of the outstanding balance of these bonds are held in portfolios of non-bank investors. While corporate bond issues have been increasing, a substantial secondary market for these securities has also developed, at least in some euro area countries.[2]

The new legal framework regulating the issuance of corporate bonds was introduced in Greece in June 2003,[3] in order to develop alternative sources of corporate funding and offer investors alternative investment opportunities. A considerable increase in corporate bond issues has been noted since then. This development, however, reflects to a significant degree the fact that businesses substitute part of their bank borrowing with corporate bonds, which remain in MFI portfolios. As a result, MFI holdings of bonds issued by local firms represented in December 2004 8.9% of total MFI loans to these enterprises, up from 2.2% in May 2003 (see Chart IV.A1).

Advantages

The increased relative importance of corporate bonds as a source of funding for Greek businesses is a trend expected to persist, as is evident from the increased announcements of corporate bond issuance, since this form of financing offers the following significant advantages:

— Corporate bonds make it possible for enterprises to access capital markets directly, thus providing an additional source of funding.

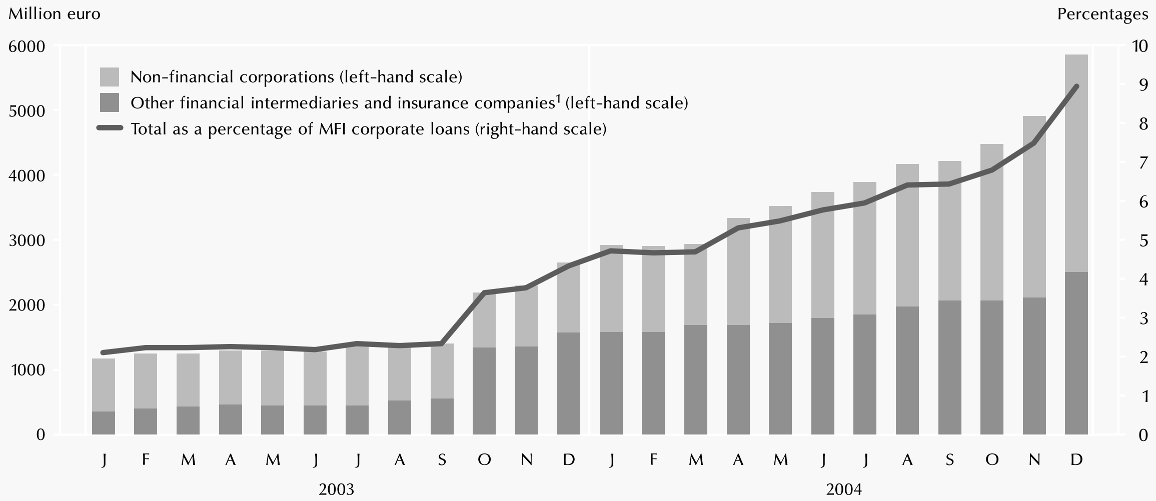
— Bonds can have relatively long maturities, whereas banks may be reluctant to grant loans with such a prolonged repayment period. This feature of bonds allows businesses to proceed with longer-term planning of their investments.

— Besides common bonds, it is possible to issue corporate bonds with special features, which are not available in ordinary bank borrowing. These special types of corporate bonds are:

1 Law 3156/2003 "Corporate bonds, securitisation of receivables and receivables from real estate, and other provisions".
2 However, the secondary market for corporate bonds in the euro area continues to suffer from relatively low liquidity compared with the respective US market.
3 Prior to the introduction of Law 3156, the issuance of corporate bonds was subject to the relevant provisions of Law 2190/1920 "on sociétés anonymes".

Chart IV. A1

Corporate bonds held by MFIs in Greece



1 The contribution of insurance companies to this figure does not exceed 1%.

Source: Bank of Greece.

a) Exchangeable bonds. The bondholders may request that the bonds in their possession be repaid —in part or in whole— by the transfer to them of other bonds, shares or securities issued by the original issuer or another company.[4]

b) Convertible bonds. The bondholders are given the option to have the bonds in their possession repaid by the transfer to them of new shares of the issuer, resulting from a share capital increase.

c) Bonds with profit participation rights. Apart from the interest payable on the bonds, the bondholders are entitled to a percentage of the profits, after preference and common share dividends have been paid, or to some other payment, the size of which is related to the profitability of the company.

– According to Article 14 of Law 3156/2003, corporate bond issuance is not subject to any tax or contribution, including the Law 128/1975 contribution. The latter amounts to 0.6% of the loan balance and, based on the current level of interest rates, represents an increase of approximately 10% in the cost of borrowing from banks.[5]

Given that in practice (according to the prevailing local market conditions) only companies of relatively large or medium size are able to issue corporate bonds,[6] the exemption of these issues from the Law 128/1975 contribution results in more favourable financing conditions for enterprises that issue bonds, compared with relatively smaller firms that cannot do so.

Public offerings – Secondary market

The current legal and institutional framework allows for part or the whole of a corporate bond issue to be covered

4 If the bonds are to be exchanged for shares of the issuer, these shares must have already been issued. Hence, there will be no increase in share capital due to the exchange of the bonds.

5 The interest rate on loans to non-financial corporations with a maturity of between one and five years stood in December 2004 at 5.26% plus the Law 128/1975 contribution.

6 This is mainly due to the fixed costs associated with the issuance of corporate bonds. However, the only limitation imposed by Law 3156/2003 regarding the size of the issuing company relates to its share capital (a minimum of €1.5 million) and this only in the case of public offering. It should be noted, however, that additional limitations have been imposed by the Capital Market Committee (CMC) regarding the minimum size of the bond issue (€200,000) and the minimum size of the net book value of the issuing company's assets (€3 million), if the securities issued are to be listed on the main market of the Athex.

by public offering and for the securities to be traded in organised (secondary) markets, e.g. HDAT or the Athex.[7] Currently, however, corporate bond issues are almost entirely absorbed by banks, either through bilateral agreements or through syndicated corporate bond issues.

The issuance of corporate bonds to the public and the development of an active secondary market for the trading of these securities have not picked up, as the cost of certain procedures which are necessary to protect investors appears to be high for Greek businesses, because of their relatively small size. Specifically, for corporate bonds to be offered to the public, it is required that the creditworthiness of the issuing company be assessed by an agency approved by CMC.[8] It is also required that a relevant prospectus be made available to the public and the issue be approved by CMC. These procedures are time-consuming and costly for the issuing companies. The underwriting services, which are also required, entail additional cost.

Bank capital adequacy

The development of an active and efficient secondary market for corporate bonds, with sufficient liquidity, will enable credit institutions to trade these securities and thus adjust quickly and at relatively low cost the amount of corporate bonds they hold in their portfolios, with favourable effects on their capital adequacy ratio.

However, insofar as these securities remain in bank portfolios, as is currently the case, the increase in their share in total bank credit will have no impact on credit institutions' capital adequacy; it will be, in effect, a substitution of bank loans with corporate bonds, and it is well known that, under the current regulatory framework, both assets carry the same weight in the calculation of the capital adequacy ratio.[9]

Benefits and risks to investors

Corporate bonds offer institutional or private investors returns that are usually higher than those of alternative investments with somewhat comparable features (e.g. government bonds). Moreover, bonds provide investors with a steady flow of income (through coupon payments), unlike alternative investments (e.g. shares), where the flow is uncertain. Additionally, by investing in corporate bonds, investors may get capital gains, besides the nominal return.

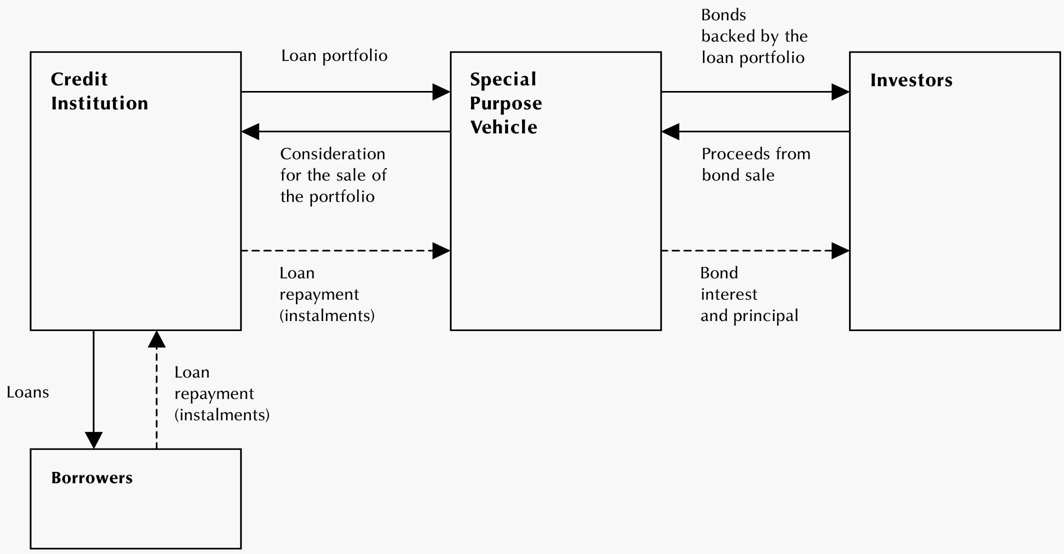
These benefits, however, are accompanied by increased risks to investors. By investing in corporate bonds, they are, in general, exposed to a higher credit risk, apart from the interest rate risk that exists in all investments with a fixed return and a defined maturity.[10] An additional sub-category of credit risk inherent in corporate bonds is event risk, which relates to the possibility of an event (e.g. a corporate transaction, a natural disaster or a change in the regulatory environment) leading to a substantial downgrading of the credit rating of the bond. An important element in assessing the credit risk of a bond is its credit rating, as determined by specialised rating agencies.[11]

Finally, corporate bonds may entail call risk. This risk pertains to bond issues where the issuing company has the right to repurchase the securities issued after a predetermined period of time and, in any case, prior to maturity. Since the issuing company will exercise this right only if it is to benefit therefrom, the inclusion of a call option among the features of the bond issue implies that the risk is unilaterally assumed by the investor.

So, it is indispensable for potential investors in corporate bonds to be briefed accordingly in advance and

7 See Law 3156/2003, Art. 1, par. 1.
8 See Law 3156/2003, Art. 15, par. 13.
9 See Bank of Greece Governor's Act 2524/2003.
10 This risk is relevant to bonds with a fixed interest rate.
11 As mentioned above, for corporate bonds to be offered to the public, Law 3156/2003 (Art. 15, par. 13) requires that the issuing company's creditworthiness be assessed by an agency approved by CMC.

Chart IV. A2
Traditional cash securitisation



carefully consider the risks involved against the returns offered.

2. Securitisation of receivables

Securitisation of receivables initially emerged in the US during the 1970s and mainly related to receivables arising from housing loans. During the 1990s it expanded rapidly in the US but also started to become increasingly important in Europe. At the same time, the types of securitised receivables were broadened to include, *inter alia*, loans to enterprises, loans for the purchase of cars and credit card receivables. Thus, as estimated by Moody's,[12] receivables securitised in Europe totalled €268 billion in 2003.

In Greece the legal framework regarding the securitisation of corporate receivables was put in place with Law 3156/2003.[13] This was followed by the initial securitisations of receivables by Greek credit institutions. The first securitisation, amounting to €250 million, took place in November 2003 (Aspis Bank), while a second followed in June 2004, amounting to €750 million (EFG Eurobank Ergasias). Both securitisations related to housing loans. As a result, MFIs' securitised housing loan receivables in December 2004 amounted to 2.8% of the outstanding housing loan balances in their financial statements.

Description of the procedure

Securitisation is essentially a means of financing the credit institution[14] that transfers its receivables. The traditional form[15] of securitisation comprises the following stages (see Chart IV.A2):

12 See ECB, *The euro bond market study*, December 2004, p. 41. This figure reflects the volume of corporate bond issues in Europe which are related to cash and synthetic securitisations of receivables that originated in Europe.
13 Law 3156/2003 regulates issues relating to the securitisation of receivables in the private sector, which is the subject of the discussion that follows. It should be noted, however, that this law was preceded by Law 2801/2000, which governs the issues relating to the securitisation of receivables in the public sector. Indeed, the Greek State has taken advantage of the provisions of this law, by securitising some of its receivables.
14 The discussion that follows covers, for ease of presentation, only the case where the enterprise that transfers its receivables is a bank. The legal framework also allows non-financial corporations to securitise receivables, although up until now Greek enterprises have not taken advantage of this possibility. The procedure described is generally the same when the transferring enterprise is not a credit institution.
15 This description refers to the traditional form of cash securitisation, which is explicitly provided for by Law 3156/2003. It should be noted that, internationally, the method of synthetic securitisation is also used, where only the credit risk associated with a loan portfolio is transferred rather than the actual portfolio.

a) The credit institution transfers its receivables from customer loans to a "Special Purpose Vehicle" (SPV). After the transfer, these loans are no longer included in the portfolio of the credit institution and do not appear on its balance sheet.[16] After the transfer of the receivables, however, the credit institution may continue to manage the loan portfolio on behalf of the SPV, for a servicing fee. As a result, the borrower may continue to transact with the credit institution which had originally granted the loan, without necessarily appreciating that the loan has been transferred.

b) The SPV (which may be located in Greece or abroad) issues bonds which are secured by the loans that have been transferred to the SPV. The proceedings from the bond sale are used to settle the liabilities of the SPV towards the transferring bank resulting from the acquisition of the receivables. The cash inflows from the receivables transferred to the SPV are used to settle its liabilities resulting from the bond issue.[17]

c) The bonds are sold to investors. According to the provisions of the relevant law, the bonds cannot be sold through a public offering, hence the sale may only be carried out through a private placement. Moreover, for mutual and investment funds based in Greece to participate in the private placement, the securities are required by law to have been awarded an investment grade credit rating by an internationally recognised rating agency.[18] Pension funds and social security funds are not permitted to participate in the private placement either directly or through mutual or investment funds. The development of the markets involved and an improvement in their efficiency, as well as an increase in the number of rated bond issues, will perhaps allow the revision of this provision in the future so that pension funds and social security funds may be permitted to invest in these securities.

Advantages

Securitisation of receivables as a means of financing offers credit institutions that use it the following advantages:

— They are able to achieve lower funding costs as, in the case of securitisation, these costs reflect the risk premium related to the securitised portfolio only and not to the entire enterprise to be funded. In most cases, the composition of the securitised portfolio (e.g. housing loans) is such that a high credit rating and, as a result, lower funding costs are achieved.

— Moreover, credit institutions increase their liquidity and gain access to an additional source of funding, thereby reducing their dependence on traditional sources, such as deposits or interbank lending. Additionally, their capital adequacy may be enhanced to a certain degree. When the securitised loans are removed from credit institutions' balance sheet, their capital adequacy ratio improves and regulatory capital is released so that it may be used in more profitable activities. Credit institutions are therefore able to restructure their portfolios quite rapidly.

Generally speaking, the use of this alternative means of financing contributes, to the extent that banks share with their customers some of the benefits they

16 It should be noted that, according to International Accounting Standards, for the transfer of the loans to be recognised as a true sale, the credit institution must transfer to the SPV all the risks and rewards linked with these receivables. Moreover, for the supervisory treatment of the loans transferred, the Bank of Greece has introduced specific rules, which are briefly outlined in the "Bank capital adequacy" section of Part 2 of this Appendix.

17 Given that the acquisition of the receivables occurs prior to the issue and sale of the bonds, the SPV may temporarily require some financing. This may be provided by the bank transferring the receivables.

18 International practice is that bonds are always rated by international rating agencies in order to establish the creditworthiness of the securities so as not only to ensure investor demand for the issue but also to correctly price it. Moreover, it is common practice for securitised receivables to be divided into tranches of assets with similar risk features, which are rated and priced individually.

enjoy, towards improving the efficiency of the financial system.

Bank capital adequacy

It was mentioned above that credit institutions securitising receivables improve their capital adequacy. This is because securitised receivables no longer appear as assets on the balance sheet of the credit institution in question and are replaced by cash, which leads to the improvement in the capital adequacy ratio. It should be noted that the Bank of Greece, in accordance with international best practices, has introduced a specific supervisory framework for the treatment of securitised receivables.[19] Accordingly, for the credit institution not to be subject to capital requirements for the securitised receivables and for the corresponding SPV not to be subject to consolidated supervision, certain conditions must be met, the most important of which are outlined below:

— The transferring bank must neither bear any remaining risk nor enjoy any remaining benefit from the initial principal of the transferred receivables.

— The securities issued by the SPV must not, under any circumstances, constitute liabilities of the transferring bank but, rather, claims of the bondholders against the SPV and, ultimately, the original borrowers.

— The transferring bank must not have assumed the obligation to exercise a call option on the securities issued or to repurchase the receivables in question, while the amount of securities held in its portfolio must not exceed 10% of the total nominal value of the issue.

— The transferring bank must not act as underwriter for the bond issue.

— A legal opinion must be obtained, certifying, among other things, that the transferring bank will be completely isolated from the receivables transferred.

— The name of the SPV must not include (or be directly related to) the name of the transferring bank, which should not be represented by more than one member on the board of directors of the SPV. However, the Bank of Greece retains the right to demand that the transferring bank have no direct or indirect equity stake in the SPV.

— The transferring bank must not cover the running costs of the SPV. It should be noted, however, that, under certain circumstances, the transferring bank is permitted to provide short-term liquidity to the SPV.

— The transfer of receivables for securitisation must not lead to a significant deterioration of the average quality of the receivables remaining on the balance sheet of the transferring bank.

It should also be noted that if the transferring bank provides "credit enhancement", i.e. assumes or retains by contract the economic risk linked with the transferred receivables so as to provide additional security to investors, the relevant amount is subtracted from the regulatory capital of the bank, thereby reducing its capital adequacy ratio.

Tax issues

The transfer of receivables to and from the SPV is not subject to any direct or indirect tax, contribution etc. Moreover, any loan or credit contracts the SPV enters into are also not subject to any tax.

Prospects

Given the advantages that the securitisation of receivables offers to transferring banks, as outlined above, it is expected that more credit institutions based in Greece will benefit from the securitisation of housing

19 See Bank of Greece Administration Circular No. 9/2003.

loans. Moreover, it is expected that they will proceed to securitise receivables from loans for the purchase of cars and other consumer loans (including those through credit cards).

It is also possible that, in the future, non-financial corporations as well will securitise receivables, given that this is permitted by the relevant law. A special case, explicitly provided for in the law, is the securitisation of receivables relating to the management and exploitation of real estate.

V. The stability of the financial system

The social and economic importance of the stability of the financial system is clear. The stability of the Greek financial system depends to a great extent on the stability of the banking system, as bank intermediation plays a dominant role and banks are major players in payment systems and money and capital markets, either directly or indirectly, through their insurance, securities and mutual fund management subsidiaries.

