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Greece

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Signs of revival after years of pain

Confidence is slowly returning but hurdles still loom ahead, writes *Kerin Hope*

The signs of economic crisis are visible everywhere in Athens, from shuttered shops and graffiti-sprayed public buildings to people of all ages ransacking dustbins in wealthier neighbourhoods of the capital.

Six years of recession, the deepest in memory, have taken a heavy toll on Greece.

The country's output shrank by almost 25 per cent, as tens of thousands of family-owned businesses collapsed, while pensioners and the unemployed suffered a disastrous fall in living standards amid deep cuts in social spending.

With jobs disappearing at an unprecedented rate, more than 100,000 skilled Greeks migrated to work in Germany, the UK and the Gulf states, knowing that it may be years before they can resume careers at home.

The crisis also pushed desperate Greeks into voting for insurgent yet backward-looking parties, Syriza on the far left and the neo-Nazi Golden Dawn on the right. Both support a return to statist policies that triggered financial collapse and the threat of a "Grexit" – Greek exit – from the euro.

Yet there are signs that wrenching reforms imposed in return for the current €172bn bailout by the EU and the International Monetary Fund are finally starting to bear fruit.

Growth is set to turn positive this year and accelerate in 2015, driven by a boom in tourism, the revival of EU-backed infrastructure projects stalled by disputes with contractors, and the increasing availability of loans from newly recapitalised banks.

Cup that cheers: fans at the Fifa World Cup in Brazil, where Greece reached the last 16 for the first time AP

Greece's successful return to international capital markets in April has boosted confidence in the country's medium-term prospects, encouraging hedge funds and private equity groups to take a closer look at Greek companies that have survived the crisis.

Budget figures for the first five months show revenues on track to hit this year's target of a primary surplus of 1.5 per cent of national output, before interest payments. This suggests that improvements in tax collection are being maintained, even though a small group of politically-connected Greeks are still able to avoid paying their full tax obligations.

These developments contribute to the narrative of a Greek "success story" being promoted by prime minister Antonis Samaras and his government. However, more hurdles must be overcome before Greece can claim to be heading for a sustained recovery.

The first is the European Central Bank's stress testing of eurozone banks this year, which is expected to give an accurate picture of Greek lenders' non-performing loan portfolios, settle a long-running debate about the banks' recapitalisation needs and lead to writedowns of bad debt on a scale that will prevent "zombie" companies from draining funds needed for healthy businesses to grow.

Then come long-awaited negotiations with the EU and IMF on debt relief. These are made more complicated by differences over whether Greece should be offered another debt "haircut" on top of its 2012 sovereign debt restructuring as the Fund would prefer, or settle for the commission's proposal of a lower interest rate and a lengthening of maturities.

"We will be in a room with two elephants and we'll have to tiptoe between them in order to come away with an agreement," says a senior Greek official. "But what matters is to reduce the debt burden for the next generation by one means or another."

A third worry for Mr Samaras is the election by parliament next February of a new president to replace the incumbent Karolos Papoulias, who is retiring.

If parliament fails to elect a president with the required three-fifths majority, a general election must be held, which pollsters already forecast would lead to the formation of another coalition government. This would delay the completion of structural reforms aimed at boosting competition and making Greece more attractive to investors.

Still to be addressed is the politically sensitive question of a new aid package for Greece after the current EU programme runs out at the end of this year, even though the IMF is to disburse another €16bn over the next 18 months.

The "troika" of officials from the commission, the IMF and the European Central Bank have identified a looming funding gap of some €12bn, yet Greek finance ministry officials claim it is smaller and can be plugged through careful management of the public finances and judicious borrowing on international capital markets.

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Exports bolster sales at mattress maker Coco-Mat
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Credit expansion and loan quality are priorities

Banks

The ECB stress tests are focusing minds, says *Dimitris Kontogiannis*

Greece's economy is stabilising after six years of recession and will need credit expansion to achieve a sustained revival of growth.

Yet the country's four systemically important banks, recapitalised with more than €35bn over the past year, are taking a cautious stance ahead of this year's European Central Bank stress tests.

With one of the world's highest ratios of non-performing loans, Greek banks are under pressure to deal with bad loans more effectively, while continuing to support creditworthy corporations and households.

Yannis Stournaras, the new central bank governor, says loans left unserviced for more than 90 days stood at €77bn or 36 per cent of the total portfolio in April. Senior Greek bankers say they are expected to peak early next year.

One of Mr Stournaras's first tasks will be to consider whether Greece should set up a standalone "bad bank" for systemic banks' non-performing loans – which would require additional funding – or rely on pressing the banks' internal restructuring units to move faster.

Previous efforts to restructure key sectors that have a high percentage of bad loans – among them the hotel, construction and fish-farming industries – have been constrained by difficulties in persuading banks and company owners to co-operate.

The Greek banks were initially recapitalised with €25bn from bailout funds held by the Hellenic Financial Stability Fund (HFSF), plus another €3bn raised privately.

This year the four banks have raised another €8.3bn on international capital markets to bolster capital adequacy ratios, following a stress test carried out by the Bank of Greece together with BlackRock, an investment management company. The fund-raisings have also allowed banks to repay preference shares held by the Greek state.

However, the International Monetary Fund says banks may need as much as €15bn in extra capital to write down bad loans more aggressively. It argues that an overhang of private debt will undermine growth if resources remain trapped in unproductive activities.

Some local analysts disagree. Kostas Manolopoulos, head of research at Investment Bank of Greece, says: "The assumptions in the Greek central bank's stress tests were quite conservative, and banks are already overcapitalised."

