4 August 2023

Sovereign and Public Sector

Hellenic Republic
Rating Report

SCOPE BBB- STABLE OUTLOOK

Credit strengths

- Strengthened European institutional support, via the EU and Eurosystem
- Strong profile of public debt
- Fiscal outperformance
- Structural reforms; NPL reduction

Credit challenges

- Very high government debt stock
- Banking-sector fragilities
- Inadequate growth potential, high unemployment, rigid labour market
- Weak external sector

Rating rationale:

Strengthened European Institutional support: Supportive monetary and fiscal policy measures have been enhanced for Greece since the Covid-19 crisis. Despite current ECB monetary-policy tightening, the central bank has stayed committed to maintaining flexibility of its reinvestments under the Pandemic Emergency Purchase Programme (PEPP) and has designed an 'anti-fragmentation' instrument. Such programmes, alongside EU fiscal support via the Next Generation EU fund, are fundamental to anchoring Greece's market access – and represent a sea change from Greece's exclusion from ECB monetary operations pre-Covid crisis. This supports debt sustainability and creates fiscal space.

Enhanced fiscal dynamics: Strong reduction underway in the public debt ratio and general government deficit since 2020, supported by the robust economic recovery, elevated inflation, alongside prudent fiscal policy driving reductions in the primary budget deficit. Fiscal dynamics are furthermore supported by past significant improvements in the public debt structure – such as low average interest costs of outstanding debt entering this cost-of-living crisis.

Structural reforms: Banks have continued to substantively curtail elevated non-performing loans (NPLs) – which reached an 8.2% system-wide average by Q1 2023. However, banking-system stability remains challenged by moderate capital adequacy and strengthened sovereign-bank links.

Rating challenges include: i) very high government debt outstanding, representing a continued contingent vulnerability during reappraisals of risk in financial markets on sustainability of debt of euro-area sovereigns; ii) banking-sector fragilities; and iii) structural economic vulnerabilities.

Greece's sovereign rating drivers

Risk pillars		Quantitative		Reserve currency	Qualitative*	Final rating
		Weight	Indicative rating	Notches	Notches	
Domestic Economic Risk		35%	bbb+		-2/3	
Public Finance Risk		20%	bb+		+2/3	
External Economic Risk		10%	c		+1/3	
Financial Stability Risk		10%	a+	EUR [+1]	0	
ESG Risk	Environmental Factors	5%	bb		-1/3	BBB-
	Social Factors	7.5%	ccc		-1/3	
	Governance Factors	12.5%	bb-		+1/3	
Indicative outcome			**bbb-**		**0**	
Additional considerations					**0**	

Note: *The qualitative scorecard adjustments, capped at one notch per rating pillar, are weighted equally with an aggregate adjustment rounded to the nearest integer. The reserve-currency adjustment applies to currencies in the IMF's SDR basket. For details, please see Scope's 'Sovereign Ratings' methodology. Source: Scope Ratings.

Outlook and rating triggers

The Stable Outlook reflects the risk to ratings being balanced over the next 12 to 18 months.

Positive rating-change drivers

- Sustained decline in the public debt ratio
- Banking-sector risks are furthered curtailed
- Strengthened economic sustainability

Negative rating-change drivers

- Eurosystem support for Greece weakens
- Impediments to declines in public debt
- Banking-sector risks re-intensify
- Macroeconomic sustainability weakens

Ratings and Outlook

Foreign currency

Long-term issuer rating	BBB-/Stable
Senior unsecured debt	BBB-/Stable
Short-term issuer rating	S-2/Stable

Local currency

Long-term issuer rating	BBB-/Stable
Senior unsecured debt	BBB-/Stable
Short-term issuer rating	S-2/Stable

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Bloomberg: RESP SCOP

Domestic Economic Risks

- **Growth outlook:** Greece grew a robust 5.9% last year, driven by strong private consumption and recovery in private investment, and further anchored by government measures for businesses and households, as well as the implementation of the National Recovery and Resilience Plan. In view of negative economic effects brought on by the Russia-Ukraine war, which resulted in strong inflationary dynamics – originally from higher energy prices – eroding household real disposable income and slowing private consumption, the Greek economy slowed in Q1 2023 (to -0.1% QoQ). Nevertheless, we expect the economy to stay resilient this year, growing 2.4%, anchored by: i) private and public consumption; ii) investment surrounding the execution of Recovery Plan assignments; and iii) easing of supply-side bottlenecks. Going forward, we see the Greek economy growing 1.6% next year, remaining above its medium-run rate of growth potential estimated around 1%. Growth is buoyed by prudent fiscal policy, adoption of structural reform, as well as a continued shift towards more investment- and export-oriented growth.