Hence, the analysis that follows focuses on the evaluation of the stability of the banking system. This evaluation includes an examination of, on the one hand, the nature and magnitude of the risks assumed by banks in relation to possible developments in the economic environment and, on the other hand, the profitability and capital adequacy of banks (i.e. the aggregates that determine banks' ability to cope safely with possible adverse, risk-enhancing developments).

1. Credit risk

Credit risk is the major risk facing Greek banks, as well as most banks globally. Its magnitude depends, on the one hand, on banks' credit policy and, on the other hand, on borrowers' financial condition, which is also connected with developments in the overall economic environment. In a period of low interest rates and strong competition, with narrowing margins between interest rates on assets and the cost of funds, banks' shift to higher-yield assets typically implies higher credit risk, which should be taken into account in the formulation of their credit policy.

1.1 Credit risk arising from loans to households

As a result of continuing strong credit expansion to households, notably through consumer loans, total bank lending to households rose to 31.4% of nominal GDP at end-2004, compared with 26.3% at end-2003; yet this rate is still considerably lower than the euro area average (50.3%). However, strong credit expansion to households may lead to increased credit risk, to the extent that certain recently granted loans may present servicing problems that had not been foreseen when the loans were granted on the basis of the banks' credit standards. This may happen notably if there is a slowdown in economic activity, which affects households' disposable income. Hence, on the one hand banks' credit standards should be tightened, so that competition does not lead to the assumption of excessive risks, and, on the other hand, households should evaluate carefully the total amount of their loans in relation to their income prospects. Besides, as interest rates have reached historic lows, any future increase will affect unfavourably the ability of households to service their loans, since in Greece consumer loans and the majority of housing loans are typically floating-rate loans.[1]

By contrast, with respect to fixed-rate loans, interest rate changes as a rule do not affect credit risk. However, they may affect interest rate risk where such loans have been financed by borrowing funds with variable interest rates subject to short-term readjustment. In addition to interest rate changes, credit risk is also directly influenced by developments in residential property prices, as the value of the relevant collaterals changes. Residential property prices have recently tended to stabilise, following a period of continuous rise, which may be largely accounted for by lower interest rates and higher income growth. Although a future fall in residential property prices in certain segments of the market cannot be ruled out, the possibility of a substantial correction is limited, especially if economic developments are in line with the relevant forecasts. Until recently, the amount of housing loans typically did not exceed 75% of the market value of real estate. However, there have been some recent indications that certain banks, under the pressure of competition, actually finance a higher proportion of this value. This usually happens when a property is used to secure both a loan for house purchase or construction and a repair loan or a consumer loan granted to the same borrower. Hence, the Bank of Greece has recommended that banks contain total lending to each borrower as a percentage of the market value of real estate collaterals.

1.2 Credit risk arising from loans to enterprises

The pace of credit expansion to enterprises falls considerably short of that to households and overall appears to be relatively stable, albeit with marked differences across sectors. Thus, for the business sector as a whole, the pace of credit expansion does not seem to be in itself a potential credit risk-enhancing factor for banks. As mentioned in Chapter III.1, the recovery of business profitability observed in 2003 continued in 2004. However, as the relevant data are aggregated and mainly concern major Greek firms, it is not certain that the relatively optimistic conclusions derived therefrom hold true for all sectors and for small and medium-sized enterprises in general. This is especially so when one takes into account the considerable increase in the value of unpaid cheques in 2004 (33% over 2003). Moreover, despite a rebound in corporate profitability, in 2003 the net pre-tax profits to total liabilities ratio, which is a measure of a firm's ability to service its outstanding obligations, was below the reasonable level of 10% for 59% of all non-financial corporations listed on the Athens Exchange.

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1 It should be pointed out, however, that the impact on households from a possible increase in interest rates is mitigated to the extent that certain banks offer loans with flexible servicing schedules, a possibility to shift from a floating- to a fixed-rate loan without considerable costs, as well as protection (with the use of financial derivatives) from interest rate increases beyond a certain limit.

1.3 Credit risk measurement and management

Credit risk developments are reflected in the *ex post* data on non-performing loans, while some indications of increased credit risk are provided by the rise in on- and off-balance-sheet credit-risk-weighted assets. Specifically, while the non-performing loans to total loans ratio of purely commercial Greek banks[2] was virtually unchanged between 31 December 2003 and 30 September 2004, there were differences across the main categories of loans (a small decline in consumer and housing loans and a small increase in corporate loans). The net non-performing loans (less provisions) to total loans ratio and the net non-performing loans (less provisions) to own funds ratio for purely commercial banks as a whole were also stable in the same period (at 2.1% and around 16% respectively), while the provisions to non-performing loans ratio rose slightly (from 57.7% to 59%). It should be noted, however, that, over the short term, the non-performing loans to total loans ratio is favourably affected by the continuing strong credit expansion and that this ratio remains more unfavourable than the euro area banks' average, although data comparability problems exist. The on- and off-balance-sheet credit-risk-weighted assets of Greek banks, on a non-consolidated basis, increased by 9.4% between 31 December 2003 and 30 September 2004; as a result, they rose to 59% of unweighted assets on the latter date, from 57% at end-2003 (compared with 43% for the euro area as a whole at end-2003). This development reflects the diversification of bank assets, as the percentage of assets (mainly loans) that carry high credit risk weights rose and the percentage of assets (mainly bonds) that carry low or zero credit risk weights dropped.

In recent years Greek banks have improved considerably their credit risk measurement and management systems. Many banks apply credit scoring models for the approval of consumer loans, while some banks have developed probability of default models. The development of similar systems and their integration into the decision-making process are necessary conditions for the adoption of the internal-ratings-based approach for the calculation of capital adequacy against credit risk under the new supervisory framework ("Basel II"). However, banks that opt for the simpler, standardised approach also ought to adjust their systems accordingly, because they will thus be better placed to manage risks effectively in an environment of strong competition and economic uncertainty. Generally, the upgrading of credit risk measurement and management systems improves the readiness of Greek banks for the timely and efficient management of the increased credit risk arising from possible unfavourable developments.

2. Market risks

Interest rate changes affect both the net income and the net worth of banks. An increase affects unfavourably net interest income to the extent that the rates on banks' placements are adjusted slower than the rates on the borrowed funds used to finance such placements. The banks' net worth is mainly influenced by the adjustment at current values of their positions in financial derivatives on debt securities and interest rates, while loans and deposits are generally not subject to adjustment. As regards net loan interest income, interest rate risk may increase in the future because certain banks, pressed by the inadequate growth of their customers' deposits, have already been forced to finance their strong credit expansion with bor-

2 I.e. excluding the Agricultural Bank of Greece.

rowed funds raised through the markets, which are more sensitive to interest rate changes. Besides, as regards the banks' trading portfolio items that are subject to interest rate risk, the rise in the relevant capital requirements points to increased risk from interest rate changes, which influence directly both the net profits and the net worth of banks. In particular, as regards general position risk from interest rate changes, it should be pointed out that the relevant capital requirements on a non-consolidated basis for all the commercial banks that use the standardised approach rose by 44.9%, from €105.7 million on 31 December 2003 to €153.1 million on 30 September 2004, but remain at a low level.

As regards equity prices, the continuation of the upward trend of the Athens Exchange composite index since September 2004 is characterised by uncertainty and will mainly depend on future developments in the profitability of listed companies and in international equity markets. Changes in equity prices lead to revaluations of banks' trading portfolio equities; as a result, both the income and own funds of banks are influenced, whereas investment portfolio equities, mainly including participations in affiliates and associated companies, are not subject to revaluation as from 1 January 2005 under the International Accounting Standards. It should be noted, however, that capital requirements for the trading portfolio equity risk facing the banks that use the standardised approach are relatively limited: on 30 September 2004 they made up only 8% of capital requirements on these banks for market risks. Any future fall in equity prices and in the volume of transactions on the Athens Exchange will have an impact mainly on banks' income from commissions and fees from financial operations.

Following the adoption of the euro, the foreign exchange risk for Greek banks has declined substantially; therefore, any changes in the euro/US dollar exchange rate should not have a material impact on their financial condition.

With respect to both credit and market risks, the Bank of Greece considers that, in addition to meeting the minimum capital requirements under the current institutional framework, banks should also ensure that their own funds provide an adequate cushion for absorbing the impact of unforeseen adverse developments. Therefore, banks should regularly carry out stress testing. To this end, they have been requested to calculate the impact on their capital position from specific hypothetical scenarios including substantial downgradings of their loan portfolios, interest rate increases, equity price declines and changes in the euro exchange rate. The possibility of a materialisation of these hypothetical changes and indeed on a cumulative basis is certainly limited, but the quantification of their impact leads to useful conclusions on the banking system's resilience to shocks.

3. Profitability and capital adequacy

As already mentioned, banks' ability to weather adverse developments hinges on their profitability and capital adequacy. The net pre-tax profits of all the Greek commercial banks listed on the Athens Exchange showed a limited increase (of 2.5%) in the January-September 2004 period over the same period in 2003, owing to unfavourable developments in the results of a small number of banks. The income increase was due to higher net interest and commission income, as well as to a large percentage rise in income from equity participations and variable-yield securities, while net income from financial operations showed a substantial decline. Besides, total operating costs grew by 5.6% in the January-September 2004 period over the same period in 2003; thus, the operating efficiency (measured by the cost-income ratio) of Greek banks listed on the Athens Exchange improved from 60.8% to 59.7% (compared with an average of 62.3% for euro area banks as a whole in 2003). Provisions grew substantially (by 33.2%), offsetting the favourable effect on net profits from the containment of operating expenses. On an annual basis, the return on assets (ROA) and return on equity (ROE) ratios reached 0.9% and 13.5% respectively in the January-September 2004 period, remaining almost unchanged from 2003, when they had exceeded the averages for euro area banks as a whole (0.5% and 11.9% respectively). Focusing on the results of the five largest commercial banks (excluding the Agricultural Bank of Greece), which make up 79% of the banking sector's assets, the conclusions are definitely more optimistic. Specifically, the net pre-tax profits of these banks rose by 19.2% in the January-September 2004 period over the same period in 2003; as a result, their annualised ROA and ROE for this period reached 1.1% and 15.9% respectively (compared with 1% and 14.8% respectively in 2003).

Broadly speaking, after three years of continuous decline, the rebound in the Greek commercial banks' profitability observed since 2003, stemming mainly from the growth of operating profits, enhances the stability of the banking system, provided that this growth is accompanied by a conservative dividend policy. Euro area banks as a whole also showed increased profitability in 2003 over 2002. According to available data, this rise continued in 2004, largely as a result of a decrease in operating costs and loan-loss provisions.

The total capital adequacy ratio (CAR) of Greek commercial banks, on a non-consolidated basis, came to 13.3% on 30 September 2004, slightly exceeding its average for the 2001-2003 period, during which it was also relatively high (13%). Taking into account the shortfall of actual provisioning against the provisioning requirements under Bank of Greece Governor's Act 2442/1999, as currently in force, this ratio falls by 0.6 percentage point. The rise in the CAR in 2004 was a result of a 12.5% increase in supervisory own funds between 31 December 2003 and 30 September 2004, while risk-weighted assets rose by 8.5% during the same period. The composition of supervisory own funds is characterised by a decline in the share of core capital (Tier I capital) over time and a commensurate increase in the share of supplementary capital (Tier II capital), which mainly includes subordinated loans. If only core capital is included, the CAR was 9.8% on 30 September 2004, still higher than the average for euro area banks as a whole (8.7% at end-2003). This reflects the improved quality of the composition of the Greek banks' own funds.

In conclusion, in the current circumstances, the Greek banks' CAR provides an adequate cushion for safeguarding the stability of the banking system and exceeds the average for euro area banks as a whole (11.9% in 2003). However, account should be taken of the impact on own funds from the implementation of the International Accounting Standards (IAS) as from 1 January 2005, notably of IAS 19, which requires that liabilities arising from defined-benefit plans for bank employees be recognised on the banks' balance sheets. While the CAR of the banking system as a whole is not expected to be affected considerably, certain banks should strengthen their capital base to restore their capital adequacy. Furthermore, the implementation of the new capital adequacy framework (''Basel II'') as from 31 December 2006 will have repercussions on the banks' CAR, the overall magnitude of which will depend on the methods for calculating capital requirements to be adopted by banks, as well as on the composition and quality of their loan portfolios, in conjunction with the evolution of the business cycle. Given the uncertainty surrounding these factors, banks should increase their own funds, notably by allocating profits to reserves and by raising hybrid and supplementary capital within reasonable limits, provided that they have not reached the respective ceilings set by the regulatory framework.

4. Insurance sector

As regards the insurance sector, any serious problems facing insurance companies may have wider implications to the extent that they limit the scope of insurance coverage or lead to excessive increases in insurance premiums. Therefore, there may be some implications for the smooth execution of certain transactions, notably the supply or the cost of bank loans where the borrowers are required to obtain insurance coverage for themselves or for the collaterals they provide. Furthermore, as regards insurance products that constitute households' assets, any insolvency of the insurance companies may affect the consumption and investment pattern of the insured. However, taking into account that in Greece both the amount of insurance companies' investment in negotiable instruments in relation to the size of the capital market and the amount of banks' financial exposures to insurance companies in relation to banks' own funds are small, the systemic risk associated with spillovers from the insurance sector to the financial sector as a whole is estimated to be low.

According to aggregated data on the Greek insurance sociétés anonymes, in 2003 their fundamentals showed an improvement over 2002, which, on the basis of the evidence so far available, continued in 2004. Specifically, in 2003 insurance companies as a whole recorded *profits*, compared with substantial losses in 2002 (2003: pre-tax profits of €92.2 million, 2002: losses of €220.3 million). Moreover, the number of loss-making companies as a proportion of the total number of companies fell (from 40% to 20%), while own funds rose by 36%, to reach €1,434.2 million at end-2003 (2002: €1,054.7 million). As a result, the ROE turned out at 7.4% in 2003, compared with a negative ROE in 2002.[3] Finally, the own funds to total insurance provisions ratio, which is a measure of the economic robustness of insurance companies, improved to 27% in 2003, from 21.5% in 2002, but is still low.

The recent establishment, by Law 3229/2004, of an independent supervisory authority for the insurance sector is expected to contribute to a more effective supervision of private insurance companies. Furthermore, if cooperation between this authority on the one hand and the Bank of Greece and the Capital Market Committee on the other is legally established, this will help considerably the coordination of action between the supervisory authorities with a view to ensuring the stability of the financial sector and increasing the effectiveness of the supervisory treatment of bankassurance products offered by banks in cooperation with insurance companies.

5. Securities companies sector

The turnover of securities companies grew by 11% in 2003, after a 26% fall in 2002, while the own funds to total assets ratio declined slightly to 36% in 2003, from 37% in 2002. Besides, the need to strengthen the capital base of certain companies,

3 As regards the life insurance sector in particular, gross operating results showed an increase of €196.8 million or 371%, mainly accounted for by a rise in income from investment, which more than offset a small decrease in accrued premiums ("retained risk"). However, the problem caused in an environment of low interest rates by old insurance policies with relatively high guaranteed yields persists. As regards the non-life sector, gross operating results showed an increase of €117.1 million or 92%, which is accounted for by a rise in income both from investments and from accrued premiums (retained risk).

notably the smaller ones, and to cope with the challenges from competition in the context of the ongoing integration of the European capital market has encouraged M&A activity in recent years. This activity is expected to continue, as in Greece the securities brokerage market is still characterised by a large number of companies in comparison with other European markets. Thus, further concentration of operations and income is expected, which should make a positive contribution to the overall financial robustness of the sector.

Credit extended by securities companies to their customers grew to €156.9 million at end-2004, from €140.5 million at end-2003 and €83.6 million at end-2002. However, the value of the collaterals that back those credits also rose commensurately; as a result, the coverage ratio of credit granted by these companies remained virtually unchanged at 350% between end-2003 and end-2004. Besides, on the basis of data on borrowers with debts of €1.5 million or higher each, total bank finance (loans, investment in debt instruments, letters of guarantee in force) of securities companies rose from €161 million at end-2003 to €250.1 million on 30 June 2004. However, given that at the latter date this finance did not exceed 1.7% of the own funds of all banks, it is estimated that it does not represent a potential risk to the banking system.

6. Payment systems

Payment systems continued to operate smoothly, contributing substantially to the maintenance of financial stability.

The average availability of the HERMES system[4] remained high in 2004. The monthly availability ratio was higher than 99%, reaching 100% in nine out of twelve months in 2004. The annual average ratio came to 99.80%, as it was influenced marginally by four short interruptions owing to technical reasons, which did not affect the smooth operation of the system.

The smooth flow of payments is helped by the adequacy of intraday liquidity provided by the Bank of Greece. An analysis of data shows that the value of collaterals provided was satisfactory, exceeding the system's requirements throughout the year. Specifically, the average daily value of collaterals was €1,547.6 million, while the average value of intraday credit rose to €411.6 million, providing an adequate margin for covering any increased liquidity requirements of member credit institutions.

An important move towards the improvement of the real-time gross payment infrastructure is the Eurosystem's decision to develop TARGET2, a new trans-European payment system to replace TARGET. Under TARGET2, credit institutions in all the EU Member States will enjoy the same services and those that have branches in more than one countries will be able to manage effectively the overall liquidity they maintain at the respective national central banks. HERMES member credit institutions will further benefit from the pricing of services under the new system, as higher effectiveness will lead to lower prices per operation than under the current system.

The DIAS S.A. systems and the Athens Clearing Office, which make up the main infrastructure for retail payments clearing, also continued to operate smoothly in 2004.

However, the end-consumer's cost for small fund transfers, despite having apparently decreased

4 The Greek real-time gross settlement system, which is an integral part of the Trans-European Automated Real-time Gross settlement Express Transfer system (TARGET).

since Greece joined EMU, is still relatively high. Although banks have integrated modern technologies into their operations, they do not seem to have taken full advantage of their potential, nor of that of the DIAS S.A. infrastructure, to expand automated operations and reduce operating costs.

The creation of a single payment area in euro by 2010, where payments will be effected more easily and economically through an account kept by the participant with any euro area credit institution, should enhance competition in small payments and possibly affect other retail banking operations. In this context, the need for banks to develop a strategic plan for taking full advantage of economies of scale in infrastructure and limiting the cost of retail payments is all the more pressing.

Appendix to Chapter V

Adjustment of provisioning ratios (Bank of Greeece Governor's Act 2557/26 January 2005)

By Bank of Greece Governor's Act 2557/26 January 2005, the Bank of Greece adjusted credit institutions' minimum provisioning ratios for certain categories of loans (earlier relevant Bank of Greece Governor's Acts: 2442/29 January 1999 and 2513/15 January 2003). The minimum provisioning ratios for credit risk are determined exclusively for supervisory purposes and are taken into account in the evaluation of the capital adequacy of credit institutions.

Specifically, this Act:

— increased the provisioning ratios for all types of consumer loans as follows: (i) from 70% to 90% for non-performing loans one year past due or in permanent arrears; and (ii) from 84% to 100% for doubtful loans;

— reduced the provisioning ratios for performing loans backed by residential mortgages from 0.7% to 0.5%, provided that the value of the loan does not exceed 70% of the objective value of the residential property.