Politicians and business-people complain the economy is being stifled by a lack of liquidity, because banks are reluctant to extend credit to support a recovery. They point out that credit to the private sector has been shrinking since 2010, falling another 3.7 per cent in April on an annual basis.

Bankers are quick to reject such criticism. Chris Megalou, chief executive of Athens-based Eurobank, says: "The credit contraction is mainly a function of weak demand and stricter credit controls."

> 'The banks' role will be to fund ventures in extrovert sectors that have robust business models'

Mr Megalou says an improving economic outlook will drive demand for loans, especially for new investment projects.

Nikos Lianeris, an analyst at Alpha Bank, says the effort to transform Greece's introverted, consumption-oriented economy into one based on exports and investment has already "left many corporate borrowers with business models based on the old paradigm in distress.

"We shouldn't expect the restructured Greek banking sector to help revive such companies through liquidity injections. The role of banks will be to fund ventures in extrovert sectors that have robust business models," Mr Lianeris says.

However, the banks' capacity to boost lending will also depend on their access to the ECB's new programme of cheap loans known as "targeted long-term refinancing operations" or TLTRO.

The four-year programme, aimed at investment in non-financial, productive sectors of the economy, is intended to benefit small and medium-sized enterprises (SMEs) that have been starved of credit. The loans will be offered from September, with banks able to borrow at 0.25 per cent provided they meet the ECB's lending target.

Greek banks have lost more than €79bn of deposits since the crisis erupted in 2009, through capital flight and withdrawals of savings by households hit hard by the recession. Until their recent return to capital markets, the banks relied heavily on ECB funding and emergency liquidity assistance from the Greek central bank.

Petros Christodoulou, deputy chief executive at National Bank of Greece, the second-largest commercial lender, is cautious about TLTRO funding, even though it would allow banks to provide liquidity injections to SMEs.

He says: "We don't have enough information at this point about the kind of collateral required for TLTRO operations to be able to determine the amount of liquidity Greek banks could look forward to."

Cheaper debt marks change in fortunes

Capital markets

After the woes of four years ago, sentiment turns, says *Ralph Atkins*

In just a few hours one day in early April, Greece demonstrated just how much the tide of global investor sentiment had turned in its favour.

The country's first foray into global capital markets in four years saw about €20bn of orders for €3bn of five-year government bonds flood into the banks organising the deal. This enabled Greece to borrow at a much lower cost than had been expected – the bonds were priced to yield just 4.95 per cent.

The contrast with the mood at the height of the country's crisis could hardly have been greater.

When Greece's debt woes erupted into a eurozone-wide threat, the cost at which investors were prepared to lend to its government soared – in effect denying it access to capital markets.

On five-year bonds, yields – which move inversely with prices – had reached 14.5 per cent by May 2010. Greece's future in the eurozone was in doubt; its economy came close to collapse.

This year, Greece has come back from the near-dead. "Markets appreciate the impressive turnaround story that Greece has realised so far," says Stelios Papadopoulos, director-general of the Public Debt Management Agency. "One needs to seize the moment and take advantage of opportune market trends."

It is not just the government that has raised funds in debt markets. Greek banks have taken advantage of the change in sentiment to strengthen balance sheets, raising funds more cheaply than would have been thought possible a few years ago.

The success of April's debt auction did not mean investors thought Greece's crisis was over. Many remain wary of structural weaknesses even in basic areas such as collecting taxes as well as the country's high debt levels. Public sector debt will be equivalent to almost 180 per cent of gross domestic product this year, according to the European Commission.

"Greece's debt stock is way too large, given its inability [to conduct] effective taxation and given its growth dynamic," warns Michael Hasenstab, global bond portfolio manager at Franklin Templeton.

He bought Irish government bonds and has invested heavily in Ukraine. Yet he warned in a Financial Times interview last month: "The underlying fundamentals don't justify an investment in Greece."

Two factors have this year worked in Greece's favour, however. First, has been the global "hunt for yield". Historically low official interest rates globally have sent international investors searching for riskier assets offering higher returns. For some at least, Greece fitted the bill.

Second, evidence has mounted that Greece's fortunes have changed. "We have reached an inflection point," says George Saravelos, a Deutsche Bank strategist. "The big problem over the past three years was that we could not see the light at the end of the tunnel in terms of stability.

"But at the end of last year, things stopped getting worse. It changed perceptions."

Greece has reduced its current account deficit and is running a budget surplus before interest payments. Moreover, the international help it has received since 2010 means its debt-to-GDP ratios are less relevant to investors looking over, say, the next three to five years. Greece's average debt maturity is exceptionally long – more than 17 years – and may be extended further.

The government's return to debt issuance has more than symbolic importance. Structural reforms are more efficient when access to capital markets is maintained, argues Mr Papadopoulos.

The debt agency's strategic goal is to recreate the Greek bond market's "yield curve" – offering a range of bonds of different maturities in order to increase its attractiveness to a range of investors. "To attract foreign direct investment and promote growth in the current environment, restoring proper access to markets for both the sovereign and banks is essential," Mr Papadopoulos says.

> 'At the end of last year, things stopped getting worse. It changed perceptions'

Alongside the government bond issuance was the wave of capital raising by the country's banks.

Before April's sovereign bond launch, Piraeus Bank became the first Greek bank to return to the capital markets with a €500m benchmark bond. A few weeks afterwards, National Bank of Greece, the country's second largest commercial lender, borrowed €750m at a lower cost than the sovereign.

Big Greek companies have also increased bond sales. Total Greek debt issuance by companies and public-sector institutions has exceeded €10bn so far this year. This compares with just €6.4bn for all of 2013 – although it remains well below pre-crisis rates, according to Dealogic data.