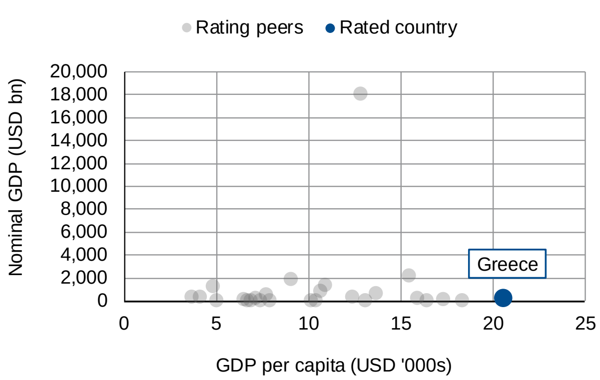
- **Inflation and monetary policy:** Headline Harmonised Index of Consumer Prices (HICP) inflation averaged 9.3% in 2022, although it began to ease late last year, standing at 3.4% in July 2023. We expect HICP inflation to average 4.2% for this year, before averaging 3.4% in 2024. Inflationary pressures have been firstly driven by earlier rises in energy and food prices but thereafter broadened to other services-sector and non-energy industrial goods prices, resulting in core inflation peaking at 7.3% YoY by May 2023, before easing to 5.4% as of July. The ECB is tightening its monetary policy, raising its three key policy rates by 425bps each since July 2022, accompanied by reductions in balance-sheet securities holdings. Still, flexibility applied during the reinvestment phase of the Eurosystem's PEPP – including the capacity to purchase Greek debt above and beyond redemptions during this phase – alongside announcement of a 'Transmission Protection Instrument' – anchor Greek debt markets and reinforce our assumption of Eurosystem support for Greece being more endurant, rather than specific to only the Covid-19 crisis phase.

- **Labour markets:** Employment expanded on average by 5.4% last year amid recovery in the economy, before slowing down to 0.6% YoY by June 2023. The unemployment rate has steadily declined, reaching 11.1% by June 2023, the lowest since the start of the Greek crisis in 2009 although still (structurally) above an EU average (5.9%). Limited economic diversification, rigidities in the labour market and high structural unemployment are credit-rating constraints, although we expect the unemployment rate to continue easing – averaging 11.1% this year, before 10.6% in 2024, supported by the adoption of labour-market reforms.

Overview of Scope's qualitative assessments for Greece's *Domestic Economic Risks*

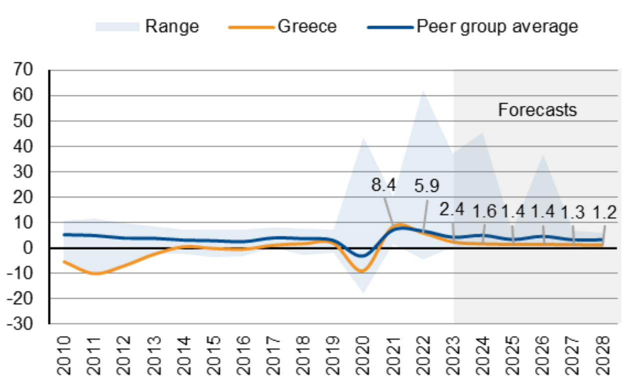
CVS indicative rating	Analytical component	Assessment	Notch adjustment	Rationale
bbb+	Growth potential of the economy	Weak	-1/3	Substantial investment gaps in several sectors; low innovation, although gradual shift towards more competitive export-oriented sectors; economic growth potential remains comparatively weak
	Monetary policy framework	Neutral	0	ECB is a highly credible and effective central bank; ECB policy innovations and Greece's enhanced access anchor Greek markets
	Macro-economic stability and sustainability	Weak	-1/3	Elevated structural unemployment; limited economic diversification; rigidities in the labour market