The amounts resulting from the above adjustment of provisioning ratios will be taken into account in the evaluation of the capital adequacy of credit institutions by 50% on the data reported on 31 March 2005 and by 50% on the data reported on 30 September 2005.

This adjustment was deemed advisable because:

1. It is considered that the possibility of losses from consumer loans one year past due has increased, as the growth rate of consumer loans, which far exceeds the growth rate of the other types of loans, is a determinant of the quality of the credit institutions' portfolios. This adjustment also aims to encourage banks to write off their doubtful loans instead of maintaining them on their balance sheets.

2. It is recognised that the credit risk associated with performing loans backed by residential mortgages is reduced in relation to the corresponding provisions, calculated with the currently applicable ratios. The recognition that credit risk from performing mortgage-backed loans is reduced is also consistent with the revised capital adequacy framework ("Basel II" and the corresponding draft Community Directive), in cases where the ratio of the loan amount to the residential property value does not exceed a reasonable limit.

The generally applicable provisioning framework does not relieve banks of their obligation to regularly re-evaluate their credit standards and continuously upgrade their credit risk management systems.

Follows the text of Bank of Greece Governor's Act 2557/26 January 2005:

Amendment to Bank of Greece Governor's Act 2442/29 January 1999 "Adequacy of credit institutions' provisioning coverage of loans", as currently in force

The Governor of the Bank of Greece, having regard to:

a) the provisions of the Statute of the Bank of Greece, notably Article 55A, as currently in force;

b)Article 1 of Law 1266/1982 ''Authorities responsible for the conduct of monetary, credit and exchange rate policies, and other provisions'', taken together with Article 12, par. 1 of Law 2548/1997;

c) Article 18 of Law 2076/1992 ''Taking up and pursuit of business of credit institutions, and other relevant provisions'', as amended by Article 38, par. 3 of Law 2937/2001;

d) Bank of Greece Governor's Act 2442/29 January 1999 "Adequacy of credit institutions' provisioning coverage of loans'', as amended by Bank of Greece Governor's Act 2513/15 January 2003;

e) Bank of Greece Governor's Act 2054/18 March 1992 "Solvency ratio of credit institutions established in Greece", as currently in force;

f) Bank of Greece Governor's Act 2523/12 June 2003 on consumer credit and personal loans;

g) Circular 412/12 May 2003 of the Department for the Supervision of Credit and Financial Institutions, providing instructions and clarifications on the implementation of the above Acts for the calculation of provisions;

h) the advisability of adjusting the minimum provisioning ratios for certain categories of loans;

i) the fact that the applicable provisioning framework does not relieve credit institutions of their obligation to develop risk management systems;

has decided to amend the provisions of Bank of Greece Governor's Act 2442/29 January 1999, as currently in force, as follows:

1. The minimum provisioning ratios set forth in par. 1 of Bank of Greece Governor's Act 2442/29 January 1999, as currently in force, applying to loans to natural persons according to Bank of Greece Governor's Act 2523/2003, shall be increased as follows:

(i) from 70% (as it resulted after the increase provided for by par. 3 (b) of Bank of Greece Governor's Act 2513/15 January 2003) to 90% for loans under categories (d) and (e) of par. 1 of Bank of Greece Governor's Act 2442/29 January 1999, as currently in force; and

(ii) from 84% (as it resulted after the increase provided for by par. 3 (b) of Bank of Greece Governor's Act 2513/15 January 2003) to 100% for loans under category (f) of par. 1 of Bank of Greece Governor's Act 2442/29 January 1999, as currently in force.

2. The minimum provisioning ratios that apply, under par. 1 (a) of Bank of Greece Governor's Act 2442/29 January 1999, to the balances of performing loans backed by residential mortgages shall be reduced from 0.7% (as it resulted after the reduction provided for by par. 3 (a) of Bank of Greece Governor's Act 2513/15 January 2003) to 0.5%, subject to the conditions of par. 3 (a) of Bank of Greece Governor's Act 2513/15 January 2003.

3. The amounts resulting from the adjustment of provisioning ratios under par. 1 and 2 above shall be taken into account in the evaluation of the capital adequacy of credit institutions as follows: by 50% on the data reported on 31 March 2005 and by 50% on the data reported on 30 September 2005.

VI. Economic prospects and challenges for economic policy and the social partners

1. Economic prospects

As discussed in Chapter III, Greece's growth rate is expected to slow down in 2005, but to remain markedly higher than the euro area average, while year-on-year inflation is projected to increase slightly, after decelerating in 2004 owing to extraordinary exogenous factors. Core inflation will remain broadly unchanged but will once again exceed the euro area average, thereby resulting in a further weakening of Greece's price competitiveness. Achieving strong and sustainable growth requires intensified efforts to safeguard macroeconomic stability, improve productivity and enhance external competitiveness. Specifically, there is a need for a determined and sustained effort to attain fiscal consolidation, for wage increases that will be in line with productivity gains and for wide-ranging structural reforms.

Based on the assumptions detailed in Chapter III.3, which are characterised by a high degree of uncertainty, real GDP is projected to rise by about 3.3% in 2005, compared with 3.8% in 2004 and an average annual rate of 4.2% over the last five years. Some of the factors that had sustained growth in the past several years will stay in place in 2005. The rise in private consumption is projected to remain the chief source of domestic demand and output growth, though it will decelerate slightly compared with 2004. Private consumption growth is expected to be driven by higher household income, the increase in consumer loans and the cumulative rise in the market value of households' assets in recent years. Private investment is also projected to contribute positively to growth, on the assumption that business investment will continue to expand (mainly as a result of the newly introduced incentive package), while residential investment should remain broadly at last year's level. In addition, as indicated by the latest world economic outlook estimates, export growth —especially in the services sector— should continue at a relatively robust pace. In contrast, general government investment —after being boosted by Olympic Games-related projects in 2003-04— is projected to decline, reflecting in part the need for fiscal consolidation. The same reason is expected to cause a sharp deceleration in public consumption growth. These projections are surrounded by considerable uncertainty, associated with oil price developments and the prospects for private investment. With regard to this last item in particular, it remains to be seen whether —in spite of the favourable influence of the factors referred to in Chapter III.3— the almost steady deterioration of certain confidence indicators in recent months[1] will adversely influence investment decisions.

Despite the rise in economic activity, employment is expected to pick up only modestly, thus keeping the unemployment rate high. The projected small increase in employment is attributable to the anticipated contraction of the labour-intensive construction sector, the restrictive hiring policy in general government (as part of the fiscal consolidation effort) and early retirement schemes in several banking institutions and large public enterprises.

The current account deficit —though expected to narrow further (after improving considerably in 2004)— should remain relatively large, mainly as a result of Greece's structural weaknesses and continued loss of price competitiveness. The favourable external environment is expected to further boost the demand for commercial shipping, Greece's internationally most competitive sector, while travel receipts should be buoyant in the wake of the Olympic Games. Although exports of goods are also expected to benefit from a favourable external environment, weak external competitiveness will lead to further losses in export market shares. Meanwhile, import growth is expected to slow down markedly in 2005, after reaching a high level in 2004, owing in part to the high import content of Olympic Games-related projects and other spending.

HICP inflation is projected to rise slightly, from 3.0% in 2004 to 3.3% in 2005 (on an average annual basis) – as a result of a small recovery in fresh fruit and vegetable prices, which reached a low level in 2004 (thus exerting downward pressure on inflation). In contrast, according to the latest crude oil price projections, fuel prices on the domestic market are expected to increase less this year than in 2004, thus accounting for a smaller direct contribution to inflation than in 2004. Core inflation, as measured by the HICP excluding energy and unprocessed food, is expected to remain roughly unchanged in 2005. The slowdown in growth of domestic demand and unit labour costs will have a downward effect on consumer prices, which, however, will be counteracted by the upward effect of certain other factors. Import prices should contain inflation to a lesser extent than in 2004, as, in line with the technical assumption used, the average annual appreciation of the euro in 2005 will be smaller than in 2004.[2] Moreover, it is estimated that some of the indirect effects of the 2004 fuel price increase on the prices of goods and services failed to materialise fully during 2004 and will therefore materialise with a lag in 2005.

1 As mentioned in Chapter III.3, the economic sentiment indicator (calculated by the European Commission) has declined almost continuously since April 2004, in spite of a small recovery in January of this year.
2 The technical assumption was made that the exchange rates between the major currencies recorded in the last ten days of January 2005 will remain unchanged throughout the rest of the year (see Chapter III.2).

2. Economic policy challenges and stance

The performance of the Greek economy has improved considerably since the early 1990s, as evidenced by the near 36% rise in per capita GDP over the past ten years. This outcome was made possible by the improved macroeconomic environment, which also enabled Greece to join the euro area, and by lower borrowing costs, as both factors helped stimulate private consumption and investment. Investment growth was also boosted by the large inflow of resources from the EU Structural Funds, which served to improve public infrastructure, and by measures targeted at reforming the product, labour, and capital markets. Rising government spending associated with the 2004 Olympic Games also contributed to the growth of domestic demand in the past few years.

Significant policy adjustments will be needed to ensure continuation of strong growth performance over the medium and longer terms. The central government deficit and debt, which reached very high levels relative to GDP in 2004,[3] are clearly unsustainable, even without taking into account the projected sharp rise in pension and health spending associated with post-2010 demographic developments. In addition, the rise in private consumption, though likely to remain an important source of growth for a few more years, will inevitably decelerate over the medium term, as household indebtedness will gradually increase and tend to stabilise as a percentage of GDP. Moreover, given the cumulative loss in competitiveness over the last several years, export growth (mostly in the services sector) has largely been sustained by the favourable external environment, which, though expected to remain favourable in 2005, is characterised by a high degree of uncertainty over the medium term, related to developments in oil prices, transport fares and world trade. In any event, the current favourable external environment is not likely to be sustainable over the medium term. For these reasons, it is of crucial importance to adopt economic policy measures fostering investment and export-led growth. These measures would need to include a determined and sustained fiscal consolidation effort and structural reforms to remove market rigidities and enhance external competitiveness, while wage increases would have to be in line with productivity gains. Unless these problems are addressed promptly, investor confidence and macroeconomic stability will be jeopardised.

Fiscal policy

Greece's fiscal imbalances have once again been exacerbated, with the fiscal deficit and public debt, at above 5.3% and 112% of GDP respectively in 2004, reaching the highest levels in the euro area.

Specifically, whereas initial forecasts (in the 2004 budget) had placed the general government deficit for 2004 at 1.2% of GDP, later estimates (in autumn 2004) revised this figure upwards to 5.3% of GDP.[4] According to 2004 cash-basis data, however, it is estimated that the deficit will in fact exceed 5.3% of GDP. The main reasons behind the overshooting of the deficit target are: (a) the upward revision of the deficit for 2003, which had a "base" effect on the 2004 deficit, (b) the very optimistic forecasts of the 2005 budget, (c) the "fiscal audit", which revised the figures for 2004 upwards, (d) shortfalls in ordinary budget revenue and EU fund inflows and (e) considerable over-

3 The Ministry of Economy and Finance and the National Statistical Service of Greece (NSSG) have not yet finalised their estimates for 2004.

4 These revised estimates were made on the basis of data reported at end-August under the Excessive Deficit Procedure and also used for the preparation of the draft state budget for 2005.

runs in expenditure (for wages and pensions, for the preparation and conduct of the Olympic Games, for transfers and for the restitution of revenue collected on behalf of third parties).

In particular, budget revenue[5] in 2004 was projected last autumn to be €1,493 million (or 0.9% of GDP) lower than budgeted, as a result of shortfalls in both ordinary budget tax receipts and inflows from the EU Structural Funds. However, the data available for the January-to-November period suggest that the actual shortfall in 2004 ordinary budget revenue must have been considerably larger, which is the main reason why the 2004 deficit is estimated to have exceeded 5.3% of GDP. On the expenditure side (excluding the outlays for the Olympic Games), the overrun was recorded at the ordinary budget primary expenditure level and —according to the autumn 2004 estimates— amounted to as much as €3,000 million or 1.8% of GDP. Overall, according to the same estimates, the slippages in budget implementation widened the deficit by an additional 2.7% of GDP (thus raising it to 5.3% of GDP).

With regard to government expenditure for the 2004 Athens Olympic Games, investment outlays exceeded by €850 million the corresponding provisions in the public investment budget, while financing from the ordinary budget exceeded initial forecasts by €297 million. Overall, according to the autumn 2004 revisions, the overrun in expenditure for the Olympic Games —which largely involved the much higher-than-forecast security expenditure— raised the deficit by €1,147 million or 0.7% of GDP.

Finally, following the fiscal audit, additional military expenditure equivalent to 0.4% of GDP was recorded (based on the dates of payment), while a special survey by the National Statistical Service of Greece (NSSG) showed that the surplus of public entities (mainly of social security organisations) had been overestimated by 0.3% of GDP.[6] Thus, the fiscal audit contributed to a 0.7% of GDP widening of the general government deficit recorded in 2004.

Therefore, roughly two-thirds of the deficit widening for 2004 (relative to the target initially set) is attributable to slippages in budget implementation (mainly primary expenditure overruns), while the extra spending for the Olympic Games and the data revisions made under the fiscal audit accounted for the remaining one-third. It goes without saying that the slippages in budget implementation reflect both fiscal management and overly optimistic initial state budget estimates.

The large fiscal imbalances are one of the more important and urgent problems that the Greek economy faces today. A large reduction in the fiscal deficit in 2005 and 2006 and sustained fiscal adjustment effort in the following years are therefore necessary to control the fiscal imbalances on a more durable basis and to achieve a budget surplus and a steady and significant decrease in the public debt in the long term. Fiscal consolidation is a top priority if Greece wants to create a stable macroeconomic environment, which is an essential prerequisite for achieving strong growth, and also because public expenditures will rise in the coming years on account of population ageing (according to estimates, the fiscal pressures from population ageing in Greece will be the most severe in the euro area). Unless the fiscal imbalances are addressed decisively, there will be adverse consequences for the viability of the social security and healthcare systems and for the

5 Based on data for 2004 contained in the Introductory Report on the State Budget for 2005.
6 The surplus of public entities is subtracted from the central government deficit in order to determine the general government deficit.

economy as a whole. By contrast, early progress in correcting fiscal imbalances will help safeguard social security and healthcare benefits, as well as the quality of public services within an environment of a stable and growing economy. Fiscal adjustment is also imperative if Greece is to fulfil its obligations under the Stability and Growth Pact and the Excessive Deficit Procedure in accordance with Article 104 of the Maastricht Treaty (see Box VI.1). It is essential that Greece complies with the ECOFIN Decision of 17 February 2005 but, more generally, it must also comply in full with the rules laid down in the Stability and Growth Pact in order to safeguard its credibility.

Fiscal consolidation must be based on measures that improve the fiscal position on a sustainable basis and, at the same time, enhance economic efficiency and growth prospects. Specifically, the fiscal adjustment effort should mainly rely on a strict control and re-assessment of current expenditure priorities, a widening of the tax base and a

BOX VI.1

The Excessive Deficit Procedure for Greece

The new data reported to Eurostat by the Greek authorities in early May 2004 on the general government deficit and debt, which revised the 2003 deficit upwards to 3.2% of GDP, prompted the European Commission to initiate the Excessive Deficit Procedure for Greece on 19 May.[1]

At the end of August, Eurostat received Greece's revised data which further raised the *2003* deficit to 4.6% of GDP (from 3.2% in May), along with updated estimates which raised the projected *2004* deficit to 5.3% of GDP (from 2.9% projected in May). It thus became obvious that the Recommendation issued by the ECOFIN Council on 5 July 2004 calling upon the Greek authorities to reduce the deficit by one percentage point of GDP was no longer sufficient to bring the deficit ratio back below the 3% of GDP reference value set out in the Maastricht Treaty and to make progress towards achieving a budgetary position close to balance or in surplus. In addition, Greece could not meet the other term of the Recommendation, i.e. the obligation to lower its deficit by 0.5% in 2004 and an additional 0.5% in 2005, since the latest estimates now indicated that the 2004 deficit would widen to 5.3% of GDP, from 4.6% in 2003.

In line with Article 104(7) of the Treaty,[2] a deadline was set for 5 November 2004 for the Greek authorities to submit a report to the European Commission outlining the deficit reduction measures. Within this time limit, the Greek authorities informed the Commission about the adoption of the following measures, which had already been incorporated into the state budget for 2005:

(a) various settlements[3] of tax obligations (Law 3259/2004),

(b) expenditure savings made possible by the completion of the Olympic Games,

(c) curtailment of public investment budget expenditure,

(d) a restrained incomes policy and restrictive public sector hiring, and ➔

1 For details on the initiation of the Excessive Deficit Procedure for Greece and the Recommendation issued by the Council, see Bank of Greece, *Monetary Policy, Interim Report 2004*, October 2004, pp. 79-80.
2 The legal framework that governs the Excessive Deficit Procedure consists of: (a) the Maastricht Treaty, Article 104, (b) Protocol 5 annexed to the Treaty and (c) the Decision adopted by the Amsterdam European Council on 17 June 1997, which —together with Council Regulations (EC) 1466/97 and 1467/97— make up the Stability and Growth Pact.
3 Including the settlement of pending tax cases for fiscal years 1999-2002, the collection of debts overdue to the State, new deadlines for submitting overdue tax returns without incurring a late-filing penalty, and arrangements to encourage capital repatriation.

➔ (e) a reduction in interest payments.[4]

All these measures concern 2005[5] and, according to the Ministry of Economy and Finance, should reduce the general government deficit by 2.5 percentage points to 2.8% of GDP in 2005.

After analysing and assessing the above measures, the European Commission concluded in its report to the Council of 22 December that Greece had not taken effective action to correct the excessive deficit of 2004, even after taking into account the effects of the statistical revisions and the expenditure overruns associated with the organisation of the Athens Olympic Games.[6] The Commission also noted that these measures, albeit in the right direction, were nonetheless insufficient to bring the deficit below the 3% threshold by end-2005. The Commission thus recommended to the Council to take the relevant decision.

The ECOFIN Council, in its meeting of 18 January 2005, acknowledged that the Greek government had implemented measures aimed at curbing the rising deficit in 2004 and at significantly reducing it in 2005. Nevertheless, acting on the recommendation of the Commission, it decided that Greece had not taken effective action to bring its deficit back below 3% of GDP, as recommended by the Council on 5 July 2004. Although the fiscal conditions specific to Greece in 2004 (Olympic Games, data revision, etc.) were taken into account, the Council ruled that, given the high deficit outturn in 2004, as well as the uncertainty surrounding fiscal prospects for 2005, the excessive deficit was not likely to fall below the 3% reference value stipulated in the Treaty. The Council nonetheless noted with satisfaction the commitment of the Greek government to reducing its deficit in order to reach the objective of a close-to-balance or in-surplus position in the medium term.