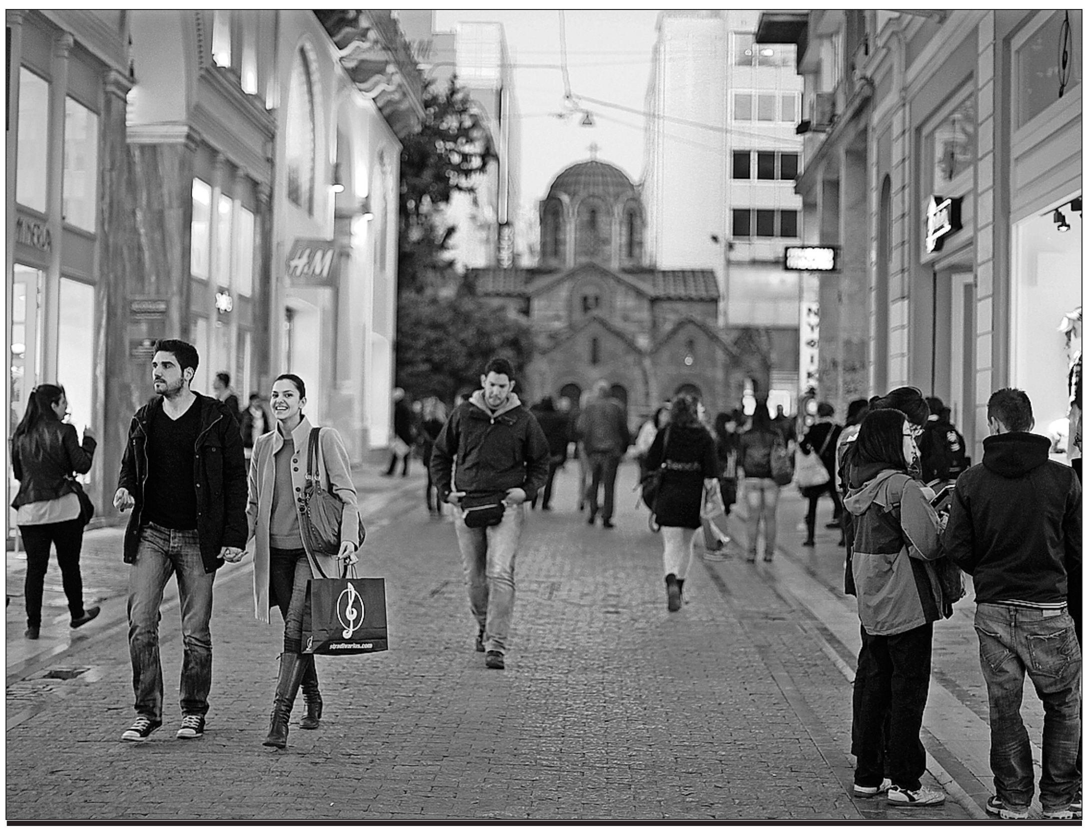
The wave of bank capital raising – in equity as well as debt markets – has enabled Greece to rebuild its financial system after the traumas of the past few years at a much faster pace than expected.

That could help the country's turnround, allowing the banking system to perform its core function of providing finance to the economy.

"Greek banks are more confident about expanding their balance sheets and lending," says Mr Saravelos at Deutsche Bank.

Concerns linger on growth as IMF calls for further reforms

Economy Business confidence is at a six-year high but more needs to be done to make the recovery sustainable, writes *Kerin Hope*



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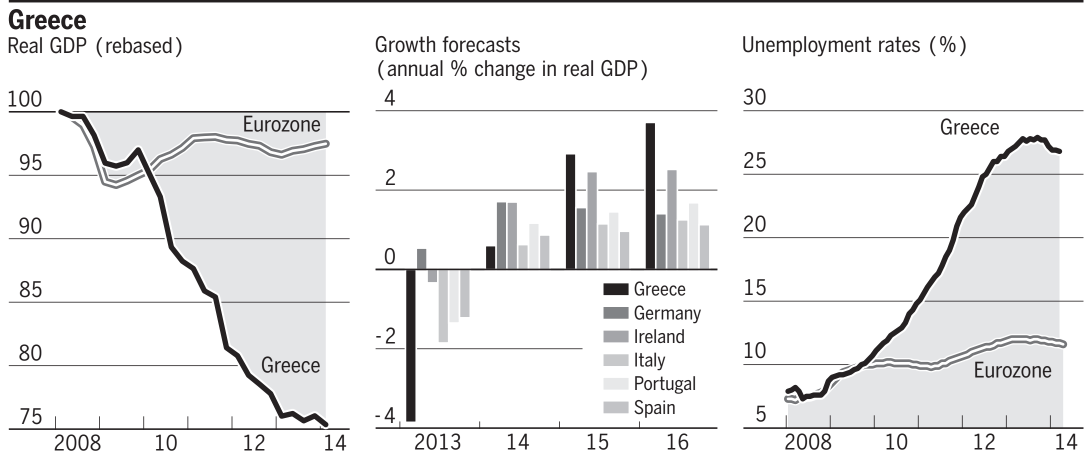

Sources: Thomson Reuters Datastream; IMF

Shoppers splash out: April's rise in retail sales was the strongest in more than two years Charlie Bibby

Greece is poised to return to growth this year after the longest and deepest recession since the second world war.

However, more reforms must be implemented before a sustained recovery can take hold.

For the first time since a joint EU-International Monetary Fund programme veered off track in 2011 – less than a year after it was launched – the IMF says it is cautiously optimistic about Greece's prospects, citing an "extraordinary fiscal adjustment" and a successful re-entry to international capital markets.