Nominal GDP and GDP per capita, USD



Source: IMF World Economic Outlook (WEO), Scope Ratings

Real GDP growth, %



Source: IMF WEO, Scope Ratings forecasts

Public Finance Risks

- **Fiscal outlook:** Fiscal metrics outperformed last year on the back of robust economic growth and high inflation, resulting in higher-than-budgeted revenue, particularly from tax and social security contributions, as well as lower-than-anticipated spending. The government adopted several measures to cushion the effects of high inflation, amounting to a cost of 4.8% of GDP, mainly covered by the resources from the Green Transition Fund. Some of these measures have been extended into 2023, although their cost ought to attenuate to around 0.8% of GDP. Additionally, authorities intend to make permanent earlier reductions in the solidarity tax, social security contributions and reduced value-added tax on several goods and services introduced during the pandemic crisis. Since the elections, the Kyriakos Mitsotakis government pledged a EUR 9bn programme – including one-off hand-outs to pensioners, pay rises to the public sector, and a rise in the tax-exemption threshold by EUR 1,000 for households with children. After having returned to a balanced primary account (0.1% of GDP) last year ahead of schedule, we see the primary balance further bettering this year to 0.5% of GDP, followed by 1% of GDP a year during 2024-28 (more conservative than the government objective of 2%). Likewise, we assume the headline deficit shrinking to 2% of GDP this year, from 2.3% last year, before averaging 1.7% during 2024-28.

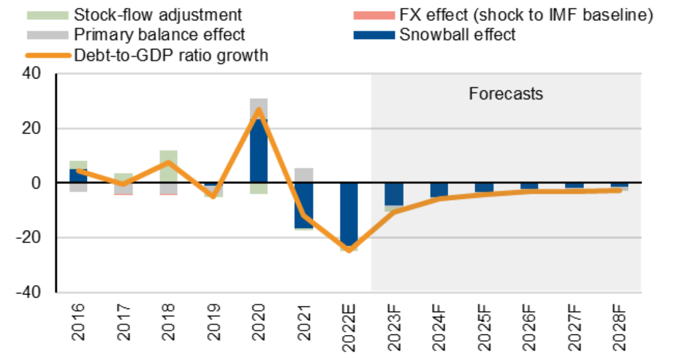
- **Debt trajectory:** The aggregate debt stock has declined surprisingly rapidly from 206.3% of GDP record peaks of 2020, reaching about 171.3% by 2022 (falling last year under pre-Covid crisis levels of 180.6% from end-2019) and we expect this ratio, under a scenario of no renewed recession, to reach 160.7% by end-2023, before 141.6% by 2028 (which, if so, would reflect the lowest public-debt ratio for Greece since the Private Sector Involvement of Q1-2012). This assumes near-term economic slowdown but nevertheless above-potential growth over the forecast horizon, and GDP deflator inflation averaging 2.3% from 2024-28 after the 8.1% in 2022 and 4.2% in 2023. However, dependence on higher-rate market financing will bring a parallel rise in net interest payments, projected to pick up to around 6.6% of revenue by 2028, from 4.9% at 2021 lows.

- **Debt profile and market access:** Greece benefits from a strong structure of its public debt: above 80% of the debt is held on the official-sector balance sheet, when one includes Greek securities temporarily held by the Eurosystem in said figure. But the share of debt held by the private sector is rising as Greece relies on market issuance, repays EUR 5.3bn of Greek Loan Facility loans early and the ECB starts reducing the size of PEPP holdings. The debt profile is furthermore anchored by a long weighted-average maturity of central-government debt (19.6 years as of March 2023) and modest weighted-average net interest rate of outstanding debt (1.5% in 2023). 100% of debt is denominated in euro and is on fixed rate (after hedging), curtailing risk from rate rises, and debt amortisations are evenly distributed medium run, anchoring moderate average gross government financing requirements of around 9% of GDP annually during 2023-28. A cash cushion of EUR 30.6bn at end-2022 (14.7% of GDP) anchors resilience.