Following this decision of the ECOFIN Council, Greece came under the provisions of Article 104(8) of the Treaty, which differ from the provisions of Article 104(7) only in that the Council decision becomes public.[7] The European Commission then prepared a Report and a proposed recommendation to the Council. Indeed, on 17 February the Council adopted a Decision under Article 104 (9) of the Treaty recommending measures for Greece to correct its excessive deficit. Specifically:

(a) Given the large magnitude of the fiscal adjustment needed to fully correct the situation by end-2005, the Council decided to extend by one year, i.e. to the end of 2006, the deadline set in the July 2004 recommendation for bringing the deficit below the 3% reference value.

(b) The Council welcomed the commitment of the Greek authorities to implement the 2005 budget strictly and to adopt adjustment measures of a permanent nature in 2006, which should lead by year-end to a deficit reduction of at least 0.6% of GDP.

(c) The Council welcomed the initiative of the Greek authorities to submit as soon as possible, and by 21 March 2005 at the latest, an updated Stability and Growth Programme.[8] The Programme —which will be evaluated by the Commission and the Council to assess compliance with the measures required by the Stability and Growth Pact— must place emphasis on the fiscal measures intended to bring the deficit below the 3% margin by end-2006 and on the fiscal consolidation measures needed to reach a close-to-balance or in-surplus position in the medium term, by improving the cyclically adjusted fiscal balance by at least 0.5% of GDP per year after the excessive deficit has been corrected (i.e. after 2006). ➔

4 This reduction is due to the fact that some of the government's liabilities, previously recorded as interest ("new coupons"), are now recorded as outstanding public debt. This has the effect of decreasing interest payments and increasing amortisation payments, which, however, are not included in the deficit.
5 Except for the tax case settlements, which should, as estimated, yield revenue equivalent to 0.2% of GDP in 2004 and 0.7% of GDP in 2005.
6 European Commission, *Commission assessment in relation to the Commission recommendation for a Council decision establishing whether effective action has been taken by Greece in response to the Council recommendation under Article 104(7),* Brussels, 22 December 2004. The Commission specifically states on p. 5 that: "In sum, the measures implemented in 2004 have not been effective in reducing the deficit in 2004. Over and above statistical revisions, the fiscal policy stance further worsened in a situation of buoyant economic activity and large, positive output gaps."
7 Greece had already made this decision public on 5 July 2004.
8 At the end of January 2005, the Greek authorities requested that the European Commission postpone its revision of the Greek Programme, since a new Updated Stability and Growth Programme for 2004-2007 was due. This request was granted on 2 February 2005.

➔ (d) Greece was called upon to continue its effort to effectively contain the other factors —apart from the public deficit— that raise the debt-to-GDP ratio (stock-flow adjustments), so as to ensure that the public debt-to-GDP ratio diminishes at a satisfactory pace and approaches the reference value of 60% of GDP.

(e) The Greek authorities were also urged to continue their effort to improve their fiscal statistics collection and processing mechanism.

(f) Greece must submit six-monthly reports on the course of its public finances (the first by end-October 2005 and the following ones in April and October 2006), so that the Commission and the Council can assess compliance with the Council's Decision.

Regardless of the provisions of the Excessive Deficit Procedure for a reduction of the deficit to slightly less than 3% of GDP, Greece will still be far from meeting the terms set in the Stability and Growth Pact, which requires the achievement of a fiscal balance in the medium term. Considering that Greece also has a large public debt, attention must be focused on achieving the medium-term objective of a fiscal position of close to balance or in surplus, so that: (a) the usual cyclical fluctuations do not cause the fiscal deficit to exceed 3% of GDP and (b) the debt-to-GDP ratio decreases sufficiently and approaches the 60% of GDP reference value at a satisfactory pace.

In light of the above —and especially after taking into account the additional burden that population ageing will have on the social security system and the budget— the reduction of the deficit to below the 3% reference value should be seen as a significant but only initial step in the direction of medium-term fiscal consolidation.

curtailment of tax evasion (which remains a big problem), so as to allow a further reduction of tax rates as well as adequate investment in public infrastructure to support economic growth. In addition, early progress in reforming the social security and healthcare systems will be required to address some of the fiscal pressures that will arise from the impending population ageing. As mentioned previously, these pressures will mount significantly and steadily after 2010.

Wage policy

As mentioned in previous Bank of Greece reports, the acceleration of unit labour cost growth after 1999 has played an important role in the persistence of relatively high inflation and the continued loss of external competitiveness. This year, the rate of increase in unit labour costs is projected to slow down, but it will nonetheless remain higher than the corresponding euro area average and inconsistent with the objective of price stability (i.e. a rate of inflation below but close to 2%). Looking forward, as pointed out in past reports, nominal wage increases will have to gradually converge towards the sum of productivity growth in Greece and the average rate of inflation in the euro area (rather than that in Greece), until the inflation differential between Greece and the euro area is essentially eliminated. Until then, the implementation of such a policy would help Greece gain some much needed external competitiveness vis-à-vis its euro area trading partners.

Labour market

Today's unacceptably high unemployment rate, especially among young people and women, and the modest rise in employment despite rapid growth over the past decade are another major cause for concern. These problems clearly point to shortcomings in the labour, tax and social security legislation, as well as in the education system, and, in general, to the adverse business environment, all of which act as disincentives for labour demand and supply and lead to a mismatching between them. The reform efforts made over the past fifteen years have had some positive results, but have been clearly insufficient. Thus, it is urgent to begin an in-depth and far-reaching dialogue, starting from the following clear premises: the social support and safety net, which is essential to exist in the labour market, will not be undermined, nor will one social group be favoured at the expense of another, but existing disincentives must be urgently removed and more effective solutions found, which will benefit all groups without compromising basic rights. Of course, it is very difficult to strike a balance between economic efficiency and social justice. Nevertheless, the economy as a whole stands much to benefit over the medium term from the improved utilisation of its labour force, especially of the newly employed. This is supported by the successful experience of other EU countries (Denmark, Spain, the Netherlands, Sweden), which took measures to enhance labour market flexibility and achieved a large decrease in unemployment.

Product markets and business environment

Greece lags behind other euro area countries in establishing competitive conditions in its goods and services markets and creating a business-friendly environment. Competitive conditions in goods and services markets encourage productivity improvements and their translation into lower prices for the consumer and lower costs for other producers. Moreover, a more business-friendly environment —through a simplification of the tax system, the establishment of a stable taxation framework, a reduction of bureaucracy and, in general, a more efficient operation of the public sector— is key to encouraging investment and economic activity. Nevertheless, despite much progress over the past ten years, the Greek economy is still subject to numerous regulatory interventions, mainly on account of pervasive state controls and economic regulations (price controls, a multitude of administrative controls etc.). Turning to specific markets, Greece has, for instance, already experienced the benefits of enhanced competition in the mobile telephony market, in the form of lower prices and improved service, but the fixed-line market still lacks adequate competition. The electricity market, which was formally liberalised in February 2001, remains effectively under the control of the Public Power Corporation (PPC); however, the adoption of new legislation is expected to remove the remaining impediments to market entry (see the Appendix to Chapter III). Looking forward, the Competition Commission should be properly staffed and fully enabled to pursue its mandate actively (as is intended by the draft law currently under consideration).

Financial sector

Greece's financial sector has been fully liberalised and its efficiency has considerably improved since the early 1990s, while its stability has also been safeguarded. As noted in Chapter V, the banking system is sound on the whole, but the uncertainties detailed below do warrant some caution from commercial banks. The overall capital adequacy ratio of Greek commercial banks (13.3% in September 2004, against 11.9% for euro area banks in 2003) offers a satisfactory cushion in the current circumstances. In this regard, it should be noted that the application, from the beginning of 2005, of the International Accounting Standards (IAS) —in particular of Standard 19 on the accounting treatment of liabilities stemming from defined-benefit insurance plans for bank employees— will affect significantly only a very small number of banks, which will have to restore their capital adequacy by augmenting their capital base. However, the overall capital adequacy ratio of the banking system will not be affected significantly. The introduction of a new supervisory framework (Basle II) as of end-2006 will also affect the capital adequacy ratio, but the size and direction of the effects on individual banks are difficult to assess at this stage. In light of these uncertainties, the Bank of Greece has recommended that banks strengthen their own capital. Moreover, because of the rapid rise in credit to households under the pressure of competition, which may lead to increased credit risk in the future, especially in the event of a slowdown in economic activity, the Bank of Greece has raised the minimum provisioning requirements for consumer loans with significant servicing delays and has recommended that banks take account of this factor in their lending decisions so as to contain their credit risk. Meanwhile, households should carefully assess their income prospects before borrowing, so as not to be burdened excessively.

* * *

As mentioned above, Greece's growth rate, though projected to slow in 2005, should remain substantially above the euro area average. Growth prospects over the medium term are subject to a certain degree of uncertainty owing to large fiscal imbalances and structural rigidities that threaten macroeconomic stability and undermine external competitiveness. Greece's inflation in 2005 should remain considerably higher than that of the euro area. Achieving price stability (i.e. a rate of inflation below but close to 2%) and satisfactory growth on a sustained basis will require determined fiscal adjustment, involving the gradual elimination of the fiscal deficit and the achievement of a surplus. Wage increases will also have to be in line with productivity growth (as mentioned above), while wide-ranging structural reforms will be needed to address rigidities in the product and labour markets. The consistent implementation of a well-designed programme of structural reforms, including a reform of the social security system, would contribute to fiscal stability and encourage investment and the development of new productive activities, thereby enhancing economic growth and employment. Important issues of social concern, however, need to be taken into account to ensure that this programme is well balanced. Adjustment often has painful side-effects, which can and must be alleviated with adequate support measures. Accordingly, there is a need for a dialogue, based on openness and transparency, about the benefits and costs of the suggested reforms (including the reform of the social security system), with a view to securing a durable social consensus. Such a consensus should be achievable considering that the economy as a whole could benefit enormously. On the contrary, failure to undertake these reforms would have serious negative implications for growth and living standards in Greece.

Monetary policy measures of the Eurosystem

8 January 2004

The Governing Council of the ECB decides that the minimum bid rate on the main refinancing operations and the interest rates on the marginal lending facility and the deposit facility will remain unchanged at 2.0%, 3.0% and 1.0% respectively.

12 January 2004

The Governing Council of the ECB decides to increase the allotment amount for each of the longer-term refinancing operations to be conducted in the year 2004 from €15 billion to €25 billion. This increased amount takes into consideration the higher liquidity needs of the euro area banking system anticipated for the year 2004. The Eurosystem will, however, continue to provide the bulk of liquidity through its main refinancing operations.

5 February, 4 March, 1 April, 6 May, 3 June, 1 July, 5 August, 2 September, 7 October, 4 November, 2 December 2004, 13 January 2005

The Governing Council of the ECB decides that the minimum bid rate on the main refinancing operations and the interest rates on the marginal lending facility and the deposit facility will remain unchanged at 2.0%, 3.0% and 1.0% respectively.

14 January 2005

The Governing Council of the ECB decides to increase the allotment amount for each of the longer-term refinancing operations to be conducted in the year 2005 from €25 billion to €30 billion. This increased amount takes into consideration the higher liquidity needs of the euro area banking system anticipated for the year 2005. The Eurosystem will, however, continue to provide the bulk of liquidity through its main refinancing operations.

3 February 2005

The Governing Council of the ECB decides that the minimum bid rate on the main refinancing operations and the interest rates on the marginal lending facility and the deposit facility will remain unchanged at 2.0%, 3.0% and 1.0% respectively.

Glossary

Community Support Framework (CSF): compiled by the Commission of the European Communities in co-operation with the Member State and approved by the Commission. It includes the country's growth strategy, activity priorities and financing resources (participation of the Community, national public expenditure, participation of the private sector).

Deposit facility: a *standing facility* of the *Eurosystem* which counterparties may use to make overnight deposits, remunerated at a pre-specified interest rate, at a national central bank.

Deposits redeemable at notice: this instrument comprises savings deposits which the depositor may withdraw once he has given notification thereof within a predetermined time period. At some instances, it is possible to withdraw part of the amount deposited at notice or before, subject to penalty. Deposits redeemable at notice of up to three months pertain to M2 (hence to M3). Longer-term deposits redeemable at notice pertain to (non-monetary) longer-term financial liabilities of monetary financial institutions (MFIs).

Deposits with an agreed maturity: deposits with a fixed maturity, which, according to the national practice, are either not convertible into cash before their maturity or are convertible into cash subject to penalty. They include some non-negotiable instruments, such as non-negotiable certificates of (private) deposit. Deposits with an agreed maturity of up to two years pertain to M2 (hence to M3). Longer-term deposits with an agreed maturity pertain to (non-monetary) longer-term financial liabilities of monetary financial institutions (MFIs).

Effective (nominal/real) exchange rates: nominal effective exchange rates are weighted averages of bilateral exchange rates. Real effective exchange rates are nominal effective exchange rates deflated by a weighted average of foreign, relative to domestic, prices or costs. They are, thus, measures of price and cost competitiveness.

EONIA (euro overnight index average): a measure of the interest rate prevailing in the euro interbank overnight market, based on transactions.

EURIBOR (euro interbank offered rate): the rate at which a prime bank is willing to lend funds in euro to another prime bank, computed daily for interbank deposits with different maturities of up to 12 months.

Euro area: the area encompassing those Member States in which the euro has been adopted as the single currency in accordance with the Treaty and in which a single monetary policy is conducted under the responsibility of the *Governing Council* of the ECB. The euro area currently comprises 12 countries: Austria, Belgium, Germany, Greece, Finland, France, Ireland, Italy, Luxembourg, the Netherlands, Portugal and Spain.

European Central Bank (ECB): the ECB lies at the centre of the *European System of Central Banks* (ESCB) and the *Eurosystem* and has legal personality under Community law. It ensures that the tasks conferred upon the Eurosystem and the ESCB are implemented either through its own activities or through those of the national central banks, pursuant to the Statute of the ESCB and of the ECB. The ECB is governed by the *Governing Council* and the *Executive Board*, and, as a third decision-making body, by the *General Council*.

European System of Central Banks (ESCB): composed of the ECB and the national central banks of all 25 EU Member States, i.e. it includes, in addition to the members of the *Eurosystem*, the national central banks of those Member States that have not yet adopted the euro. The ESCB is governed by the *Governing Council* and the *Executive Board*, and, as a third decision-making body, by the *General Council*.

Eurosystem: comprises the ECB and the national central banks of those Member States that have adopted the euro. There are currently 12 national central banks in the Eurosystem. The Eurosystem is governed by the *Governing Council* and the *Executive Board* of the ECB.

Executive Board: one of the decision-making bodies of the ECB. It comprises the President and the Vice-President of the ECB and four other members appointed by common accord by the Heads of State or Government of the countries that have adopted the euro.

General Council: one of the decision-making bodies of the ECB. It comprises the President and the Vice-President of the ECB and the governors of the 25 EU national central banks.

General government: as defined in the European System of Accounts 1995 (ESA 95), comprises central, state and local government and social security funds.

Governing Council: one of the decision-making bodies of the ECB. It comprises all the members of the *Executive Board* and the governors of the national central banks of the countries that have adopted the euro.

Harmonised Index of Consumer Prices (HICP): a measure of consumer prices which is compiled by Eurostat and harmonised for all EU countries.

Key ECB interest rates: the interest rates, set by the *ECB*, which reflect the monetary policy stance of the ECB. Currently, key ECB interest rates are the minimum bid rate on the *main refinancing operations*, the interest rate on the *marginal lending facility* and the interest rate on the *deposit facility*.

Main refinancing operation: a weekly open market operation conducted by the *Eurosystem*. The operations are conducted as variable rate tenders with a pre-announced minimum bid rate and have a maturity of one week.

Marginal lending facility: a *standing facility* of the *Eurosystem,* which counterparties may use to receive overnight credit from a national central bank at a pre-specified interest rate against eligible assets.

Monetary aggregates: a monetary aggregate is the sum total of currency in circulation plus the overdue amounts of certain liabilities of MFIs and central governments which have a high degree of "moneyness" (or liquidity in a broad sense). The narrow monetary aggregate M1, as defined by the *Eurosystem*, comprises currency in circulation plus *overnight deposits* which non-MFI *euro area* residents (other than central government) keep with *euro area* institutions that issue money. The monetary aggregate M2 comprises M1 plus *deposits with an agreed maturity* of up to two years plus *deposits redeemable at* a period of *notice* of up to three months. The broad monetary aggregate M3 comprises M2 and repurchase agreements (repos), money market fund shares/units, money market paper and debt securities with a maturity of up to two years.

Overnight deposits: deposits due on the next working day. This instrument comprises both fully transferable (through cheques etc.) and non-transferable deposits convertible into cash upon request or until the end of the next working day. Particularly for Greece, this instrument includes sight deposits, deposits in current accounts and savings deposits.

Standing facility: a national central bank facility available to counterparties on their own initiative. The *Eurosystem* offers two overnight standing facilities: the *marginal lending facility* and the *deposit facility*.