A double-digit budget deficit was transformed into a primary surplus (excluding interest payments on debt) in just four years, thanks to draconian spending cuts and an unprecedented drive to boost tax collection.

Finance ministry officials boast that Greece now has the highest "cyclically-adjusted primary balance" in the eurozone, that is, after taking into account the impact of the business cycle on revenues.

The economy is forecast to grow by 0.4-0.6 per cent this year after six straight years of decline, but some analysts are confident that a record year for tourism could lift growth higher, perhaps to 0.9-1.0 per cent.

There are signs that consumers may gradually be regaining confidence. Private consumption rose 0.7 per cent in the first quarter, the first quarterly increase in more than four years.

Retail sales were up 7.3 per cent by volume in April, the strongest rise in more than two years, as Greeks splashed out for Easter at supermarkets and clothing stores.

The business confidence index hit a six-year high in June, with banks reporting increased demand for loans from companies working in recovery-oriented sectors such as energy and infrastructure.

The seasonally adjusted jobless rate is still high at 26.8 per cent, but has edged down from last September's record 27.8 per cent of the workforce.

However, it is unclear whether Greece can pull off sustained annual growth rates of about 3 per cent, the level required to increase the primary surplus to 4.5 per cent of output in 2016 – the target set by international creditors – and make a serious dent in the country's bloated public debt.

George Pagoulatos, professor of political economy at Athens university of business and economics, says: "Growth is the key issue . . . It's a major concern whether the rate will be considerably above the level of stagnation, whether it's sustainable, whether companies can make the export-oriented shift that's needed."

Greece has recovered most of the 30 per cent drop in competitiveness it suffered during the first decade of euro membership as a result of a steep fall in wages, and reforms that have opened up the labour market.

Individual contracts and part-time working, once effectively banned by unions, have become the rule for new entrants to the workforce. Employers' contributions to IKA, the main social security fund, have been cut and pensions slashed across the board.

"The economy that's emerging from the recession is a very different and much healthier animal," says Michael Masourakis, chief economist at Alpha Bank in Athens. "A 3 per cent annual growth rate should be sustainable as we are starting from a lower base."

The IMF warns, however, that further structural reforms "are key for the incipient recovery that we hope to see turn this year into a robust, sustained recovery over the medium term".

> 'The economy that is emerging from the recession is a . . . much healthier animal'

The government has adopted most of the 550-odd reforms in a "toolkit" of measures prepared by the Paris-based Organisation for Economic Co-operation and Development to reduce barriers to competition, yet some measures have been delayed or diluted because of pressure from powerful interest groups.

The 12,000-strong union of pharmacists, for example, successfully resisted the abolition of a guaranteed profit margin on drugs, even though it has been cut from 35 per cent to 15 per cent.

Objections raised by interest groups, the judiciary and, in some cases, EU competition regulators, are deemed responsible for the slow pace of privatisation sales.

A target of raising €50bn by 2025 from sales of state-controlled companies, properties and land for development, has been slashed to €25bn as the scale of legal and administrative obstacles became clear.

The Hellenic Asset Development Fund (Taiped), the privatisation agency, has already cut this year's revenue target from €3.5bn to €1.5bn.

The target will have to be cut again following a recent judgment against the sale of the state's stake in Eydap, the Athens water utility, issued by the council of state, Greece's highest administrative court.

The council unexpectedly ruled that water companies should remain under public ownership on grounds that a for-profit private operator could not be relied on to supply affordable, high-quality services in the public interest.

The decision was seen as a blow to attracting large European entities to participate in Greek disposals.

Miranda Xafa, chief executive of EF Consulting in Athens and a former Greek representative to the IMF, says: "People don't yet have the confidence to invest here. The main inflows have been from hedge funds, so they could be reversed very quickly.

"At the moment, nobody is building plants or making long-term decisions," she adds.

Crisis forces rethink as entrepreneurs win funds for their ventures

Technology start-ups

IT experts are using the home market as a springboard for global success, writes *Kerin Hope*

With the jobless rate among young graduates approaching 40 per cent, the incentive for skilled Greeks to travel abroad to find work is strong.

Yet several hundred young entrepreneurs are testing their abilities by founding technology start-ups at home.

Until the crisis struck, Greece had few aspirations to become an internet hub, even though several university IT departments staffed by US-trained professors who keep up their Silicon Valley connections turn out highly qualified software engineers.

Now there is a drive to catch up.

"The crisis has changed things in a positive way," says Marco Veremis, co-founder and chief executive of Upstream, an Athens-based mobile marketing company.

"There's a start-up culture that's buoyant. It's still early days, but people are working to produce something with value-added."

The bulk of financing for technology start-ups comes from four venture capital funds backed by an EU regional development package covering 70 per cent of a seed capital investment.

Aristos Doxiadis, a private equity professional, says: "There have never been many angel investors in Greece and it was hard to raise funding at the height of the crisis, but there's a community of people here who trust each other, so we managed."

He adds: "Now that several start-ups have taken off, there's growing interest."

Mr Doxiadis is a partner in Openfund II, a €11m operation that provides Greek technology start-ups with business tools and advice for competing in a global market, from guidance on pitching for funding to access to 50 international mentors. It is backed by the EU's European Investment Fund and a dozen private investors.

One early success was Taxibeat, a smartphone application for hailing cabs that was launched in 2011. It made headlines in Athens at a time when taxi services were being disrupted by cabbies resisting reforms of the transport sector.

Taxibeat differs from other taxi-hailing apps by enabling customers to choose the driver they prefer, based on ratings by other passengers plus extras such as speaking fluent English.

Considered a good fit for European cities with heavy tourist traffic and for emerging markets where taxi services are less regulated, Taxibeat has expanded in markets across Europe from Bucharest to Paris and also in Latin America.