Overview of Scope's qualitative assessments for Greece's *Public Finance Risks*

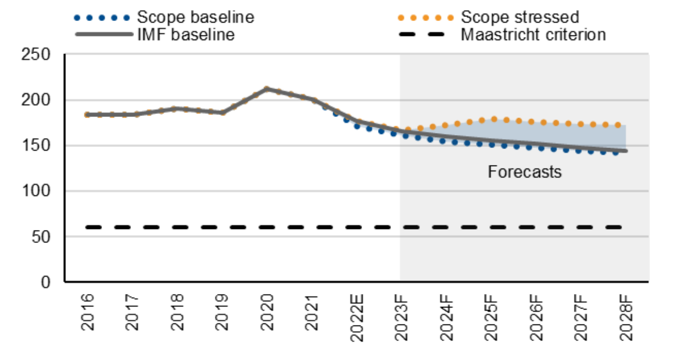
CVS indicative rating	Analytical component	Assessment	Notch adjustment	Rationale
bb+	Fiscal policy framework	Strong	+1/3	Benefits from EU/euro-area fiscal governance institutions; reduced EU fiscal oversight; target of primary surpluses; some policy slippage
	Debt sustainability	Neutral	0	Very high public-sector debt but strong decline expected; comparatively low risk from rate rises or forex volatility
	Debt profile and market access	Strong	+1/3	Strong debt structure and cash cushion, but debt structure is weakening; strengthened access to regional lenders of last resort

Contributions to changes in debt levels, pps of GDP



Source: IMF WEO, Scope Ratings forecasts

Debt-to-GDP forecasts, % of GDP



Source: IMF WEO, Scope Ratings forecasts

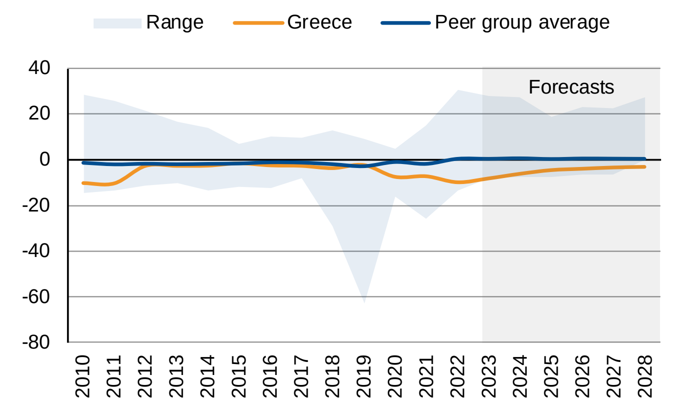
External Economic Risks

- **Current account:** Goods and services exports growth was strong last year (+36.9% YoY), fostered by the recovery in tourism export services and resilience of goods exports under conditions of slowdown in external demand. Imports, however, rose (+42.3% YoY) more than exports did, due to strong domestic-demand growth. Furthermore, the surge in import prices for fuels, food, raw materials and transportation had an adverse effect on the current-account balance. The current-account deficit widened as such to 9.7% of GDP last year, from 6.8% in 2021 and the between 0.7% and 2.9% of GDP yearly of 2013 to 2019. This deterioration last year mainly reflected weakening in the balance of goods trade only partially compensated for by higher services trade surpluses. The current-account deficit has gradually started to shrink since the start of 2023, reaching around 7.9% by the twelve months to May 2023, as the enlarged goods deficit receded. The current account is expected to continue improvement medium run, with exports rising as a response to recovering foreign-sector demand, easing supply-chain bottlenecks and the return of foreign-tourism inflows towards pre-pandemic levels. Past competitiveness gains ought to also help. Nevertheless, much warmer weather and wildfires are presenting indirect consequences for the Greek tourism industry, which, prior to the Covid-19 crisis, amounted to 27% of GDP. Net foreign direct investment picked up to 3.5% of GDP in the year to April 2022, but has moderated more recently to 0.9% in the year to May 2023.
- **External position:** Greece has a sizeable net international investment liability position of 141.4% of GDP as of Q1 2023, although nevertheless bettered compared against peaks of 181.6% reached in Q2 2021 and anticipated to further shrink long run – as concessional economic assistance loans are gradually redeemed. In Q1 2023, gross external debt stood at an elevated 261.3% of GDP, nevertheless 48pps beneath its peaks from Q2 2021. Furthermore, 67.5% of external debt holds a long-term maturity. External debt is mostly owed by the government (50.1% of aggregate gross external debt) and the central bank (24.5%). Still, the Greek Target-II balance stood at EUR -114.9bn as of May 2023, significantly weaker than pre-crisis levels of EUR -25.7bn (from December 2019).
- **Resilience to short-term external shocks:** Greece benefits from issuance in euro, given the currency's status as an international reserve currency, supporting the economy's resilience against external crises.