Statistical appendix

Tables

T a b l e 1

Consumer price index: general index and basic sub-indices

Period	General index		Goods		Services		CPI excluding fresh fruit/ vegetables and fuel		CPI excluding food and fuel	
	(1999=100)	Percentage change over previous year	(1999=100)	Percentage change over previous year	(1999=100)	Percentage change over previous year	(1999=100)	Percentage change over previous year	(1999=100)	Percentage change over previous year
2001	106.4	3.4	106.7	3.2	105.9	3.7	105.3	3.8	105.0	3.7
2002	110.2	3.6	110.1	3.2	110.4	4.3	109.0	3.6	108.7	3.6
2003	114.1	3.5	113.5	3.1	115.1	4.2	112.6	3.2	112.2	3.1
2004	117.4	2.9	116.0	2.3	119.5	3.8	116.2	3.3	115.7	3.2
2003 I	112.8	3.8	112.4	3.4	113.4	4.5	110.7	3.6	110.1	3.4
II	114.9	3.7	114.9	3.4	114.7	4.1	112.8	3.1	112.5	3.0
III	113.3	3.4	112.0	2.9	115.4	4.1	112.1	3.0	111.6	2.9
IV	115.5	3.2	114.6	2.5	116.9	4.3	114.6	3.2	114.5	3.3
2004 I	115.8	2.7	114.4	1.8	118.0	4.0	114.3	3.3	113.7	3.2
II	118.2	2.9	117.5	2.3	119.1	3.9	116.6	3.3	116.1	3.2
III	116.5	2.8	114.3	2.1	119.9	3.9	116.0	3.4	115.3	3.4
IV	119.1	3.2	117.9	2.9	121.0	3.5	118.0	3.0	117.8	2.9
2002 Jan. . . .	108.4	4.4	108.5	5.2	108.4	3.3	106.5	3.3	106.0	3.2
Feb. . . .	107.3	3.4	106.7	3.1	108.3	3.9	105.7	3.1	105.2	3.2
March .	110.0	4.0	110.7	3.8	109.0	4.4	108.4	3.6	108.3	3.7
Apr. . . .	110.9	3.8	111.7	4.0	109.6	3.6	109.0	3.4	108.8	3.5
May . . .	110.8	3.4	111.1	2.4	110.5	4.9	109.7	4.2	109.5	4.3
June . . .	110.6	3.3	110.9	2.5	110.3	4.5	109.7	3.9	109.5	3.8
July . . .	108.7	3.3	107.6	2.7	110.5	4.4	108.1	3.7	107.4	3.5
Aug. . . .	109.0	3.5	107.9	2.9	110.7	4.5	108.2	3.6	107.6	3.6
Sept. . .	111.0	3.5	110.8	2.7	111.5	4.8	110.3	3.7	110.1	3.8
Oct. . . .	111.6	3.7	111.6	3.2	111.7	4.6	110.7	3.5	110.6	3.6
Nov. . . .	111.6	3.6	111.5	3.1	111.9	4.5	110.9	3.5	110.8	3.5
Dec. . . .	112.4	3.4	112.3	2.8	112.7	4.3	111.4	3.5	111.2	3.5
2003 Jan. . . .	111.8	3.1	110.8	2.1	113.4	4.7	110.4	3.7	109.9	3.6
Feb. . . .	112.0	4.3	111.1	4.1	113.3	4.7	109.7	3.8	108.9	3.5
March .	114.5	4.1	115.2	4.1	113.4	4.1	112.0	3.4	111.6	3.1
Apr. . . .	114.6	3.4	114.6	2.6	114.6	4.5	112.6	3.4	112.3	3.1
May . . .	115.1	3.8	115.4	3.9	114.7	3.7	112.8	2.9	112.6	2.8
June . . .	114.9	3.8	114.9	3.6	114.9	4.2	113.0	3.0	112.7	3.0
July . . .	112.7	3.6	111.1	3.2	115.0	4.1	111.2	2.9	110.5	2.9
Aug. . . .	112.6	3.3	110.9	2.8	115.2	4.0	111.4	3.0	110.7	2.9
Sept. . .	114.8	3.3	113.9	2.8	116.1	4.2	113.8	3.2	113.5	3.1
Oct. . . .	115.2	3.2	114.4	2.5	116.4	4.2	114.3	3.2	114.1	3.2
Nov. . . .	115.4	3.3	114.7	2.9	116.5	4.1	114.4	3.1	114.3	3.2
Dec. . . .	115.9	3.1	114.7	2.2	117.7	4.5	115.2	3.3	115.0	3.4
2004 Jan. . . .	115.1	2.9	113.3	2.3	117.9	3.9	114.0	3.2	113.4	3.2
Feb. . . .	114.8	2.5	112.7	1.5	117.9	4.0	113.2	3.1	112.2	3.1
March .	117.6	2.7	117.2	1.8	118.2	4.2	115.9	3.4	115.3	3.3
Apr. . . .	117.9	2.9	117.2	2.3	119.0	3.9	116.3	3.2	115.9	3.2
May . . .	118.5	2.9	118.1	2.4	119.0	3.8	116.6	3.3	116.1	3.2
June . . .	118.1	2.8	117.3	2.1	119.4	3.9	116.9	3.5	116.5	3.3
July . . .	116.0	2.9	113.6	2.2	119.6	4.0	115.5	3.8	114.8	3.8
Aug. . . .	115.7	2.7	113.0	1.9	119.8	4.0	115.0	3.2	114.1	3.1
Sept. . .	118.0	2.8	116.4	2.2	120.5	3.7	117.5	3.3	117.1	3.2
Oct. . . .	118.9	3.2	117.9	3.1	120.4	3.5	117.7	3.0	117.5	3.0
Nov. . . .	119.0	3.1	117.9	2.8	120.7	3.6	117.9	3.1	117.6	2.9
Dec. . . .	119.5	3.1	117.9	2.8	121.8	3.5	118.5	2.9	118.2	2.8
2005 Jan. . . .	119.8	4.0	118.1	4.3	122.3	3.7	118.7	4.2	118.5	4.5

Source: Calculations based on NSSG data.

Table 2

Harmonised index of consumer prices: general index and basic sub-indices

Period	HICP (general)		Unprocessed food		Processed food		Non-energy industrial goods	
	(1996=100)	Percentage change over previous year	(1996=100)	Percentage change over previous year	(1996=100)	Percentage change over previous year	(1996=100)	Percentage change over previous year
2001	120.1	3.7	124.8	6.7	120.4	5.1	115.1	2.9
2002	124.8	3.9	133.5	6.9	127.0	5.5	118.0	2.5
2003	129.0	3.4	142.0	6.4	131.7	3.6	119.8	1.6
2004	133.0	3.0	137.8	–2.9	138.0	4.8	122.6	2.3
2003 I	127.3	3.8	141.0	0.8	129.6	4.7	116.8	1.7
II	129.9	3.5	150.4	12.3	130.6	2.4	122.0	1.8
III	128.2	3.4	138.9	9.0	132.4	3.2	117.4	1.3
IV	130.8	3.2	137.5	3.8	134.2	4.4	123.1	1.5
2004 I	130.9	2.9	146.2	3.7	135.9	4.9	118.9	1.7
II	133.9	3.1	142.8	–5.1	138.2	5.9	124.5	2.1
III	132.0	3.0	128.9	–7.2	138.9	4.9	120.8	3.0
IV	135.0	3.2	133.3	–3.1	139.0	3.6	126.4	2.6
2002 Jan.	122.4	4.8	143.4	20.9	123.3	4.8	113.9	3.3
Feb.	121.0	3.8	137.5	13.9	123.5	4.3	111.4	2.6
March ..	124.5	4.4	138.8	12.8	124.6	5.1	119.3	2.6
Apr.	125.5	4.1	138.3	10.1	126.9	7.0	119.4	2.6
May	125.8	3.8	132.4	2.2	127.6	7.4	120.0	2.9
June ...	125.5	3.6	131.2	3.9	128.0	6.1	120.2	2.6
July	123.0	3.6	126.6	3.8	128.2	5.7	113.7	2.4
Aug. ...	123.2	3.8	127.3	4.5	128.4	5.6	113.7	2.4
Sept. ...	125.8	3.8	128.4	4.2	128.4	5.3	120.1	2.2
Oct.	126.4	3.9	130.8	5.1	128.5	5.0	121.1	2.1
Nov. ...	126.5	3.9	132.4	4.8	128.6	5.0	121.4	2.1
Dec. ...	127.4	3.5	134.5	–1.1	128.6	4.7	121.4	2.1
2003 Jan.	126.4	3.3	136.6	–4.7	128.9	4.5	116.1	1.9
Feb.	126.1	4.2	141.6	3.0	129.7	5.0	113.1	1.5
March ..	129.3	3.9	144.8	4.4	130.2	4.5	121.3	1.7
Apr.	129.6	3.3	147.7	6.8	130.5	2.8	121.5	1.7
May	130.2	3.5	153.8	16.1	130.6	2.3	122.2	1.8
June ...	130.0	3.6	149.8	14.2	130.7	2.1	122.2	1.7
July	127.3	3.5	141.2	11.6	130.8	2.1	115.5	1.6
Aug. ...	127.3	3.3	137.8	8.3	132.0	2.9	115.2	1.3
Sept. ...	129.9	3.3	137.6	7.2	134.3	4.6	121.4	1.1
Oct.	130.4	3.2	136.3	4.2	134.2	4.5	122.8	1.4
Nov. ...	130.6	3.2	137.4	3.8	134.1	4.3	123.2	1.5
Dec. ...	131.4	3.1	138.9	3.3	134.2	4.4	123.4	1.7
2004 Jan.	130.3	3.1	142.3	4.1	134.7	4.5	118.4	1.9
Feb.	129.4	2.6	148.1	4.5	135.8	4.7	114.6	1.3
March ..	133.1	2.9	148.3	2.4	137.2	5.4	123.6	1.9
Apr.	133.6	3.1	144.6	–2.1	137.5	5.4	123.8	2.0
May	134.2	3.1	144.8	–5.8	138.5	6.1	124.7	2.0
June ...	133.9	3.0	138.9	–7.3	138.7	6.2	125.0	2.3
July	131.3	3.1	127.9	–9.5	138.8	6.1	119.7	3.6
Aug. ...	130.9	2.8	129.4	–6.1	138.9	5.2	117.5	2.0
Sept. ...	133.7	2.9	129.5	–5.9	138.9	3.5	125.4	3.3
Oct.	134.7	3.3	130.9	–4.0	138.9	3.5	126.4	2.9
Nov. ...	134.8	3.2	131.4	–4.4	139.1	3.7	126.3	2.6
Dec. ...	135.5	3.1	137.6	–1.0	139.1	3.7	126.4	2.4
2005 Jan.	135.8	4.2	138.0	–3.0	139.2	3.4	126.5	6.9

Source: Calculations based on NSSG data.

T a b l e 2 *(continued)*

Harmonised index of consumer prices: general index and basic sub-indices

Period	Energy		Services		HICP excluding unprocessed food and energy	
	(1996=100)	Percentage change over previous year	(1996=100)	Percentage change over previous year	(1996=100)	Percentage change over previous year
2001	106.4	–1.7	128.1	3.9	121.1	3.8
2002	106.1	–0.3	133.8	4.5	125.8	3.9
2003	110.0	3.7	139.4	4.1	129.7	3.1
2004	117.0	6.4	144.7	3.8	134.2	3.4
2003 I	114.1	12.6	137.4	4.5	127.3	3.5
II	106.8	–1.0	139.0	3.9	130.2	2.8
III	109.5	1.5	139.8	4.1	129.0	2.9
IV	109.7	2.1	141.4	4.1	132.3	3.2
2004 I	110.4	–3.3	142.8	4.0	131.5	3.3
II	117.2	9.7	144.3	3.8	134.8	3.5
III	118.2	7.9	145.3	3.9	133.8	3.7
IV	122.4	11.6	146.5	3.6	136.6	3.2
2002 Jan.	99.9	–3.7	131.4	3.6	122.5	3.6
Feb.	100.6	–6.6	130.9	4.1	121.3	3.5
March ..	103.7	–3.0	132.0	4.7	125.1	4.0
Apr.	108.6	–1.4	133.0	3.7	126.0	3.8
May	108.1	–4.9	134.5	5.4	127.0	4.8
June ...	106.8	–3.0	133.8	4.7	126.8	4.1
July	107.0	–0.2	134.0	4.6	124.3	3.9
Aug. ...	108.2	1.5	134.1	4.6	124.4	3.9
Sept. ...	108.6	0.5	135.0	4.9	127.4	3.9
Oct.	108.9	4.9	135.2	4.6	127.9	3.7
Nov. ...	105.1	4.5	135.4	4.5	128.1	3.6
Dec. ...	108.1	9.9	136.8	4.4	128.7	3.6
2003 Jan.	111.0	11.2	137.7	4.8	127.0	3.7
Feb.	115.2	14.5	137.2	4.7	125.7	3.6
March ..	116.1	12.0	137.3	4.0	129.1	3.2
Apr.	107.9	–0.6	139.0	4.5	130.0	3.2
May	105.9	–2.0	138.8	3.2	130.2	2.5
June ...	106.5	–0.3	139.1	4.0	130.4	2.8
July	108.4	1.3	139.3	4.0	127.8	2.8
Aug. ...	110.1	1.7	139.6	4.1	128.0	2.9
Sept. ...	110.1	1.3	140.4	4.0	131.2	3.0
Oct.	110.5	1.4	140.8	4.1	131.9	3.1
Nov. ...	110.6	5.2	140.8	4.0	132.1	3.1
Dec. ...	107.9	–0.2	142.7	4.3	133.0	3.3
2004 Jan.	109.5	–1.4	143.0	3.9	131.2	3.3
Feb.	108.9	–5.5	142.5	3.9	129.6	3.1
March ..	112.8	–2.9	143.0	4.1	133.7	3.5
Apr.	115.6	7.0	144.3	3.8	134.4	3.4
May	119.0	12.4	143.9	3.7	134.7	3.5
June ...	116.9	9.8	144.6	4.0	135.2	3.7
July	117.5	8.4	144.9	4.0	133.2	4.2
Aug. ...	118.6	7.8	145.2	4.0	132.4	3.5
Sept. ...	118.3	7.5	145.8	3.8	135.9	3.6
Oct.	125.1	13.3	145.7	3.5	136.3	3.3
Nov. ...	124.6	12.7	145.9	3.6	136.3	3.2
Dec. ...	117.5	8.9	147.8	3.6	137.2	3.1
2005 Jan.	118.1	7.9	148.0	3.5	137.4	4.7

Source: Calculations based on NSSG data.

Table 3

Wholesale price index: general index and basic sub-indices

Period		General index		Domestic primary products[1]		Domestic industrial products[1]		Exported products		Imported products	
		(1995=100)	Percentage change over previous year	(1995=100)	Percentage change over previous year	(1995=100)	Percentage change over previous year	(1995=100)	Percentage change over previous year	(1995=100)	Percentage change over previous year
2001		126.8	2.3	139.2	10.0	128.7	2.7	128.9	0.7	120.7	1.9
2002		129.8	2.4	154.7	11.2	132.0	2.6	131.4	1.9	121.2	0.4
2003		132.5	2.1	168.1	8.6	135.6	2.7	131.5	0.1	122.5	1.1
2004		135.7	2.4	165.2	–1.7	141.6	4.5	136.0	3.4	123.1	0.5
2003	I	132.6	1.7	169.8	–2.5	134.9	3.6	131.9	1.1	122.6	1.5
	II	132.7	2.2	183.1	19.6	134.4	1.9	129.6	–2.0	122.3	0.9
	III	132.0	2.2	159.9	12.2	135.7	2.4	131.4	0.2	122.6	1.0
	IV	132.8	2.2	159.5	7.1	137.2	3.1	132.8	1.0	122.6	0.8
2004	I	134.9	1.8	177.6	4.6	138.7	2.8	134.0	1.6	122.5	0.0
	II	136.2	2.6	168.3	–8.1	141.7	5.4	137.0	5.6	123.1	0.6
	III	135.1	2.4	150.4	–6.0	142.4	4.9	136.8	4.1	123.2	0.5
	IV	136.5	1.1	164.4	9.3	143.6	0.9	136.1	–0.5	123.7	0.4
2002	Jan.	130.4	5.1	181.4	44.4	129.7	2.7	129.4	2.4	120.7	0.8
	Feb.	129.6	3.6	168.5	29.5	129.8	2.0	129.9	1.9	120.7	0.5
	March	131.1	4.2	172.6	30.5	131.4	3.0	132.3	2.8	121.0	0.5
	Apr.	131.7	3.7	172.2	23.3	132.1	2.7	133.5	2.8	121.2	0.4
	May	129.5	1.2	147.0	1.4	132.0	2.1	132.2	1.2	121.2	0.2
	June	128.5	0.3	140.2	–3.4	131.5	1.8	131.0	–0.3	121.1	0.0
	July	128.2	0.8	136.0	–0.7	132.1	2.3	130.4	0.5	121.0	–0.1
	Aug.	129.2	2.1	144.3	9.2	132.5	2.5	130.8	1.6	121.5	0.4
	Sept.	130.0	1.9	147.5	6.0	133.1	2.5	132.3	1.7	121.6	0.4
	Oct.	130.0	2.4	145.7	5.6	133.3	3.1	132.3	3.2	121.6	0.3
	Nov.	129.5	2.1	147.2	4.5	132.7	2.9	130.6	2.2	121.5	0.5
	Dec.	130.5	1.4	154.0	–6.8	133.3	3.2	131.5	2.7	121.8	0.9
2003	Jan.	131.0	0.5	155.6	–14.2	134.3	3.5	131.2	1.4	122.4	1.4
	Feb.	133.0	2.6	172.7	2.5	135.2	4.1	132.3	1.9	122.7	1.6
	March	133.7	2.0	181.0	4.9	135.4	3.0	132.4	0.0	122.7	1.4
	Apr.	133.0	1.0	183.4	6.5	134.5	1.8	130.6	–2.2	122.4	1.0
	May	132.6	2.4	188.3	28.1	134.3	1.7	127.8	–3.3	122.3	0.9
	June	132.5	3.1	177.5	26.6	134.4	2.2	130.5	–0.3	122.3	1.0
	July	131.9	2.9	164.3	20.9	134.9	2.1	131.3	0.7	122.4	1.2
	Aug.	132.1	2.2	159.7	10.6	135.8	2.5	131.7	0.7	122.6	1.0
	Sept.	131.9	1.5	155.8	5.6	136.4	2.5	131.3	–0.7	122.7	0.9
	Oct.	132.4	1.9	156.6	7.5	136.8	2.7	132.6	0.2	122.6	0.9
	Nov.	132.9	2.6	158.9	7.9	137.4	3.5	133.0	1.8	122.6	0.9
	Dec.	133.1	2.0	163.0	5.9	137.3	3.0	132.9	1.1	122.5	0.6
2004	Jan.	134.1	2.3	172.1	10.6	137.9	2.7	133.7	1.9	122.4	0.0
	Feb.	134.8	1.4	180.9	4.7	138.6	2.5	132.9	0.5	122.5	–0.1
	March	135.8	1.6	179.7	–0.7	139.6	3.1	135.5	2.3	122.7	0.0
	Apr.	136.7	2.8	179.2	–2.3	141.2	5.0	136.6	4.6	123.2	0.7
	May	136.7	3.1	172.2	–8.5	142.2	5.9	137.4	7.5	123.1	0.7
	June	135.0	1.9	153.6	–13.5	141.7	5.4	136.8	4.8	123.0	0.6
	July	134.9	2.3	150.9	–8.2	142.0	5.3	136.7	4.1	123.1	0.5
	Aug.	134.9	2.2	148.4	–7.1	142.4	4.9	136.9	4.0	123.1	0.3
	Sept.	135.4	2.7	152.0	–2.5	142.7	4.6	136.9	4.2	123.5	0.7
	Oct.	136.3	2.9	153.1	–2.2	144.0	5.2	138.1	4.1	123.8	0.9
	Nov.	136.3	2.6	161.4	1.5	143.8	4.7	135.9	2.2	123.7	0.8
	Dec.	136.9	2.9	178.8	9.7	143.0	4.1	134.4	1.1	123.5	0.9

1 For home consumption.

Source: Calculations based on NSSG data.