"Taxibeat has played a catalytic role for Greek start-ups because it was such a good story," Mr Doxiadis says.

Openfund II has backed 12 start-ups since its launch last year and plans to reach 25 by the end of 2015.

So far, only one company has reached Silicon Valley. Bugsense, which collects and analyses crash reports from mobile apps, was launched in 2010 with a seed investment of $100,000 from a group of Greek diaspora IT experts working in California.

It was sold last year to Splunk, a US-based data analytics company, for an undisclosed amount.

Workable, founded by two former Upstream employees, is tipped as Greece's next success story after raising $1.5m in a new funding round led by Greylock Partners, a Silicon Valley venture capital fund.

Workable is developing cloud-based recruitment software for small and medium enterprises.

"When a Greek start-up raises funding from an international fund, it sends a clear message to investors here," says Mr Veremis, an angel investor and board adviser to Workable.

The Taxibeat hailing app 'has played a catalytic role for Greek start-ups'

Several start-ups aimed at the tourist industry, the most important sector of the economy, have since expanded into global markets.

Incrediblue's website connects yacht-owners and crew with customers who book sailing holidays based on price, location and reviews by users, reducing costs in a fragmented market where local brokers charge high fees.

Locish, a smartphone question-and-answer app that has attracted $820,000 of funding from two Greek venture capital funds, provides travellers with tips from local residents on where to eat and drink in Athens, New York and San Francisco.

Incubators that provide business space along with "open coffee" sessions and weekend meetings give young entrepreneurs an opportunity to exchange ideas and receive feedback, says George Kasselakis, Openfund II's executive director.

Thanos Kosmidis and his partner Alex Giamas work at Microsoft's innovation centre in Athens, which supports several start-ups with technology advice and mentoring.

CareAcross, their English-language website supporting cancer patients and care givers, which is financed with €100,000 of private funding, is at an early stage of development.

"It's useful to have a physical base with a diverse set of people supporting you," says Mr Kosmidis, who worked for 12 years before returning to Greece to start as an entrepreneur.

Greece

Coalition faces critical chapter in its fight for life

Politics European election turmoil emphasises the system's fragmentation, writes *Kerin Hope*

Faces of protest: environmental campaigners outside the Greek parliament, wearing masks of Antonis Samaras (left) and Evangelos Venizelos Getty

Greece's first coalition government in more than a generation looked wobbly from the moment it took office after a hard fought election in June 2012.

Relations are tense between Antonis Samaras, prime minister and leader of the centre-right New Democracy party (ND) and foreign minister Evangelos Venizelos, head of the PanHellenic Socialist Movement (Pasok), the two parties that are held jointly responsible by voters for plunging Greece into economic disaster.

Their junior partner, the Democratic Left of Fotis Kouvelis, a leftwing fringe group, pulled out of the coalition last year over a unilateral decision by Mr Samaras to shut down – albeit temporarily – the state broadcaster ERT.

Mr Kouvelis's departure, along with serial defections by ND and Pasok lawmakers opposed to specific structural measures, has left the government with a majority of only three seats, making a cliffhanger out of every vote on reforms agreed with the "troika" of international lenders: the European Commission, the European Central Bank and the IMF.

Yet the coalition stumbles on, delivering fewer measures than agreed with the troika but still enough to sustain regular disbursements of aid from the country's €172bn second bailout package.

The next few months, however, will be critical for the government's survival. It will face renewed pressure from the troika to implement measures delayed because of opposition by special interest groups, while at the same time seeking a consensus candidate for the (mostly ceremonial) post of president of the republic.

With Karolos Papoulias, the 85-year-old incumbent, due to step down next February, the hunt is on for a personality above politics who can win the required three-fifths majority in parliament and avert an early general election.

"The government could pull this off by persuading a clutch of independent deputies to back their candidate, if it can't find a Greek of international stature to try for the job. But nothing's clear-cut," says Costas Iordanides, a veteran Athenian political commentator and columnist.

ND lost the European parliamentary elections in May to the far-left Syriza party of Alexis Tsipras, who campaigned on a platform of reversing the majority of bailout reforms.

Yet Syriza's win by less than 4 percentage points fell short of the margin that would have signalled the coalition's imminent downfall.

With a combined percentage of 30.73 per cent for ND and Pasok, against 26.5 per cent for Syriza, the coalition could still claim it was backed by a majority of voters, despite an unprecedented jobless rate and record levels of taxation in the past two years.

Yet the election underscored the increasing fragmentation of Greek politics, with voters switching to anti-establishment parties, both left and right.

Syriza has attracted many former Pasok supporters still nurturing hopes of a return to the generous public sector hiring policies of the 1990s, even as the coalition acts to shed jobs in the civil service and privatise state-controlled corporations.

Makis Andronopoulos, an author and political commentator, says: "Syriza doesn't have to move to the centre to have a chance of winning power . . . It only has to wait. The continuing impact of austerity will bring it many more voters who want to make a protest."

To the government's dismay, former ND voters have become the backbone of support for the neo-Nazi Golden Dawn party. It has three European parliament deputies after winning 8.9 per cent of the vote, even though its founder and leader, Nikos Mihaloliakos, was jailed last year and is awaiting trial on charges of founding and running a criminal organisation.

The party spokesman, Ilias Kasidiaris, insists Golden Dawn is a nationalist, not a neo-Nazi, party and denies that its black-shirted members have participated in violent attacks against immigrants. Golden Dawn's 18 deputies in the Greek parliament will all face charges of belonging to a criminal organisation, according to the judiciary, but it is unclear whether the party will be banned.