Overview of Scope's qualitative assessments for Greece's *External Economic Risks*

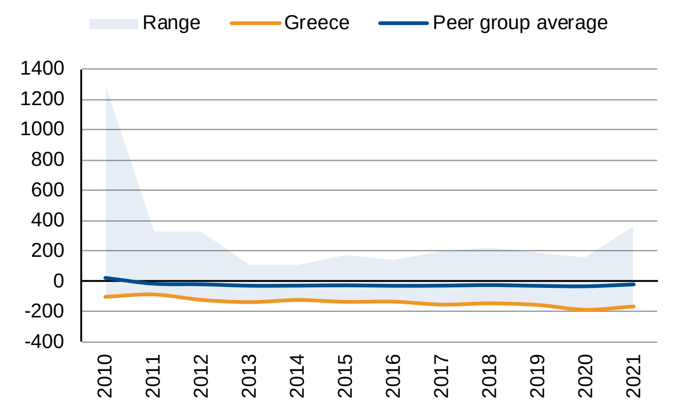
CVS indicative rating	Analytical component	Assessment	Notch adjustment	Rationale
c	Current account resilience	Neutral	0	Current account sensitive to changes in tourism behaviour; currently significant current-account deficit
	External debt structure	Strong	+1/3	Elevated external debt, but very long maturity and in the form of euro-denominated sovereign debt owed to the official sector
	Resilience to short-term external shocks	Neutral	0	Benefits from euro-area membership

Current-account balance, % of GDP



Source: IMF WEO, Scope Ratings

Net international investment position (NIIP), % of GDP



Source: IMF, Scope Ratings

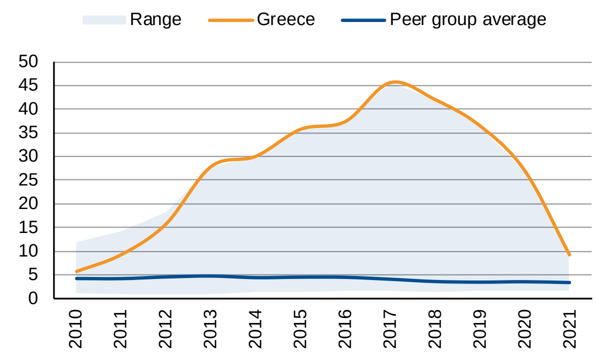
Financial Stability Risks

- **Banking sector:** System-wide tier 1 ratio remains at moderate levels, declining slightly to 14.5% in Q1 2023, from 15.2% the previous quarter, but strengthened compared with the 13% at Q3-2021 lows. Capital adequacy remains under Q4-2019 heights of 16.4% as risk-weighted assets rose, banks continue to clean up balance sheets via NPL securitisations and the effects of IFRS 9 were fully phased in. Bank liquidity positions have been enhanced, with liquidity coverage ratios of 205.1% as of Q1 2023, above a pre-Covid ratio of 130.8%. Banks returned to record profits last year, due to declining loan loss provisioning, increased non-recurrent income from financial operations and hedging instruments, as well as a rise in interest income benefitting from currently higher rates. System-wide NPLs have continued to decline meaningfully and reached 8.2% of gross loans by March 2023 on a consolidated basis, with all four systemic Greek banks having achieved objectives of a single-digit NPL ratio by the end of 2022. Nevertheless, the NPL ratio remains well above EU averages (of 1.8% as of March), and the transfer of NPLs out of the banking system does not mean they are permanently removed. Pressures on banking-system asset quality remain from high shares of deferred tax credits in bank capital (which accounted for 56% of total prudential own funds as of December 2022, accounting for the fully phased-in effects of IFRS 9) and still elevated NPL ratios (44.8%) of the non-significant banks, which did not benefit from government guarantee schemes. Two of four systemic banks demonstrated fully-loaded common equity tier 1 ratios falling near or beneath 8% in the adverse scenario of the European Banking Authority 2023 stress test.
- **Private debt:** Non-financial private-sector debt totalled 99.4% of GDP in Q4 2022, well under a euro-area average of 162.2% of GDP the same quarter, and below a pre-crisis level of 110.7% as of end-2019 – according to Bank for International Settlements data. Resident deposits stood at a ten-year high of EUR 198.1bn as of June 2023, anchored by the higher savings of households and non-financial corporates.
- **Financial imbalances:** Provision of credit by the banks to the private sector improved over 2022, but recently slowed again to 0.9% YoY by June 2023. Annual growth of net credit to non-financial corporates rose last year, before slowing this year due to higher funding rates. Annual net credit growth to households has improved although it remains negative. The latter is restrained by existing private-sector cash cushions accrued during the pandemic crisis. In addition, bank domestic government bond holdings, equity stakes held by the State in the banks and State guarantees under the Hercules Asset Protection Scheme suggest a strengthened sovereign-bank nexus – raising contingent risks for the sovereign under stressed banking-system scenarios. The government plans to divest its holdings in the banks.