T a b l e 4

CPI goods and services by descending 12-month rate of change in December 2004

A. Rate of change higher than 3.1%[1]

Item	Weights ‰ (base year 1999)	Percentage change
Heating oil	14.67	27.1
Olive oil	7.22	14.6
Olives	0.58	13.9
Eggs	1.45	9.6
Bread	12.24	9.1
Dried fruit and nuts	1.37	8.6
Taxi fare	5.24	8.3
Radio and television contributions	3.74	7.9
Honey	0.89	7.9
Accommodation services	5.42	7.5
Tobacconist's	0.07	7.5
Medical services	17.20	7.4
Private school tuition fees (secondary education)	2.16	7.2
Transportation of commodities	0.37	7.2
Private school tuition fees (primary education)	3.31	6.0
Major durables for recreation and culture	0.09	5.6
Water supply – sewage collection	6.48	5.6
Toasted bread – rusks	1.05	5.3
Lubricants – coolants	0.59	5.2
Rents	39.19	5.2
Dental services	24.62	4.9
"Feta" cheese	9.29	4.8
Sweets – confectionery	5.83	4.7
Refuse collection	4.93	4.6
Frozen vegetables	1.06	4.6
Meals out (snacks)	12.45	4.6
Household services	9.83	4.5
Gas	1.49	4.5
Preserved meat	0.12	4.5
Domestic services	1.27	4.5
Motor fuels	32.28	4.4
Vegetable butter	0.82	4.4
Hard cheese	5.65	4.4
Repair of home appliances	1.01	4.3
Preserved milk	3.14	4.2
Textiles	0.61	4.2
Wine	1.65	4.2
Recreational and cultural services	2.69	4.2
Flowers	3.41	4.2
Vegetable fat	0.23	4.1
Women's footwear	9.87	4.1
Sausages – ham etc.	3.12	4.0
Foreign language tuition fees	9.01	4.0
Holiday packages	2.44	4.0
"Frontistirion" tuition fees	9.14	3.9
Sporting services	0.63	3.8
Children's clothes	11.04	3.8
Children's footwear	5.37	3.7
Shoe repairs	0.15	3.7
Other garments	1.75	3.7
Drinks (served)	10.36	3.6
Refreshments and confectionery (served out)	10.75	3.6
Insurance connected with transport	10.05	3.6
Yogurt	4.39	3.6
Miscellaneous bakery and confectionery products	5.18	3.6
Men's footwear	7.82	3.5
Miscellaneous services	10.02	3.5

T a b l e 4 *(continued)*

CPI goods and services by descending 12-month rate of change in December 2004

A. Rate of change higher than 3.1% *(cont'd)*

Item	Weights ‰ (base year 1999)	Percentage change
Preserved tomatoes	0.78	3.5
Meals in restaurants	42.29	3.4
Solid fuels	2.60	3.4
Babies' clothes	2.53	3.4
Barbers – hairdressers	4.49	3.4
Beer	2.01	3.3
Ice cream	1.23	3.3
Women's clothes	31.51	3.3
Nurse for the exclusive care of patients	2.59	3.3
Repair of audio-visual equipment	0.66	3.3
Men's clothes	24.95	3.3
Other services related to housing n.e.c.	5.71	3.2
Newspapers – magazines	6.98	3.2
House repair and maintenance	12.46	3.2
Fresh pasteurised milk	8.56	3.2

B. Rate of change between 2% and 3.1%

Item	Weights ‰ (base year 1999)	Percentage change
Education fees	3.80	3.1
Social protection services	0.54	3.1
Hospital services	8.96	3.1
Paramedical services	2.18	3.0
Financial services	0.20	3.0
Coffee (served)	9.67	3.0
Maintenance and repair of personal transport equipment	8.69	3.0
Insurance connected with health	3.53	2.9
Chocolate – chocolate products	1.46	2.9
Stationery	2.20	2.8
Therapeutic appliances and equipment	2.07	2.8
Theatre tickets	0.60	2.8
Refreshments	3.84	2.8
Electricity	18.76	2.7
Fresh butter	0.32	2.7
Canteens	5.67	2.7
Cocoa	0.19	2.7
Seed oil	1.27	2.6
Pharmaceutical products	0.77	2.6
Electrical appliances for personal care	0.12	2.6
Other cereals	1.10	2.6
Flour	0.99	2.6
Powder milk	0.73	2.6
Alteration of garments	0.79	2.5
Kitchen and household utensils	3.69	2.5
Books	7.53	2.5
Cleaning products	13.79	2.5
Clothing material	0.54	2.4
Mattresses – bed linen – pillows etc.	2.22	2.4
Salted fish	0.90	2.4
Preserved fish	0.66	2.4
Goods for house repair and maintenance	10.86	2.4
Fresh veal	19.58	2.3
Other meat products	0.68	2.3
Cars	47.56	2.1
Dry cleaning	2.13	2.1
Chocolate milk	0.36	2.1

Table 4 *(continued)*

CPI goods and services by descending 12-month rate of change in December 2004

C. Rate of change between 0% and 2%

Item	Weights ‰ (base year 1999)	Percentage change
Ready sauces, soups etc.	0.82	2.0
Jewelry – watches	2.91	2.0
Tableware – glassware	5.04	2.0
Rice	1.52	2.0
Floor coverings	2.18	2.0
Other services in respect of personal transport equipment	6.95	2.0
Museum tickets	0.16	2.0
Frozen meat	0.67	1.9
Wood and metal furniture	12.44	1.8
Other appliances and products for personal care	26.38	1.8
Tea	0.11	1.7
Travel items	2.76	1.7
Sports and camping goods	0.89	1.7
Insurance connected with dwellings	0.44	1.6
Pets and related products	1.62	1.6
Other personal effects	2.67	1.6
Alcoholic drinks	2.24	1.5
Garden equipment	0.95	1.5
Household maintenance articles	1.00	1.5
Postal services	0.25	1.5
Mineral water	0.65	1.5
Veterinary services	0.52	1.5
Fruit juices	1.93	1.4
Other household items	7.03	1.4
Domestic and kitchen utensils	0.48	1.4
Car spare parts	14.96	1.2
Cinema tickets	1.99	1.1
Passenger transport by air	2.38	1.1
Rental of audio-visual, photographic and information processing equipment	0.10	1.1
Pulse	1.52	1.1
Passenger transport by sea and inland waterway	2.03	1.0
Potato products	0.45	1.0
Photo films	0.16	1.0
Cutlery	0.69	0.8
Games. toys and hobbies	4.14	0.8
Development of photographic films	0.60	0.8
Children's food	0.28	0.7
Discs – cassettes – diskettes	2.28	0.7
Fresh pork	5.45	0.7
Fresh fruit	13.50	0.7
Salt – spices	0.71	0.6
Electronic games	0.54	0.6
Fresh beef	0.18	0.5
Blankets and household linen	5.03	0.5
Sugar	1.49	0.5
Fresh poultry	6.01	0.4
Curtains – coverlets etc.	8.57	0.4
Major household appliances	6.43	0.3
Jams	0.23	0.3
Intercity buses	2.20	0.1
Tobacco	32.97	0.0
Urban transportation	4.70	0.0
Drugs – medicines	10.68	0.0
Intercity trains	0.37	0.0

Table 4 *(continued)*

CPI goods and services by descending 12-month rate of change in December 2004

D. Negative rate of change

Item	Weights ‰ (base year 1999)	Percentage change
Fresh lamb-goat	6.28	–0.1
Coffee	3.65	–0.2
Musical instruments	0.22	–0.3
Pasta	2.12	–0.3
Frozen fish	2.37	–0.5
Fresh vegetables	14.11	–0.5
Motorcycles – bicycles	1.49	–1.0
Lighting – decoration items	1.54	–1.0
Radios – TVs – VCRs	3.14	–1.6
Computers	1.29	–1.6
Air condition	2.83	–2.7
Sweepers	0.37	–3.0
Photographic and cinematographic equipment	0.40	–3.7
Telephone equipment	0.24	–4.7
Telephone services	37.06	–5.2
Fresh fish	10.37	–5.8
Fresh potatoes	4.16	–30.7

1 The 12-month rate of change of the general CPI in December 2004 was 3.1%

Source: NSSG.

Table 5
Gross value added at basic prices and gross domestic product at market prices

	Million euro	Annual percentage changes (at constant prices of year 1995)					
	1995	1999	2000	2001	2002	2003	2004
Primary sector (agriculture)	7,277	3.5	–4.2	–4.1	–1.3	–4.2	. . .
Secondary sector	16,550	2.4	5.4	6.4	2.0	5.5	. . .
Mining and quarrying	476	–17.9	23.2	2.2	8.4	–4.8	. . .
Manufacturing	9,572	1.3	4.6	3.3	2.4	2.5	. . .
Electricity - natural gas - water supply	1,751	13.4	4.8	1.3	1.8	6.3	. . .
Construction	4,751	2.3	5.7	14.4	0.8	11.2	. . .
Tertiary sector	50,031	2.0	5.1	5.2	3.6	4.9	. . .
Trade	10,018	–0.8	3.1	11.4	1.4	6.7	. . .
Hotels - restaurants	4,821	–5.7	5.4	6.2	5.2	5.2	. . .
Transport - communications	4,978	33.4	16.2	1.3	5.9	6.0	. . .
Financial intermediaries	3,112	11.0	10.0	5.9	–5.2	8.9	. . .
Real estate management and other activities	12,577	–5.9	3.5	3.6	1.6	2.8	. . .
Public administration - security	5,308	0.9	–2.8	1.1	8.0	2.4	. . .
Education	3,298	–2.2	1.6	–1.2	12.2	1.4	. . .
Health	3,855	–2.0	3.0	2.5	4.9	4.9	. . .
Miscellaneous services	2,064	9.6	7.6	15.2	7.4	6.0	. . .
Gross value added	73,858	2.1	4.4	4.8	3.0	4.4	. . .
Imputed bank services	–2,175	2.8	13.7	12.1	–9.4	13.1	. . .
Gross value added at basic prices	71,683	2.1	4.1	4.5	3.5	4.1	. . .
Private consumption	58,405	2.5	2.0	3.0	3.0	4.4	3.6
Public consumption	12,250	2.1	14.8	–3.1	5.3	–2.5	5.5
Gross fixed capital formation	14,867	11.0	8.0	6.5	5.7	13.7	5.8
Housing	4,031	3.7	–4.3	4.8	8.8	7.3	–6.5
Other constructions	5,391	6.6	8.9	8.2	0.7	13.2	12.6
Equipment	4,680	21.4	14.1	4.9	6.9	18.3	6.5
Other	765	–2.4	7.6	20.1	21.0	3.4	2.0
Change in stocks and statistical discrepancy (as a percentage of GDP)	251	0.0	0.7	0.1	0.4	0.1	0.0
Domestic final demand	85,774	3.8	5.6	2.4	4.2	5.3	4.3
Exports of goods and services	14,087	18.1	14.1	–1.1	–7.7	1.0	7.3
Exports of goods	8,344	6.3	8.7	–1.6	–7.1	4.2	–10.0
Exports of services	5,743	29.0	18.2	–0.7	–8.1	–1.3	20.0
Final demand	99,861	6.1	7.2	1.7	2.0	4.6	4.8
Imports of goods and services	19,934	15.0	15.1	–5.2	–2.9	4.8	8.3
Imports of goods	18,084	8.5	15.2	–6.3	3.2	6.6	7.5
Imports of services	1,849	52.9	14.4	–0.4	–26.5	–5.3	13.0
GDP at market prices	79,927	3.4	4.5	4.3	3.6	4.5	3.7

Source: NSSG/National Accounts, September 2004: final data for 1999 and revised data for 2000-2003. For 2004, Ministry of Economy and Finance (Stability and Growth Programme 2004-2007) – *data under revision*.

Table 6

Employed persons (in thousands) of 15 years and over, by branch of economic activity

	2004 Q2	
	Total employed persons	Salaried employees
Total	**4,329.7**	**2,745.6**
Agriculture, animal breeding, hunting and forestry	533.1	36.5
Fishing	12.1	2.8
Mining and quarrying	14.7	13.2
Manufacturing	569.7	418.5
Electricity, gas, steam and water supply	39.1	38.9
Construction	350.0	235.6
Wholesale and retail trade; repair of motor vehicles, motorcycles and personal and household goods	748.2	369.1
Hotels and restaurants	279.4	161.8
Transport, storage and communication	272.4	204.4
Financial intermediation	112.4	100.7
Real estate, renting and business activities	283.0	160.5
Public administration and defence, compulsory social security	356.0	354.3
Education	318.4	292.9
Health and social work	219.0	182.5
Other community, social and personal service activities	155.1	110.5
Private households with employed persons	65.8	62.3
Extra-territorial organisations and bodies	1.4	1.4

Source: NSSG, Labour Force Survey.

Table 7

Balance of payments

(Million euro)

	January - December			December		
	2002	2003	2004	2002	2003	2004
I CURRENT ACCOUNT BALANCE (I.A+I.B+I.C+I.D)	**–8,571.3**	**–8,646.3**	**–6,411.0**	**–1,557.5**	**–1,590.4**	**–1,327.3**
***I.A TRADE BALANCE** (I.A.1-I.A.2)*	***–22,708.7***	***–22,643.5***	***–25,435.8***	***–2,002.3***	***–2,260.7***	***–2,389.0***
Non-oil trade balance	–19,203.7	–18,607.7	–20,960.8	–1,662.1	–1,870.9	–2,085.4
Oil trade balance	–3,505.0	–4,035.8	–4,475.0	–340.2	–389.8	–303.6
I.A.1 *Exports of goods*	*10,433.6*	*11,113.6*	*12,653.3*	*987.1*	*1,025.6*	*1,237.0*
Fuel	1,121.7	1,280.7	1,544.7	109.0	94.5	143.6
Other goods	9,311.9	9,832.9	11,108.6	878.1	931.1	1,093.4
I.A.2 *Imports of goods*	*33,142.3*	*33,757.1*	*38,089.0*	*2,989.4*	*3,286.3*	*3,626.0*
Fuel	4,626.7	5,316.5	6,019.7	449.2	484.3	447.2
Other goods	28,515.6	28,440.6	32,069.3	2,540.2	2,802.0	3,178.8
***I.B SERVICES BALANCE** (I.B.1-I.B.2)*	***10,755.4***	***11,506.5***	***15,467.0***	***280.9***	***406.7***	***655.6***
I.B.1 *Receipts*	*21,131.4*	*21,430.3*	*26,742.5*	*1,135.5*	*1,437.3*	*1,726.8*
Travel	10,284.7	9,495.3	10,347.8	241.4	221.5	228.8
Transport	8,523.4	9,569.8	13,307.0	704.9	970.2	1,212.3
Other services	2,323.3	2,365.3	3,087.7	189.3	245.5	285.7
I.B.2 *Payments*	10,376.1	9,923.9	11,275.5	854.6	1,030.6	1,071.2
Travel	2,548.7	2,136.0	2,310.4	204.7	190.4	231.9
Transport	5,029.7	4,923.6	5,728.2	402.9	527.0	497.6
Other services	2,797.7	2,864.3	3,236.9	247.1	313.1	341.8
***I.C INCOME BALANCE** (I.C.1-I.C.2)*	***–2,073.4***	***–2,597.4***	***–2,457.4***	***–209.1***	***–221.4***	***–169.7***
I.C.1 *Receipts*	*1,626.5*	*1,569.1*	*1,686.5*	*139.2*	*171.2*	*158.1*
Wages. salaries	509.6	337.2	280.0	35.4	27.3	26.7
Interest. dividends. profits	1,116.9	1,231.9	1,406.5	103.8	143.9	131.4
I.C.2 *Payments*	3,699.9	4,166.5	4,144.0	348.3	392.7	327.7
Wages. salaries	240.4	169.9	188.9	14.4	16.7	16.7
Interest. dividends. profits	3,459.5	3,996.6	3,955.1	333.9	376.0	311.0
***I.D TRANSFERS BALANCE** (I.D.1-I.D.2)*	***5,455.4***	***5,088.1***	***6,015.1***	***372.9***	***485.0***	***575.8***
I.D.1 *Receipts*	*7,801.4*	*7,817.4*	*8,974.3*	*564.9*	*854.8*	*892.3*
General government (mainly transfers from the EU)	5,458.0	5,375.0	6,544.2	356.9	645.2	693.9
Other sectors (emigrants' remittances etc.)	2,343.4	2,442.4	2,430.1	208.0	209.5	198.4
I.D.2 *Payments*	2,346.0	2,729.3	2,959.2	192.0	369.8	316.6
General government (mainly payments to the EU)	1,695.7	2,169.3	2,286.6	119.9	311.6	249.0
Other sectors	650.3	560.0	672.6	72.0	58.1	67.6
II FINANCIAL ACCOUNT BALANCE (II.A+II.B+II.C+II.D)	**10,310.4**	**9,663.7**	**7,834.0**	**1,932.6**	**1,932.7**	**1,616.1**
II.A DIRECT INVESTMENT[1]	***–643.0***	***544.7***	***599.6***	***–126.4***	***1,143.8***	***35.7***
By residents abroad	–696.3	–41.2	–488.8	–150.2	425.3	–38.2
By non-residents in Greece	53.4	585.9	1,088.4	23.8	718.5	73.9
II.B PORTFOLIO INVESTMENT[1]	***10,937.8***	***12,334.0***	***13,727.5***	***–45.6***	***1,693.5***	***3,243.3***
Assets	–2,230.0	–8,737.9	–11,489.4	–964.7	–793.2	–1,266.1
Liabilities	13,167.8	21,071.8	25,216.9	919.2	2,486.7	4,509.5
II.C OTHER INVESTMENT[1]	***1,998.6***	***–7,623.9***	***–9,104.1***	***2,030.5***	***–1,443.6***	***–2,368.9***
Assets	–7,481.9	–4,034.5	–6,215.7	308.3	984.8	5,140.5
Liabilities	9,480.5	–3,589.4	–2,888.4	1,722.3	–2,428.4	–7,509.4
(General government loans)	–4,510.1	–2,618.4	–1,027.4	–432	–158.9	–222.7
II.D CHANGE IN RESERVE ASSETS[2]	***–1,983.0***	***4,409.0***	***2,611.0***	***74.0***	***539.0***	***706.0***
III ERRORS AND OMISSIONS	**–1,739.0**	**–1,017.4**	**–1,423.0**	**–375.1**	**–342.3**	**–288.8**
RESERVE ASSETS[3]				9,014.0	4,605.0	1,994.0

1 (+) net inflow, (–) net outflow.
2 (+) decrease, (–) increase.
3 Reserve assets, as defined by the European Central Bank, include only monetary gold, the "reserve position" at the IMF, "Special Drawing Rights", and Bank of Greece's claims in foreign currency on residents of non-euro area countries. Conversely, reserve assets do not include claims in euro on residents of non-euro area countries, claims in foreign currency and in euro on residents of euro area countries, and the Bank of Greece participation in the capital and the reserve assets of the ECB.
Source: Bank of Greece.