Then there is To Potami (The River), a pro-reform party founded by a popular television journalist, Stavros Theodorakis and backed by moderates from the centre-left. To Potami won 6.6 per cent of the vote at the European election, only three months after it was launched.

Its programme is still being shaped after a recent congress, yet its supporters are optimistic that Mr Theodorakis will become a key player in Greece's next coalition government.

Signs of revival emerge after six years of pain

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Despite his government's dogged execution of the current programme, Mr Samaras is as keen as Alexis Tsipras, the Syriza leader, to tell voters that the unpopular "memorandum", as the bailout is known in Greece, has expired.

While some Greek officials accept that a precautionary arrangement of some kind will be needed to maintain investor confidence and ensure access to markets, the troika worries that reform fatigue and the influence of powerful vested interest groups could lead to weaker implementation or even the reversal of key measures to liberalise domestic markets.

Yet if Athens can hold the line on reforms, Greece's family-run businesses would have an opportunity to revive the flagging export sector by developing niche markets in food processing, manufacturing and technology, says Mike Efmorfides, co-founder of Coco-Mat, a producer of luxury mattresses.

"We survived the crisis by focusing on exports and developing more outlets abroad. For a small Greek company making a high-quality product, it is the only way to go," he says.

Reforms making it easier for young entrepreneurs to set up a new business and hire part-time staff, together with EU-backed funding for small and medium companies, are making an impact, even though venture capital and bank financing is still in short supply.

"The crisis forced young Greeks to change their mentality and look for a new model," says Mareva Grabowski, a former investment banker and founder of the Greek branch of Endeavor, a global organisation that supports entrepreneurs in emerging markets.

"Their attitude to risk is different and they're willing to try to become entrepreneurs," she adds.

When it comes to large-scale investment, infrastructure projects that take advantage of Greece's strategic location in southeast Europe are taking priority.

Greece is already involved in the Trans-Adriatic Pipeline (TAP) project to transport natural gas from the Shah Deniz field in the Caspian Sea to central Europe. Construction of the Greek segment would provide work for dozens of small Greek construction companies and more than 1,000 jobs across the north of the country, where the unemployment rate exceeds 30 per cent of the workforce.

Socar, the Azeri state gas company, has bought Greece's gas grid operator Desfa in a privatisation sale and plans to invest in extending the distribution network to smaller cities across the country.

€12bn

'Funding gap' identified by the troika

Yet China has emerged as the keenest potential investor in Greece, described by premier Li Keqiang during a visit to Athens last month as Beijing's "gateway to Europe".

Shortly before the crisis erupted, the Chinese state shipping operator Cosco won a concession to operate a container terminal at Piraeus, a successful investment that has since seen further capacity added.

Now Cosco is bidding for the Greek state's majority stake in Piraeus port authority, the port's owner. Other Chinese companies are interested in acquiring concessions to operate the state railway company and Athens International Airport, the city's only international gateway, which will both be up for privatisation next year.

Reform still way short of victory over old habits

Opinion
Tony Barber

In the bigger scheme of Greece's ordeal by financial collapse, it may seem a modest triumph for good government that its ministers and financial police are finally getting to grips with the timeworn scam of welfare cheats claiming pensions on behalf of deceased Greeks.

The perpetrators are a small minority of Greece's 10.8m people, and the sums recovered – about €40m – pale into insignificance next to the public debt of about €320bn, equivalent to 175 per cent of annual economic output.

Yet the elimination of pensions fraud, like the suppression of tax evasion, lies at the core of the modernisation programme on which Greece embarked after its first emergency international financial rescue in May 2010.

It is no exaggeration to say that if these efforts falter, because of a failure to refashion parasitical and mistrustful attitudes to the state that go back to the early days of independence in the 1830s, the pain and suffering that Greek society has endured over the past five years will not have been worthwhile.

For the Greek crisis was always about much more than sky-high sovereign bond yields, excessive budget deficits, rigid labour markets and the cartel-like behaviour of private sector businesses and professional cadres.

It was about social attitudes, respect for the law and the need for a proper relationship between the citizen and the state, a bond stripped of suspicion and cleansed of peculation. It was about whether Greece as a state – rather than Greece as an economy – was fit to share the same currency as Germany.

The nation plunged into calamity because, long before the euro's creation in 1999, generations of Greek politicians and the general public had preferred to think of the state not as a disciplined, impartial dispenser of tax-funded public services, but as a pot to be picked clean by patronage and pilfering.

The wake-up call of 2010, though a shock to the two-party political order that had ruled and misruled Greece since the collapse in 1974 of a seven-year military dictatorship, did not immediately result in improvements.

Entrenched political, bureaucratic and trade union interests proved masterful at sabotaging change in the public sector. As unemployment raced past 25 per cent of the workforce, in the early phase of the crisis the private sector bore the brunt of the hardship.

> 'If these efforts falter, the suffering of the past five years will not have been worthwhile'

Eventually, widespread social distress, the absence of substantive economic reform and the emergence of political extremists on the left and right, coupled with the fear that Greece might drop out of the euro or renege on its obligations to allies and creditors, produced an election victory in June 2012 for a conservative-led coalition.

Led by Prime Minister Antonis Samaras, the new government saw that the sand in the hourglass was running out. A more convincing effort at reform was essential in order to save the economy, Greece's international standing and perhaps democracy itself.

Two years on, the cause of Greek reform is making progress but is way short of comprehensive victory over the forces of inertia and old habits. The tax system is a case in point.

In the pre-crisis era, a profusion of tax offices in geographically remote and technologically backward parts of Greece encouraged taxpayers to reduce their bills by doing deals with corrupt officials. The structure of tax collection was, in itself, an impediment to change.