Overview of Scope's qualitative assessments for Greece's *Financial Stability Risks*

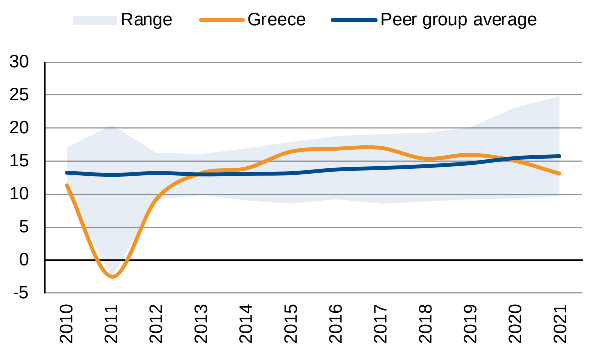
CVS indicative rating	Analytical component	Assessment	Notch adjustment	Rationale
a+	Banking sector performance	Weak	-1/3	Improved profitability, poor asset quality and moderate capitalisation; sharp reductions in NPLs and strengthened liquidity; inadequate credit growth
	Banking sector oversight	Strong	+1/3	Effective oversight by the Bank of Greece and the ECB as part of Banking Union
	Financial imbalances	Neutral	0	Moderate private debt; no credit growth imbalances such as those of sovereign peers; banks' interconnectedness with the sovereign

Non-performing loans, % of total loans



Source: IMF, Scope Ratings

Tier 1 ratio, % of risk-weighted assets



Source: IMF, Scope Ratings

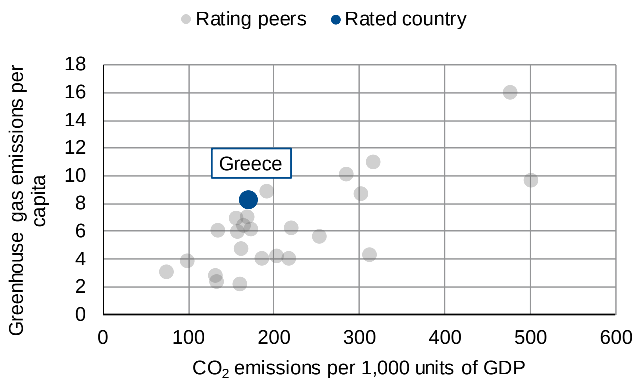
ESG Risks

- **Environment:** Greece is exposed to natural-disaster risk such as droughts and wildfires, such as the intense fires experienced this summer due to record temperatures. Such risks stress existing challenges surrounding water management, air pollution and the shifting of the energy mix to cleaner sources. A 2011 study commissioned by the Bank of Greece estimated climate change could cost EUR 577-701bn to the Greek economy by year 2100. In 2021, Greece's climate footprint was below the EU average (per capita emissions of 4.8 tonnes of CO_2/year against an EU average of 6.7), while 43% of electricity was derived from renewables (slightly above an EU average of 37%) as of 2022. The government aims to reduce its greenhouse gas emissions by at least 55% by 2030 as compared with 2005 levels, 80% by 2040 before full carbon neutrality by 2050. Fossil fuels still account for a significant share of Greece's aggregate energy mix with oil and fossil fuels covering 56%, gas 26% and renewables 18% in 2021. Issuance of an inaugural green sovereign bond has been postponed due to prevailing market conditions.
- **Social:** Greece sees net emigration and a declining working-age population, high and rising old-age dependency and structurally elevated unemployment. As of June 2023, seasonally adjusted unemployment was 11.1% against an EU average of 5.9%. Greek unemployment, however, has been on a steadily declining trajectory. Unemployment of those under 25 years of age was an elevated 23.6% as of June 2023, below Spain's 27.4%, but above the 21.3% figure for Italy. Regional inequalities are evident in labour productivity and labour-market conditions, with nearly two third of economic activity concentrated in the regions of Attica and North Macedonia. The share of persons at risk of poverty and social exclusion remains high, at 26.3% in 2022.
- **Governance:** While Greece scores moderately on World Bank Worldwide Governance Indicators, the reform agenda since 2017 has advanced institutional scores and progress on areas such as tax administration and compliance, the judicial system, public administration, and anti-corruption. The economic and institutional reform agenda has been advanced under comparatively stable policy-making conditions with Prime Minister Mitsotakis holding an absolute majority since 2019. His party re-secured an absolute parliamentary majority following the second round of elections in June 2023, gaining 40.6% of votes and 185 seats (of 300) in Parliament. Such prolonged political stability helps strengthen government capacity to pursue its reform priorities such as i) bringing incomes significantly closer to European peers'; ii) tendering 30% of Athens Airport; iii) restructuring national health care; and iv) allowing Greeks abroad to vote in national elections.