Table 8
Monetary aggregates in the euro area[1,2]
(Outstanding balances in billion euro, not seasonally adjusted)

End of period	Currency in circulation (1)	Overnight deposits (2)	**M1** (3)=(1)+(2)	Deposits with agreed maturity up to two years (4)	Deposits redeemable at notice up to three months (5)	**M2** (6)=(3)+(4)+(5)	Repurchase agreements (7)	Money market fund shares/units (8)	Money market paper and debt securities up to two years (9)	**M3**[3] (10)=(6)+(7)+(8)+(9)
2001	239.7	2,039.2	2,279.0	1,088.8	1,316.6	4,684.4	218.5	398.0	145.9	5,446.8
2002	341.2	2,158.3	2,499.4	1,075.7	1,406.3	4,981.4	226.9	470.5	127.6	5,806.4
2003	397.9	2,331.4	2,729.3	1,039.0	1,529.6	5,297.9	208.7	581.4	88.5	6,176.5
2004	468.5	2,474.2	2,942.7	1,043.6	1,641.5	5,627.9	227.5	603.8	100.7	6,560.0
2002 Jan.	246.7	1,993.4	2,240.0	1,081.0	1,335.0	4,656.1	216.2	416.6	141.8	5,430.7
Feb.	240.5	1,987.9	2,228.3	1,076.8	1,339.1	4,644.2	221.1	427.0	138.8	5,431.0
March	254.3	1,983.7	2,238.0	1,088.5	1,342.8	4,669.3	229.6	431.2	137.2	5,467.4
Apr.	261.7	2,016.0	2,277.7	1,092.1	1,335.8	4,705.6	228.1	437.5	134.7	5,505.9
May	273.8	2,016.5	2,290.3	1,099.6	1,337.8	4,727.7	234.8	442.6	144.0	5,549.1
June	285.7	2,064.0	2,349.7	1,074.9	1,343.2	4,767.8	229.6	439.2	132.8	5,569.4
July	296.6	2,031.4	2,328.0	1,083.7	1,346.2	4,757.9	228.8	450.3	125.5	5,562.4
Aug.	301.1	2,000.1	2,301.2	1,096.9	1,351.6	4,749.7	236.5	463.4	126.5	5,576.1
Sept.	306.7	2,057.4	2,364.1	1,073.6	1,353.7	4,791.4	238.3	460.4	131.3	5,621.5
Oct.	313.9	2,041.2	2,355.1	1,093.7	1,362.2	4,811.0	235.6	463.1	133.7	5,643.4
Nov.	321.4	2,093.2	2,414.6	1,086.3	1,374.6	4,875.5	229.6	477.6	131.1	5,713.8
Dec.	341.2	2,158.3	2,499.4	1,075.7	1,406.3	4,981.4	226.9	470.5	127.6	5,806.4
2003 Jan.	312.1	2,128.8	2,440.9	1,077.3	1,405.5	4,923.6	232.8	535.4	110.6	5,802.5
Feb.	319.3	2,131.9	2,451.2	1,079.6	1,420.7	4,951.5	233.3	547.3	109.5	5,841.7
March	327.2	2,170.3	2,497.5	1,073.0	1,435.8	5,006.4	224.0	555.7	99.6	5,885.7
Apr.	336.3	2,190.9	2,527.2	1,082.1	1,443.1	5,052.4	230.5	565.3	125.0	5,973.2
May	343.8	2,217.7	2,561.5	1,097.4	1,450.5	5,109.4	231.7	571.7	103.6	6,016.4
June	351.0	2,254.4	2,605.4	1,060.6	1,464.0	5,130.1	215.0	571.0	99.8	6,015.8
July.	361.5	2,223.3	2,584.8	1,064.1	1,475.3	5,124.3	219.9	584.9	94.2	6,023.3
Aug.	362.7	2,210.5	2,573.2	1,070.1	1,482.7	5,126.0	217.1	587.2	92.3	6,022.6
Sept.	364.8	2,250.8	2,615.6	1,038.6	1,482.8	5,137.0	211.5	576.9	87.6	6,013.0
Oct.	371.3	2,249.1	2,620.4	1,049.6	1,487.9	5,157.9	224.7	582.3	99.6	6,064.5
Nov.	379.2	2,288.6	2,667.8	1,043.5	1,494.8	5,206.0	224.7	585.2	99.3	6,115.3
Dec.	397.9	2331.4	2,729.3	1,039.0	1,529.6	5,297.9	208.7	581.4	88.5	6,176.5
2004 Jan.	389.1	2,314.0	2,703.1	1,021.5	1,547.2	5,271.7	214.6	591.6	90.9	6,168.8
Feb.	393.5	2,310.1	2,703.6	1,016.2	1,553.8	5,273.5	228.6	599.2	92.2	6,193.5
March	399.6	2,346.2	2,745.8	1,005.3	1,559.1	5,310.2	219.4	602.6	89.6	6,221.8
Apr.	409.4	2,361.6	2,771.0	1,006.1	1,567.5	5,344.5	225.5	610.9	94.5	6,275.4
May	416.6	2,372.3	2,788.9	1,015.1	1,573.4	5,377.4	221.9	609.0	91.0	6,299.4
June	423.0	2,410.5	2,833.5	988.8	1,585.7	5,407.9	217.7	609.2	95.0	6,329.9
July	436.2	2,398.5	2,834.7	1,000.2	1,593.3	5,428.1	223.0	613.1	92.7	6,356.9
Aug.	433.4	2,362.8	2,796.2	1,003.2	1,599.0	5,398.4	226.0	624.1	93.8	6,342.3
Sept.	438.0	2,420.3	2,858.4	992.8	1,600.9	5,452.1	217.6	609.5	95.0	6,374.2
Oct.	444.4	2,422.8	2,867.2	1,019.2	1,605.0	5,491.4	230.7	617.1	93.1	6,432.3
Nov.	448.7	2,464.9	2,913.7	1,003.5	1,611.5	5,528.7	225.1	613.4	97.5	6,464.6
Dec.*	468.5	2,474.2	2,942.7	1,043.6	1,641.5	5,627.9	227.5	603.8	100.7	6,560.0

1 Monetary aggregates comprise monetary liabilities of MFIs and central government (Post Office, Treasury) vis-à-vis non-MFI euro area residents excluding central government.
2 Data for the euro area until the end of 2000 concern the Euro-11. As from 1 January 2001. they concern the Euro-12.
3 M3 and its components exclude non-residents' holdings of money market fund shares/units and debt securities up to 2 years.
* Provisional data.
Source: ECB.

T a b l e 9

The Greek contribution to the monetary aggregates of the euro area[1]

(Outstanding balances in billion euro. not seasonally adjusted)

End of period	Overnight deposits			Deposits with an agreed maturity up to two years	Deposits redeemable at notice up to three months[2]	Repurchase agreements (repos)	Money market fund shares/units	Debt securities up to two years	Total[3] (M3 excluding currency in circulation)
		Sight deposits and current accounts	Savings deposits						
	(1)=(1.1)+(1.2)	(1.1)	(1.2)	(2)	(3)	(4)	(5)	(6)	(7)=(1)+(2)+ +(3)+(4)+ +(5)+(6)
2001	70.8	16.1	54.7	29.4	2.4	24.2	9.7	0.1	136.7
2002	71.7	15.2	56.5	28.9	2.3	20.0	10.7	0.2	133.8
2003	79.5	17.6	61.9	32.3	2.0	10.8	15.7	0.5	140.8
2004	91.7	20.7	71.0	33.4	1.9	9.5	15.2	0.5	152.3
2002 Jan.	69.2	14.3	54.9	26.5	2.4	23.9	9.8	0.1	131.9
Feb.	68.9	13.8	55.1	27.3	2.4	23.0	9.4	0.1	131.1
March	67.4	12.5	54.9	27.2	2.4	24.2	9.3	0.1	130.7
Apr.	69.3	13.7	55.6	26.9	2.4	22.9	8.9	0.0	130.4
May	69.0	13.3	55.7	26.6	2.4	22.8	8.9	0.0	129.8
June	70.6	14.2	56.4	26.0	2.3	22.6	8.7	0.0	130.2
July	70.8	14.3	56.5	26.0	2.3	22.5	8.9	0.0	130.6
Aug.	71.3	14.1	57.2	26.3	2.3	22.8	8.9	0.1	131.7
Sept.	72.3	14.7	57.6	25.4	2.3	22.9	9.1	0.1	132.2
Oct.	70.0	13.5	56.5	26.6	2.3	23.2	9.0	0.1	131.2
Nov.	69.1	13.3	55.8	27.3	2.3	22.0	9.1	0.2	130.0
Dec.	71.7	15.2	56.5	28.9	2.3	20.0	10.7	0.2	133.8
2003 Jan.	70.3	14.2	56.1	28.9	2.2	20.2	12.0	0.2	133.7
Feb.	71.8	14.4	57.4	27.1	2.2	19.2	12.9	0.2	133.5
March	72.5	14.9	57.6	27.3	2.2	16.8	14.1	0.2	133.2
Apr.	72.7	14.6	58.1	28.7	2.2	16.3	14.4	0.3	134.7
May	71.9	14.5	57.4	28.8	2.0	15.7	14.7	0.3	133.4
June	74.9	16.7	58.2	29.7	2.1	13.5	15.7	0.4	136.3
July	72.9	15.8	57.1	32.0	2.1	13.0	15.8	0.4	136.3
Aug.	74.0	16.1	57.9	33.0	2.2	12.2	15.7	0.4	137.5
Sept.	74.9	17.1	57.8	32.7	2.1	12.0	15.6	0.4	137.7
Oct.	74.0	16.2	57.8	33.3	2.1	11.8	15.6	0.5	137.3
Nov.	74.1	15.4	58.7	32.9	2.1	11.6	15.5	0.5	136.7
Dec.	79.5	17.6	61.9	32.3	2.0	10.8	15.7	0.5	140.8
2004 Jan.	79.5	17.2	61.6	32.5	2.1	10.6	15.2	0.5	139.7
Feb.	79.6	17.3	62.3	32.1	2.1	10.5	15.2	0.5	139.9
March	82.1	17.8	64.3	31.8	2.1	9.5	15.8	0.4	141.6
Apr.	81.4	17.8	63.6	33.5	2.2	9.1	15.9	0.4	142.5
May	82.5	17.0	65.5	32.2	2.1	8.9	15.6	0.4	141.8
June	84.9	18.3	66.6	32.4	2.1	9.4	15.8	0.4	145.0
July	85.5	18.3	67.2	33.0	2.1	9.3	15.9	0.4	146.2
Aug.	84.9	17.7	67.2	33.2	2.1	9.6	15.8	0.4	146.1
Sept.	86.0	18.7	67.3	33.4	2.1	10.5	15.3	0.5	147.8
Oct.	86.4	18.9	67.5	33.6	2.0	10.4	15.4	0.5	148.2
Nov.	87.5	19.6	67.9	33.8	2.0	10.1	15.3	0.5	149.1
Dec.	91.7	20.7	71.0	33.4	1.9	9.5	15.2	0.5	152.3

1 The Greek contribution begins upon Greece's entry into the euro area (1 January 2001). For statistical reasons, however, the data on monetary aggregates were extended to cover previous years as well.
2 Including savings deposits in currencies other than the euro.
3 As in all other euro area countries, Greece's M3 can no longer be calculated accurately, since part of the quantity of euro banknotes and coins in circulation in each country is held by residents of other euro area countries (as well as non-euro area residents). Owing to these technical problems, the compilation of the Greek M0, M1, M2 and M3 was discontinued in January 2003.
Source: Bank of Greece.

Table 10

Greece: deposits of domestic firms and households with Other MFIs,[1] by currency and type

(Outstanding balances in million euro, not seasonally adjusted)

End of period	Total deposits	Breakdown by currency: Deposits in euro[2]	Breakdown by currency: Deposits in other currencies	Breakdown by type: Sight deposits	Breakdown by type: Savings deposits	Breakdown by type: Time deposits[3]
2001	101,809.5	79,566.0	22,243.5	13,385.2	58,323.1	30,101.1
2002	104,761.1	87,732.3	17,028.8	13,367.3	60,406.1	30,987.7
2003	115,750.1	98,119.3	17,630.8	15,395.8	65,141.1	35,213.2
2004	128,424.6	110,206.7	18,217.9	18,274.2	73,954.2	36,196.1
2002 Jan.	97,542.0	78,693.6	18,848.4	11,839.1	58,355.2	27,347.7
Feb.	98,302.4	79,029.9	19,272.4	11,356.7	58,674.4	28,271.3
March	96,741.8	77,970.2	18,771.6	10,267.5	58,309.6	28,164.7
Apr.	98,685.7	80,274.3	18,411.5	11,584.4	58,979.2	28,122.2
May	97,779.9	79,934.6	17,845.3	10,795.2	59,174.0	27,810.7
June	98,751.5	81,549.4	17,202.1	11,758.3	59,654.1	27,339.2
July	99,132.9	81,816.4	17,316.4	11,888.0	59,768.1	27,476.8
Aug.	99,924.1	82,255.7	17,668.4	11,656.2	60,475.4	27,792.5
Sept.	101,076.4	84,497.2	16,579.2	12,328.6	61,820.2	26,927.6
Oct.	100,492.7	83,175.9	17,316.8	11,399.8	60,572.9	28,519.9
Nov.	100,771.6	83,612.4	17,159.2	11,686.3	59,933.8	29,151.4
Dec.	104,761.1	87,732.3	17,028.8	13,367.3	60,406.1	30,987.7
2003 Jan.	102,687.7	85,423.3	17,264.4	11,703.0	59,707.7	31,277.0
Feb.	102,455.9	85,527.5	16,928.4	12,419.8	60,981.4	29,054.7
March	103,684.4	86,637.5	17,046.9	12,996.7	61,203.6	29,484.0
Apr.	105,407.4	87,642.8	17,764.6	12,664.5	61,690.6	31,052.2
May	104,593.8	86,997.3	17,596.5	12,586.4	60,809.6	31,197.8
June	108,637.5	90,199.0	18,438.5	14,702.7	61,700.5	32,234.3
July	108,694.9	89,934.1	18,760.8	13,670.6	60,471.2	34,553.1
Aug.	110,793.2	91,498.3	19,294.9	14,035.9	61,242.3	35,515.0
Sept.	111,384.5	92,881.7	18,502.8	14,958.4	61,151.5	35,274.5
Oct.	111,068.9	92,207.8	18,861.1	14,024.4	61,020.5	36,024.0
Nov.	110,668.9	92,383.7	18,285.2	13,157.4	61,846.9	35,664.6
Dec.	115,750.1	98,119.3	17,630.8	15,395.8	65,141.1	35,213.2
2004 Jan.	114,996.0	96,977.6	18,018.4	14,874.7	64,645.4	35,476.0
Feb.	115,491.9	97,036.0	18,455.9	15,089.7	66,332.2	34,070.0
March	117,571.4	98,647.3	18,924.1	15,479.0	67,322.0	34,770.4
Apr.	118,835.4	99,526.4	19,309.0	15,687.6	66,697.8	36,450.0
May	118,645.4	99,905.7	18,739.7	14,995.6	68,548.9	35,100.9
June	120,997.2	102,774.4	18,222.8	16,078.1	69,641.4	35,277.7
July	122,396.3	103,778.5	18,617.8	16,368.9	70,186.6	35,840.9
Aug.	122,065.6	103,347.9	18,717.7	15,579.5	70,397.0	36,089.1
Sept.	123,471.3	104,687.8	18,783.6	16,727.8	70,396.8	36,346.7
Oct.	123,971.8	105,394.3	18,577.5	16,840.4	70,593.6	36,537.8
Nov.	124,875.8	106,408.6	18,467.2	17,304.0	70,903.5	36,668.3
Dec.	128,424.6	110,206.7	18,217.9	18,274.2	73,954.2	36,196.1

1 Other Monetary Financial Institutions (Other MFIs) comprise credit institutions other than the Bank of Greece and money market funds.
2 Including (until 31 December 2001) deposits in drachmas and the other euro legacy currencies.
3 Including blocked deposits.
Source: Bank of Greece.

Table 11
ECB and Bank of Greece interest rates
(Percentages per annum)

1. ECB interest rates				2. Bank of Greece interest rates				
With effect from:[1]	Deposit facility	Main refinancing operations[3]	Marginal lending facility	With effect from:	Overnight deposit facility – first tier[4]	Overnight deposit facility – second tier[4]	14-day intervention rate	Lombard rate
1999 1 Jan.	2.00	3.00	4.50	**1999** 14 Jan.	11.50	9.75	12.00	13.50
4 Jan.[2]	2.75	3.00	3.25	21 Oct.	11.00	9.75	11.50	13.00
22 Jan.	2.00	3.00	4.50	16 Dec.	10.25	9.25	10.75	12.25
9 Apr.	1.50	2.50	3.50	27 Dec.	10.25	9.00	10.75	11.50
5 Nov.	2.00	3.00	4.00					
2000 4 Feb.	2.25	3.25	4.25	**2000** 27 Jan.	9.50	8.50	9.75	11.00
17 March	2.50	3.50	4.50	9 March	8.75	8.00	9.25	10.25
28 Apr.	2.75	3.75	4.75	20 Apr.	8.00	7.50	8.75	9.50
9 June	3.25	4.25	5.25	29 June	7.25	–	8.25	9.00
28 June[3]	3.25	4.25	5.25	6 Sept.	6.50	–	7.50	8.25
1 Sept.	3.50	4.50	5.50	15 Nov.	6.00	–	7.00	7.75
6 Oct.	3.75	4.75	5.75	29 Nov.	5.50	–	6.50	7.25
				13 Dec.	4.75	–	5.75	6.50
				27 Dec.	3.75	–	4.75	5.75
2001 11 May	3.50	4.50	5.50					
31 Aug.	3.25	4.25	5.25					
18 Sept.	2.75	3.75	4.75					
9 Nov.	2.25	3.25	4.25					
2002 6 Dec.	1.75	2.75	3.75					
2003 7 March	1.50	2.50	3.50					
6 June	1.00	2.00	3.00					

1 The date refers to the deposit and marginal lending facilities. For main refinancing operations, unless otherwise indicated, changes in the rate are effective from the first operation following the date indicated. The change on 18 September 2001 was effective on that same day.
2 On 22 December 1998 the ECB announced that, as an exception measure between 4 and 21 January 1999, a narrow corridor of 50 basis points would be applied between the interest rates for the marginal lending facility and the deposit facility, aimed at facilitating the transition to the new regime by market participants.
3 Until 21 June 2000: fixed rate tenders, from 28 June 2000: minimum bid rate in variable rate tenders.
4 On 29 June 2000 the second tier of the deposit facility was abolished; the interest rate thereafter applies to the unified deposit acceptance account.
Sources: ECB and Bank of Greece.