Now the authorities have shut scores of regional tax offices, bringing stronger centralised control. And information technology has enabled more monitoring of tax assessments. About 2,000 audits a week are conducted at restaurants, shops, doctors' premises and other places suspected of concealing income. Tax revenue is rising.

The system has not been strengthened sufficiently to capture the biggest and wealthiest tax evaders – a point made by Haris Theoharis, Greece's senior tax collection official, when he abruptly resigned in early June, much to the dismay of the nation's European partners. According to Mr Theoharis, 280 investigations of large taxpayers had collected a mere €80m in extra revenues.

This serves as a reminder that the deepest question that will face Greece in the next 12 months is not whether its foreign creditors will agree to another debt relief deal to shore up its eurozone membership.

Nor is it whether the tourism industry, so important a source of foreign income, will enjoy another record-beating season. It is not even whether the Samaras government will fall and there will have to be an early election.

Rather, it is whether the political classes, state employees, business people and the general public will maintain the wrenching effort to place their country on an irreversible path to modernity.

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Drive upmarket as visitor numbers soar

Tourism Capital projects point to a brighter future, write *Dimitris Kontogiannis* and *Kerin Hope*


Ready for take-off: the former Athens International Airport is to be redeveloped into a tourism and leisure hub Getty

Greece is enjoying a record year for tourism, with popular resorts booked to capacity in July and August and international cruise ships queueing up to call at Aegean Island ports.

Visitor numbers jumped by 30 per cent to 1.9m in the first four months of 2014 compared with last year, according to SETE, an association of Greek high-end hoteliers and tour operators. Athens saw a 36 per cent rise in arrivals, while the Aegean Islands notched up a 120 per cent increase, thanks to a surge of visitors over the Easter holidays.

Andreas Andreadis, SETE's president, forecasts that Greece will attract more than 19m visitors this year, beating last year's record of 17.9m.

A recovery in traditional markets such as the UK and Germany is expected to offset a sharp fall in arrivals from Russia, Ukraine and the Balkan countries.

Another 2.2m visitors are expected to arrive on cruise ships, which compete in high season for a slot to disembark passengers for a stay of a few hours on the islands of Corfu, Santorini and Mykonos.

"I'm very bullish about the tourism industry, I think it will help lift [GDP] growth this year closer to 1 per cent compared with the official projection of 0.4 per cent," Mr Andreadis says.

Revenues from tourism, Greece's largest foreign exchange earner, are projected to reach €13.5bn this year, up from €12bn in 2013. Mr Andreadis expects spending per head to show a modest increase from €650 to €700.

"Greece is on a par for visitor spending with Italy and Spain, and a bit higher than Turkey," he says.

There is still plenty of room for Greece's tourist industry to expand and move upmarket, however.

A study by McKinsey, the consultancy, suggests that arrivals could reach 21m by 2024 with annual revenue increasing to €18bn (in today's money), provided Greece maintains political stability and manages to attract substantial private investment in the tourism sector.

The "shoulder" season in spring and autumn is still under-developed. Greece lacks high-end integrated resorts, while few luxury hotel brands are present. Golf courses, which attract high-spending tourists, are in short supply.

In spite of having the EU's longest coastline and almost 200 inhabited islands, only a handful of Greek marinas offer the same standards of service as found in Croatia and Turkey, the country's main rivals for yachting tourism.

So far, only a few international funds and tourism operators have acquired hotels in Greece or have teamed up with local partners with expertise in hotel management.

One prime Athens property, the Astir hotel at Vouliagmeni south of the capital, was sold last year to Jermyn Real Estate, a fund backed by investors from Abu Dhabi, Kuwait and Turkey in a deal managed by the Hellenic Republic Asset Development Fund (Taiped), the country's privatisation agency. The transaction valued the Astir property, consisting of three hotels and a marina on a secluded peninsula overlooking the Saronic Gulf, at €440m, the highest price paid to date for a Greek hotel.

Oaktree Capital Management, a US investment fund, has teamed up with Sani, Mr Andreadis's family-owned hotel company, to create a luxury resort group that plans to invest more than €100m in acquiring and upgrading existing hotels around Greece.

The partnership has already acquired two properties in Halkidiki, a northern Greek resort area popular with Russian visitors. It is considering another purchase in Messenia, where the Greek-owned luxury resort Costa Navarino is setting the pace for high-end tourist development.

Greece's biggest privatisation project, the €6bn development of the former Athens International Airport site at Hellenikon into a tourism and leisure hub for the east Mediterranean, is finally taking off. Developers warn that it may take 25 years to complete the project: the 640-hectare coastal site is bigger than the principality of Monaco.

An investor group led by Latsis, a Greek family group, in partnership with the Chinese conglomerate Fosun and Al Maabar, a property company linked to Abu Dhabi's sovereign wealth fund, agreed to pay €915m for a 99-year-lease on Hellenikon.

Hellenikon has an acclaimed airport terminal designed by Eero Saarinen, the Finnish-American architect, but has lain abandoned since hosting a handful of events at the 2004 summer Olympics. A plan being prepared by Foster & Partners, the UK-based architectural company, provides for a 200-hectare metropolitan park, more than doubling green space in the greater Athens area.

Meanwhile, Taiped is working to boost the quality of tourism infrastructure through the privatisation of 14 regional airports that handle the bulk of traffic to the islands. Binding offers are due this month for two separate clusters of airports.

A further project, to be awarded by the transport ministry at the end of this year, covers a concession to build and operate a new international airport on a greenfield site in central Crete to replace an outdated facility at Heraklion, the island's capital.

Ioannis Emiris, Taiped's chief executive, says the new regional airport operators will be expected to invest €300m over the next four years. "We want to upgrade facilities, security and operations to the high standards of Athens international airport."