Overview of Scope's qualitative assessments for Greece's *ESG Risks*

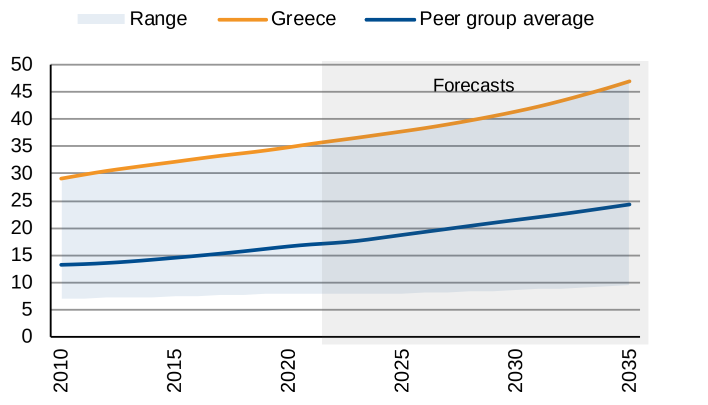
CVS indicative rating	Analytical component	Assessment	Notch adjustment	Rationale
b+	Environmental factors	Weak	-1/3	High exposure to natural-disaster risks; ambitious decarbonisation targets; low share of renewables in the aggregate energy mix
	Social factors	Weak	-1/3	Adverse demographics; moderate educational outcomes but long healthy life expectancy; inequality between the regions and elevated poverty
	Governance factors	Strong	+1/3	Comparatively stable political conditions following elections and institutional reforms; lingering geopolitical tensions

Emissions per GDP and per capita, $mtCO_2e$



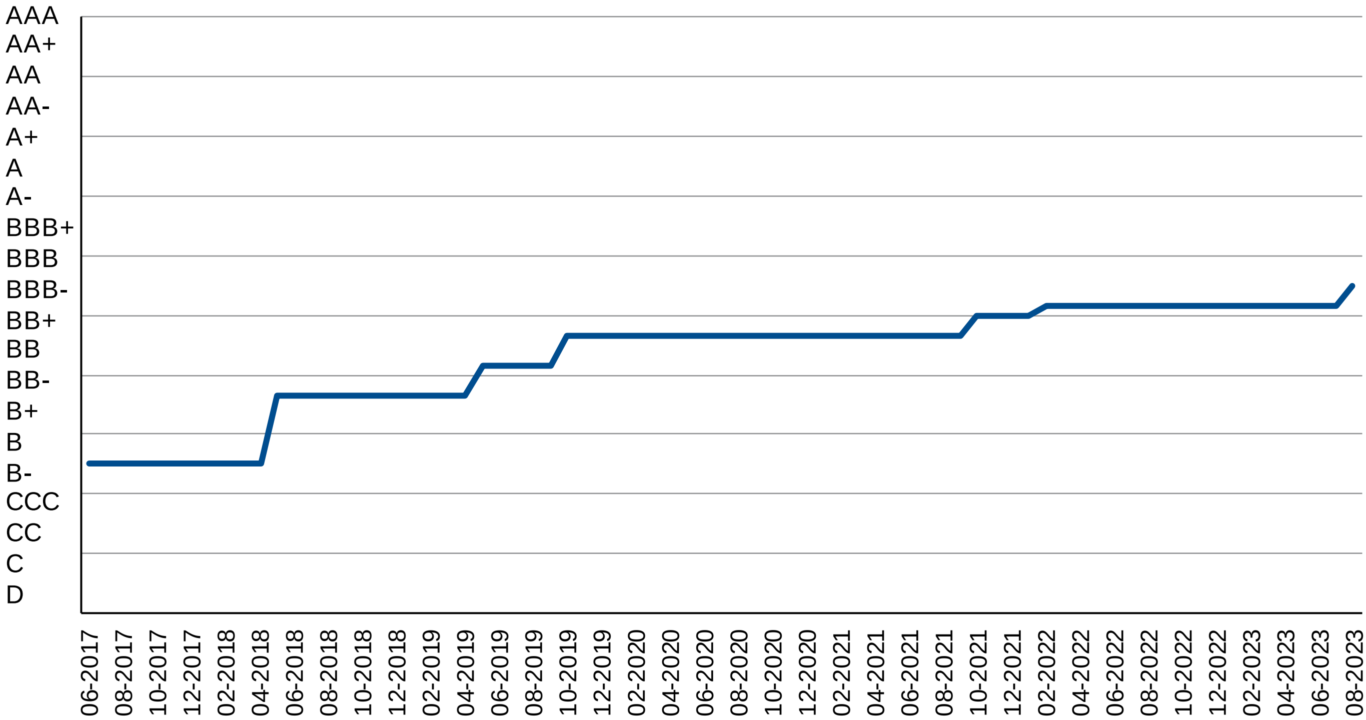
Source: European Commission, Scope Ratings