T a b l e 12

Money market interest rates

(Percentages per annum, period averages)

Period	Overnight deposits[1]	1-month deposits[2]	3-month deposits[2]	6-month deposits[2]	9-month deposits[2]	12-month deposits[2]
2000	8.24	8.28	7.89	7.32	6.90	6.55
2001	4.39	4.33	4.26	4.15	4.10	4.08
2002	3.29	3.30	3.32	3.35	3.41	3.49
2003	2.32	2.35	2.33	2.31	2.31	2.34
2004	2.05	2.08	2.11	2.15	2.20	2.27
2002 Jan.	3.29	3.35	3.34	3.34	3.39	3.48
Feb.	3.28	3.34	3.36	3.40	3.48	3.59
March	3.26	3.35	3.39	3.50	3.65	3.82
Apr.	3.32	3.34	3.41	3.54	3.70	3.86
May	3.31	3.37	3.46	3.62	3.80	3.95
June	3.35	3.38	3.46	3.59	3.73	3.87
July	3.30	3.36	3.41	3.48	3.54	3.64
Aug.	3.29	3.33	3.35	3.38	3.40	3.44
Sept.	3.32	3.32	3.31	3.27	3.23	3.24
Oct.	3.30	3.31	3.26	3.17	3.12	3.13
Nov.	3.30	3.23	3.12	3.04	3.01	3.02
Dec	3.09	2.98	2.94	2.89	2.87	2.87
2003 Jan.	2.79	2.86	2.83	2.76	2.72	2.71
Feb.	2.76	2.77	2.69	2.58	2.53	2.50
March	2.75	2.60	2.53	2.45	2.42	2.41
Apr.	2.56	2.58	2.53	2.47	2.45	2.45
May	2.56	2.52	2.40	2.32	2.27	2.26
June	2.21	2.18	2.15	2.08	2.04	2.01
July	2.08	2.13	2.13	2.09	2.07	2.08
Aug.	2.10	2.12	2.14	2.17	2.21	2.28
Sept.	2.02	2.13	2.15	2.18	2.21	2.26
Oct.	2.01	2.10	2.14	2.17	2.23	2.30
Nov.	1.97	2.09	2.16	2.22	2.31	2.41
Dec	2.06	2.13	2.15	2.20	2.28	2.38
2004 Jan.	2.02	2.08	2.09	2.12	2.15	2.22
Feb.	2.03	2.06	2.07	2.09	2.11	2.16
March	2.01	2.04	2.03	2.02	2.02	2.06
Apr.	2.08	2.05	2.05	2.06	2.11	2.16
May	2.02	2.06	2.09	2.14	2.21	2.30
June	2.03	2.08	2.11	2.19	2.29	2.40
July	2.07	2.08	2.12	2.19	2.26	2.36
Aug.	2.04	2.08	2.11	2.17	2.22	2.30
Sept.	2.05	2.08	2.12	2.20	2.28	2.38
Oct.	2.11	2.09	2.15	2.19	2.25	2.32
Nov.	2.09	2.11	2.17	2.22	2.27	2.33
Dec	2.05	2.17	2.17	2.21	2.25	2.30
2005 Jan.	2.08	2.11	2.15	2.19	2.25	2.31

1 Until end-December 2000: interbank overnight rate in Greece. As from January 2001: euro overnight index average (EONIA).

2 Until end-December 2000: interbank rates (ATHIBOR). As from January 2001: euro interbank offered rates (EURIBOR).

Sources: Bank of Greece and Bloomberg.

Table 13
Greek government paper yields
(Percentages per annum, period averages)

Period	Yield on one-year Treasury bills	Bond yields					
		3-year	5-year	7-year	10-year	15-year	20-year
2000	6.22	5.99	5.98	6.05	6.10	6.26	6.35
2001	4.08	4.28	4.58	4.82	5.30	5.51	5.76
2002	3.50	4.06	4.45	4.78	5.12	5.24	5.52
2003	2.34	2.82	3.37	3.83	4.27	4.32	4.91
2004	2.27	2.87	3.37	3.81	4.25	4.53	4.77
2002 Jan.	3.48	4.27	4.51	4.95	5.24	5.36	5.55
Feb.	3.59	4.37	4.73	5.07	5.31	5.41	5.60
March	3.81	4.58	5.00	5.27	5.51	5.58	5.78
Apr.	3.86	4.59	4.99	5.27	5.51	5.60	5.84
May	3.98	4.63	5.00	5.27	5.52	5.60	5.86
June	3.87	4.46	4.81	5.09	5.36	5.47	5.71
July	3.65	4.23	4.59	4.90	5.21	5.33	5.57
Aug.	3.44	3.90	4.29	4.60	4.95	5.07	5.34
Sept.	3.24	3.59	3.98	4.33	4.73	4.86	5.18
Oct.	3.13	3.52	3.95	4.34	4.79	4.94	5.32
Nov.	3.02	3.40	3.87	4.26	4.76	4.90	5.33
Dec.	2.87	3.19	3.63	4.05	4.58	4.71	5.13
2003 Jan.	2.70	2.91	3.36	3.81	4.43	4.51	4.97
Feb.	2.50	2.65	3.31	3.89	4.24	4.27	4.83
March	2.41	2.82	3.38	3.83	4.26	4.33	4.90
Apr.	2.46	2.99	3.50	3.96	4.38	4.45	5.02
May	2.25	2.64	3.12	3.57	4.02	4.09	4.73
June	2.02	2.38	2.88	3.33	3.81	3.86	4.57
July	2.08	2.62	3.18	3.65	4.12	4.16	4.83
Aug.	2.28	2.98	3.51	3.91	4.29	4.34	4.90
Sept.	2.26	2.91	3.47	3.91	4.32	4.37	4.96
Oct.	2.30	2.94	3.52	3.95	4.38	4.43	5.02
Nov.	2.41	3.06	3.67	4.09	4.51	4.55	5.10
Dec.	2.38	2.97	3.58	4.02	4.45	4.49	5.04
2004 Jan.	2.21	2.71	3.34	3.81	4.37	4.33	4.94
Feb.	2.17	2.91	3.28	3.90	4.35	4.28	4.91
March	2.06	2.71	3.26	3.71	4.17	4.43	4.75
Apr.	2.16	2.90	3.45	3.90	4.35	4.72	4.88
May	2.30	3.08	3.63	4.07	4.49	4.86	5.01
June	2.41	3.19	3.73	4.15	4.55	4.89	5.03
July	2.36	3.07	3.61	4.03	4.44	4.79	4.93
Aug.	2.30	2.91	3.43	3.85	4.28	4.63	4.78
Sept.	2.37	2.91	3.40	3.79	4.22	4.56	4.70
Oct.	2.32	2.76	3.25	3.65	4.11	4.47	4.61
Nov.	2.33	2.66	3.12	3.53	3.97	4.33	4.47
Dec.	2.30	2.59	2.98	3.36	3.77	4.10	4.24
2005 Jan.	2.31	2.72	2.96	3.29	3.69	3.99	4.12

Source: Bank of Greece.

Table 14
Greece: domestic MFI loans to domestic firms and households, by branch of economic activity
(Balances in million euro)

End of period	Total	In euro	In foreign currency	Branch of economic activity: Agriculture	Industry[1]	Trade	Housing	Tourism	Consumer credit	Other
2000	59,330.0	50,065.6	9,264.4	3,884.9	11,823.7	12,374.2	11,271.9	1,814.3	5,511.3	12,649.7
2001	74,027.4	66,722.6	7,304.8	3,724.2	12,614.9	15,524.3	15,652.2	2,171.3	7,852.0	16,488.5
2002	86,510.5	80,099.7	6,410.8	3,224.7	14,364.0	15,670.8	21,224.7	2,903.2	9,755.4	19,367.7
2003	101,178.1	95,649.4	5,528.7	3,082.7	15,865.1	16,514.4	26,534.2	3,488.2	12,409.6	23,283.9
2004	117,201.7	111,951.1	5,250.6	3,248.0	15,675.6	18,821.6	33,126.8	4,040.0	17,053.8	25,235.9
2002 Jan.	73,982.0	66,648.1	7,333.9	3,230.0	12,435.1	15,174.6	16,024.7	2,236.0	7,783.7	17,097.9
Feb.	75,202.2	67,723.9	7,478.3	3,030.3	12,724.5	15,846.7	16,417.5	2,267.5	7,944.7	16,971.0
March	76,235.3	69,080.0	7,155.3	3,139.4	13,168.1	15,788.0	16,891.9	2,316.4	8,129.8	16,801.7
Apr.	76,958.0	69,886.9	7,071.1	3,196.1	12,801.1	15,939.4	17,362.1	2,341.0	8,301.2	17,017.1
May	78,009.6	71,192.8	6,816.8	3,193.0	12,912.6	16,064.7	17,721.8	2,372.2	8,508.3	17,237.0
June	79,960.9	73,475.3	6,485.6	3,167.7	13,360.0	16,516.2	18,194.3	2,414.5	8,678.1	17,630.1
July	81,233.9	74,622.8	6,611.1	3,167.7	13,720.8	16,570.9	18,759.9	2,411.6	8,868.0	17,735.0
Aug.	82,041.4	75,311.8	6,729.6	3,191.4	13,625.4	16,580.6	19,304.9	2,399.3	8,997.7	17,942.1
Sept.	82,662.6	75,930.7	6,731.9	3,212.8	13,785.6	16,059.8	19,503.8	2,560.0	9,228.1	18,312.5
Oct.	83,996.1	77,164.1	6,832.0	3,221.6	13,961.2	16,161.2	19,914.7	2,635.0	9,420.9	18,681.5
Nov.	85,614.8	78,732.9	6,881.9	3,167.1	14,528.2	15,663.2	20,416.6	2,761.1	9,612.9	19,465.7
Dec.	86,510.5	80,099.7	6,410.8	3,224.7	14,364.0	15,670.8	21,224.7	2,903.2	9,755.4	19,367.7
2003 Jan.	88,241.8	81,751.6	6,490.2	2,964.2	14,529.2	16,321.5	21,599.4	2,978.4	9,884.9	19,964.2
Feb.	88,787.7	82,332.2	6,455.5	2,980.5	14,485.6	16,310.3	22,062.6	3,049.0	10,023.3	19,876.4
March	89,363.0	83,075.2	6,287.8	2,994.0	14,422.3	16,053.5	22,366.8	3,095.5	10,247.3	20,183.6
Apr.	90,770.3	84,710.6	6,059.7	3,043.0	14,565.0	16,113.4	22,747.1	3,149.2	10,344.7	20,807.9
May	92,497.1	86,811.4	5,685.7	3,027.6	14,866.7	16,488.6	23,183.1	3,085.8	10,432.6	21,412.7
June	94,344.1	88,447.4	5,896.7	3,062.3	15,165.2	16,139.3	23,705.7	3,201.0	10,600.9	22,469.7
July	96,253.7	90,203.0	6,050.7	3,062.9	15,674.1	16,307.5	24,267.2	3,207.5	10,871.8	22,862.7
Aug.	97,350.8	91,177.5	6,173.3	3,102.1	15,681.4	16,700.8	24,573.2	3,255.1	11,075.2	22,963.0
Sept.	97,747.2	91,865.5	5,881.7	3,103.0	15,544.4	16,612.9	25,043.9	3,278.1	11,301.1	22,863.8
Oct.	98,403.4	92,480.6	5,922.8	3,117.3	15,481.2	16,393.0	25,559.5	3,321.0	11,670.4	22,861.0
Nov.	99,829.3	94,044.9	5,784.4	3,093.6	15,780.9	16,633.3	25,808.6	3,392.4	12,063.2	23,057.3
Dec.	101,178.1	95,649.4	5,528.7	3,082.7	15,865.1	16,514.4	26,534.2	3,488.2	12,409.6	23,283.9
2004 Jan.	102,748.9	96,982.9	5,766.0	3,055.4	16,005.1	16,822.7	26,902.8	3,536.8	12,690.8	23,735.3
Feb.	103,899.7	98,214.0	5,685.7	3,042.0	15,948.2	17,060.8	27,334.5	3,587.7	13,041.9	23,884.6
March	105,263.2	99,372.4	5,890.8	3,095.5	15,831.8	17,012.4	27,894.2	3,661.6	13,442.3	24,325.4
Apr.	106,447.1	100,530.0	5,917.1	3,150.5	15,734.1	17,134.7	28,465.8	3,703.2	13,798.6	24,460.2
May	108,835.0	103,158.1	5,676.9	3,242.6	15,950.4	17,773.5	29,080.6	3,766.9	14,169.3	24,851.7
June	109,806.8	104,096.1	5,710.7	3,324.8	15,831.1	17,952.6	29,035.7	3,801.5	14,585.6	25,275.5
July	111,624.2	105,976.3	5,647.9	3,348.0	15,997.2	18,214.6	29,822.1	3,862.7	14,985.2	25,394.4
Aug.	111,905.0	106,222.2	5,682.8	3,376.4	15,740.2	18,062.7	30,244.2	3,841.8	15,327.8	25,311.9
Sept.	113,392.1	107,821.5	5,570.6	3,402.8	15,743.6	18,335.8	30,832.5	3,865.3	15,722.9	25,489.2
Oct.	114,868.1	109,490.1	5,378.0	3,397.8	15,988.2	18,687.8	31,404.7	3,987.5	16,114.1	25,288.0
Nov.	115,636.5	110,275.4	5,361.1	3,303.2	15,755.2	18,612.8	32,138.9	3,930.4	16,580.3	25,315.7
Dec.	117,201.7	111,951.1	5,250.6	3,248.0	15,675.6	18,821.6	33,126.8	4,040.0	17,053.8	25,235.9

1 Comprising manufacturing and mining.
Source: Bank of Greece.

Table 15

Greece: bank rates on new euro-denominated deposits of, and loans to, euro area residents

(Percentages per annum)

Period		Deposits by households			Deposits by non-financial corporations		Repurchase agreements (repos)[3]
		Overnight deposits[1,2]	Savings deposits[2]	Deposits with agreed maturity up to one year[3]	Overnight deposits[2]	Deposits with agreed maturity up to one year[3]	
2002	Sept	1.57	1.57	3.13	0.84	3.36	3.22
	Oct.	1.56	1.57	3.17	0.90	3.39	3.01
	Nov.	1.55	1.55	3.15	0.84	3.46	3.17
	Dec.	1.10	1.09	2.93	0.74	3.10	2.97
2003	Jan.	1.10	1.09	2.83	0.74	2.88	2.75
	Feb.	1.10	1.10	2.73	0.75	2.79	2.71
	March	1.06	1.05	2.68	0.69	2.40	2.54
	Apr.	1.05	1.04	2.70	0.73	2.67	2.46
	May	1.04	1.03	2.61	0.70	2.66	2.45
	June	0.82	0.81	2.44	0.55	2.41	2.10
	July	0.80	0.79	2.38	0.60	2.36	2.04
	Aug.	0.81	0.79	2.29	0.52	2.31	2.00
	Sept.	0.81	0.80	2.30	0.55	2.30	1.98
	Oct.	0.87	0.85	2.27	0.62	2.37	1.98
	Nov.	0.87	0.85	2.29	0.54	2.33	1.94
	Dec.	0.87	0.86	2.22	0.59	2.35	1.98
2004	Jan.	0.88	0.86	2.26	0.55	2.18	1.99
	Feb.	0.88	0.87	2.18	0.57	2.17	1.98
	March	0.89	0.87	2.29	0.54	2.13	1.95
	Apr.	0.89	0.88	2.26	0.56	2.13	1.97
	May	0.90	0.89	2.24	0.56	2.23	1.95
	June	0.91	0.90	2.29	0.54	2.16	1.97
	July	0.91	0.91	2.32	0.56	2.18	1.97
	Aug.	0.92	0.91	2.31	0.60	2.19	1.96
	Sept.	0.93	0.92	2.33	0.53	2.12	1.97
	Oct.	0.94	0.93	2.35	0.53	2.17	1.98
	Nov.	0.95	0.94	2.36	0.51	2.18	2.00
	Dec.	0.96	0.94	2.30	0.55	2.20	2.01

1 The rate on overnight deposits by households is the weighted average of the current account rate and the savings deposit rate.
2 End-of-month interest rate.
3 Average monthly rate.
Source: Bank of Greece.

T a b l e 15 *(continued)*

Greece: bank rates on new euro-denominated deposits of, and loans to, euro area residents

(Percentages per annum)

Period	Loans to households[1]					Loans to non-financial corporations[1]		
		Consumer loans[4]		Housing loans[4]			With a floating rate or an initial rate fixation of up to one year[4]	
	Loans without defined maturity[2,3]	With a floating rate or an initial rate fixation of up to one year	Total consumer loans average rate	With a floating rate or an initial rate fixation of up to one year	Total housing loans average rate	Loans without defined maturity[3,5]	Up to €1 million	Over €1 million
2002 Sept.	14.40	10.86	10.43	4.62	4.74	7.31	6.64	5.33
Oct.	14.51	10.69	10.45	4.65	4.81	7.28	6.37	4.98
Nov.	14.48	10.87	10.61	4.56	4.75	7.23	5.78	4.54
Dec.	14.54	10.58	10.45	4.42	4.61	7.23	5.76	4.50
2003 Jan.	14.71	10.46	10.17	4.53	4.77	7.15	5.53	4.39
Feb.	14.68	11.13	10.60	4.58	4.81	7.09	5.59	4.27
March	14.66	10.82	10.76	4.58	4.87	7.04	5.37	4.06
Apr.	14.76	11.15	10.82	4.58	4.93	7.07	5.55	4.14
May	14.58	11.13	10.70	4.59	4.93	6.95	5.68	3.76
June	14.54	10.61	10.44	4.53	4.86	6.84	5.15	3.47
July	14.24	10.41	10.33	4.37	4.66	6.70	5.06	3.68
Aug.	14.05	10.24	10.37	4.48	4.76	6.67	4.95	3.60
Sept.	14.14	10.37	10.60	4.62	4.81	6.67	5.14	4.27
Oct.	14.22	10.57	10.58	4.57	4.81	6.68	5.24	4.68
Nov.	14.27	10.36	10.46	4.35	4.63	6.72	5.14	3.66
Dec.	14.08	9.60	9.86	4.31	4.53	6.78	5.13	3.78
2004 Jan.	13.92	9.82	9.94	4.36	4.68	6.74	5.12	3.92
Feb.	13.97	9.94	9.99	4.35	4.63	6.85	5.16	4.09
March	14.00	9.44	9.87	4.37	4.63	7.13	4.88	3.45
Apr.	14.06	9.56	9.85	4.36	4.55	7.11	5.15	3.49
May	13.79	9.82	10.07	4.33	4.54	7.02	4.91	3.45
June	13.89	9.71	10.05	4.30	4.54	7.06	4.89	3.58
July	13.84	9.60	9.67	4.24	4.43	7.03	4.84	3.53
Aug.	13.77	9.70	10.05	4.34	4.53	7.06	4.95	3.52
Sept.	13.62	9.37	9.91	4.23	4.43	7.05	4.87	3.80
Oct.	13.72	9.68	9.87	4.29	4.45	7.02	4.86	3.83
Nov.	13.75	9.40	9.72	4.23	4.36	7.05	5.06	3.61
Dec.	13.41	8.58	9.36	4.21	4.37	6.97	5.04	3.77

1 Associated costs are not included.
2 The interest rate is the weighted average of the rates on loans to households through credit cards. on open account loans and on overdrafts from current accounts.
3 End-of-month interest rate.
4 Average monthly rate.
5 The interest rate is the weighted average of the rates on corporate loans via credit lines and on overdrafts from sight deposit accounts.
Source: Bank of Greece.