Profile Expansion back on flight plan at Aegean Air

The Greek crisis put paid to Aegean Airlines' bold ambitions, pushing the Athens-based regional carrier into the red for three successive years, **writes Kerin Hope.**

Yet the crisis also allowed Aegean to acquire its ailing rival Olympic Air at a knockdown price.

Aegean, which is controlled by the Vassilakis family, the airline's founder, and several senior Greek shipowners, agreed last year to pay €72m for Olympic after the European Commission withdrew earlier concerns that a takeover would result in a quasi-monopoly on many Greek domestic routes.

Eftichios Vassilakis, Aegean's executive vice-chairman, believes the airline will see the benefits of consolidation this year, with domestic traffic reviving and international tourist arrivals poised to hit a new record.

"Greece started to recover as a tourist destination in late 2012 and things have been improving ever since," he says. "We expect the recovery to continue over the coming years, provided small but important improvements take place."

Aegean turned profitable again in 2013, with net earnings of €56.3m on revenues of €683m. This excludes Olympic's losses, which were €13.9m last year on revenues of €168m.

Aegean is operating from eight bases around Greece this summer, offering 14 new routes, among them three regional cities in Germany and three Middle East destinations, in addition to seasonal flights to Manchester and the south of France.

With a market share of less than 20 per cent of international traffic to Greece, the consolidated airline has plenty of room to grow.

"Our plan is to double our routes out of Athens by 2017, expanding our reach and supporting Greek tourism," says Mr Vassilakis.

An expanded version of this article is available at www.ft.com/greece-2014

Donors step in to assist the victims of austerity

Philanthropy

In spite of some help, NGOs are reporting worsening poverty and a funds drought, writes *Kerin Hope*

Hard times: protesters demand help for the homeless Getty

Christina, an Athenian in her mid-40s, has been living on the streets of the Greek capital since losing her job and her home more than two years ago.

"I feel my situation gets more desperate every week," says the former supermarket employee, interviewed at a day-care centre in Metaxourgeion, a gritty central neighbourhood. The centre is run by Praksis, a Greek non-governmental organisation working with the country's "new poor".

Christina spends two or three days a week job-hunting all over the city. Like other Greeks left destitute during the country's deepest recession on record, she eats a daily meal at a soup kitchen run by the Athens municipality, and uses the day-care centre to take a shower and wash clothes.

The Praksis centre is backed by the Stavros Niarchos foundation (named after the late Greek shipping tycoon) as part of a three-year, €100m programme that funds Greek NGOs attempting to alleviate high levels of poverty and social exclusion – now believed to affect about one-third of the population.

Private donors have helped plug a yawning welfare gap caused by a 40 per cent cut in social spending as Greece implemented an austerity programme agreed with international lenders. The Niarchos foundation came up with the largest single donation, followed by a €25m grant from the international financier George Soros's own foundation.

Greek companies have made smaller cash donations and contributed in kind, supporting social groceries and providing computers and other equipment to NGOs. The Greek shipowners' union, representing hundreds of Athens-based owners, has faced criticism for delaying a planned €25m donation because of a tax dispute with the government.

Epaminondas Farmakis, founder of Elpis, an Athens-based consultancy for philanthropists and donors, says: "It's unfortunate that wealthy groups such as shipowners and industrialists don't seem interested enough in alleviating social pain through collective action. These very high poverty rates will have an impact on the environment and on society, eventually affecting everyone's quality of life."

Some hope that as Greece's economy recovers, the government will be able to claw back more funds for welfare spending. A €230m income-support package is being prepared for Greeks with monthly incomes of €400 or less who live in rented accommodation.

A new round of EU structural funding is expected to provide €1.3bn of funding for social programmes including retraining for the long-term unemployed and cash for poverty alleviation projects that would be managed by NGOs.

> 'Even in the provinces, families' resources are close to being exhausted'

Yet private donors will still be vital to protecting vulnerable groups, Mr Farmakis says. "Past experience shows that disbursement of funds from EU programmes can be delayed for three to five years after they're approved."

Niarchos, a global donor which also supports the arts, has set new benchmarks for NGO operations in Greece, carrying out rigorous due diligence before awarding grants and requiring strict accounting practices.

John Zervakis, the foundation's chief operating officer in Athens, says: "With a few exceptions, Greek NGOs are not in a position to absorb large amounts of funding. There's a need for capacity building and for education in philanthropy."

Praksis, one of Greece's largest NGOs with 150 paid staff, including a full-time fundraiser, and an annual budget of more than €10m, has been a big beneficiary of the Niarchos programme.

In addition to the Athens day-care centre, Praksis operates a mobile medical clinic in the capital, runs a programme to enable impoverished families to stay in their homes, and has opened a shelter in the port of Patras for young irregular migrants who arrive in Greece without adult relatives.

"The needs are large and varied, because so much of Greece's middle class has been wiped out by the crisis," says Tzannetos Antypas, chairman of Praksis.

Lazaros Papageorgiou, founder and director of Artos-Drassi (Bread-Action), which supplies staple foods and serves meals to impoverished families in the decaying industrial suburbs of western Athens, says donations in cash and kind have fallen by 50 per cent over the past year even as more people seek help.

"In spite of better economic figures, we see increasing demand both for basic foodstuffs and for meals," he says.

Last year, Artos-Drassi extended its activities to two northern regions of Greece, where strong family support networks and widespread ownership of smallholdings to grow food until now eased problems caused by a jobless rate of more than 45 per cent.

"Severe poverty is no longer confined to Athens and other big cities," Mr Papageorgiou says. "It's happened slowly, but even in the provinces, families' resources are close to being exhausted."