Old age dependency ratio, %



Source: United Nations, Scope Ratings

Appendix I. Rating history (foreign-currency long-term debt)



NB. Positive/Negative Outlooks are treated with a +/-0.33-notch adjustment. Credit Watch positive/negative with a +/-0.67-notch adjustment.

Appendix II. Rating peers

Rating peers are related to sovereigns with an indicative rating in the same rating category or in adjacent categories per Scope's Core Variable Scorecard, including a methodological reserve-currency adjustment.

Peer group*
China
Georgia
Hungary
Romania
Serbia
Türkiye

*Publicly-rated sovereigns only; the full sample may be larger.

Appendix III. Statistical table for selected CVS indicators

This table presents a selection of the indicators (24 out of 30 – with the governance indicator reflecting a composite of six indicators) used in Scope's quantitative model, the Core Variable Scorecard, in line with Scope's Sovereign Rating Methodology. The metrics and sources for the data presented here ensure comparability across global peers and may therefore differ from national and other selective international statistics.

Pillar	Core variable	Source	2018	2019	2020	2021	2022
Domestic Economic	GDP per capita, USD '000s	IMF	19.8	19.1	17.6	20.1	20.6
	Nominal GDP, USD bn	IMF	212.1	205.3	188.8	215.0	219.2
	Real growth, %	IMF	1.7	1.9	-9.0	8.4	5.9
	CPI inflation, %	IMF	0.8	0.5	-1.3	0.6	9.3
	Unemployment rate, %	WB	19.3	17.3	16.3	14.7	12.2
Public Finance	Public debt, % of GDP	IMF	190.7	185.5	212.4	200.7	177.4
	Net interest payment, % of revenue	IMF	6.9	6.3	6.1	5.0	4.9
	Primary balance, % of GDP	IMF	4.2	3.2	-7.7	-5.5	-1.5
External Economic	Current-account balance, % of GDP	IMF	-3.6	-2.2	-7.3	-7.1	-9.7
	Total reserves, months of imports	WB	1.0	1.1	1.8	1.6	1.1
	NIIP, % of GDP	IMF	-144.1	-154.6	-186.9	-164.5	-143.0
Financial Stability	NPL ratio, % of total loans	IMF	42.0	36.4	27.0	9.2	6.5
	Tier 1 ratio, % of risk-weighted assets	IMF	15.8	14.9	14.6	13.7	12.6
	Credit to the private sector, % of GDP	WB	91.7	81.0	82.3	57.1	-
ESG	CO_2 per EUR 1,000 of GDP, $mtCO_2e$	EC	217.0	197.3	180.3	170.1	-
	Income share of bottom 50%, %	WID	20.9	21.1	21.5	21.5	-
	Labour-force participation rate, %	WB	67.5	67.7	66.6	66.5	-
	Old-age dependency ratio, %	UN	33.8	34.3	34.9	35.5	36.0
	Composite governance indicators*	WB	0.3	0.3	0.4	0.4	-

* Average of the six World Bank Worldwide Governance Indicators.

Appendix IV. Economic development and default indicators

IMF Development Classification	Advanced economy
5y USD CDS spread (bps) as of 2 August 2023	72.4

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