ALPHA BANK

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Greece
Economic & Financial Outlook

Executive Summary

- Greece's remarkable adjustment in the last four and a half years has led to the rebalancing of the economy. This was made possible through fiscal consolidation, mainly by reducing spending and expanding the tax base on a permanent basis. Moreover, substantial productivity-enhancing and employment-increasing structural reforms (especially in the labour and product markets) were implemented successfully, boosting Greece's international competitiveness, as well as net exports, business and consumer sentiment.

- Greece has benefited from the spectacular increase in external tourism in 2013 and in Jan.-April 2014, which, in combination with the continuing healthy increase in exports of goods, have contributed to the substantial deceleration of the falling trend of its GDP to -3.9% in 2013 and, more importantly, to -2.3% in Q4 2013 and to -1.1% in Q1 2014, from -6.0% in Q1 2013. A 1.0% GDP growth is now more likely in 2014.

- In 2013, a significant improvement in the general government (GG) primary balance was recorded, with a surplus of 0.8% of GDP, compared with a planned zero balance, from -1.2% % of GDP primary deficit in 2012. For 2014, the GG primary surplus target has been set at 1.6% of GDP. In fact, the successful implementation of the 2013 budget and of the 2014 budget in Jan.-April 2014, have already set the ground for a better than expected implementation of the 2014 budget as well.

- With internal devaluation since 2009, Greece has recouped in full competitiveness losses during the 2000s, while the restoration of flexibility in the labour market and strong economic performance implies further gains in competitiveness in the following years.

Basic Conjunctural Indicators (average annual % change)

	2010	2011	2012	2013	2014	
					available period	
Retail sales volume (except automotive fuel)	-6.9	-8.7	-11.8	-8.4	-2.9	Jan-Feb
Automobile sales	-37.2	-29.8	-41.7	3.1	22.0	Q1
Tax on mobile telephony	37.1	-16.8	-7.9	-12.8	-13.5	Jan-Mar
VAT revenue	4.8	-2.8	-11.4	-7.4	-1.8	Jan-Apr
Consumption tax on fuels	30.3	-18.3	-4.1	-5.3	-5.3	Jan-Apr
Private Consumption	-6.2	-7.7	-9.3	-6.0	…	…
Government Consumption	-8.7	-5.2	-6.9	-4.1	…	…
Private building activity (volume, according to permits)	-23.3	-37.7	-30.6	-25.6	-41.1	Jan
Concrete production	-14.5	-35.9	-40.6	-7.1	10.3	Jan-Feb
Public investment expenditure	-11.3	-21.8	-6.8	8.8	91.6	Jan-Mar
Fixed investment	-15.0	-19.6	-19.2	-12.8		
Unemployment	12.5	17.7	24.2	27.3	26.5	Feb
Manufacturing production	-5.1	-8.5	-4.2	-2.0	0.9	Jan-Mar
Economic sentiment indicator	82.0	80.6	80.3	90.8	95.4	Apr
-Industry	75.8	76.9	77.2	87.8	91.9	Apr
-Consumer confidence	-63.4	-74.1	-75.0	-69.3	-55.0	Apr
PMI (manufacturing)	43.8	43.6	41.2	46.0	51.1	Apr
Exports of goods - excluding oil (El.Stat.)	9.3	10.4	0.9	-2.1	-4.7	Jan-Mar
Exports of goods (El.Stat.)	11.6	37.0	13.5	-0.2	-3.0	Jan-Mar
Imports of goods - excluding oil (El.Stat.)	-10.7	-12.4	-7.5	-4.8	10.5	Jan-Mar
Imports of goods (El.Stat.)	-1.9	-6.9	1.8	-4.9	-0.3	Jan-Mar
Tourist arrivals (airports)	-0.7	8.7	-5.5	10.8	23.2	Jan-Mar
Tourism receipts (BoP)	-7.6	9.3	-0.6	14.9	21.7	Jan-Mar
Exports goods & services	7.7	7.2	1.4	1.6	5.1	Jan-Mar
Imports goods & services	0.3	1.4	-12.1	-6.1	0.5	Jan-Mar
GDP growth	-4.9	-7.1	7.0	-3.9	-1.1	Q1
Inflation (CPI)	4.7	3.3	1.5	-0.9	-1.3	Apr
Current Account (% of GDP)	-9.2	-8.6	-1.2	1.3	0.2	Jan-Mar

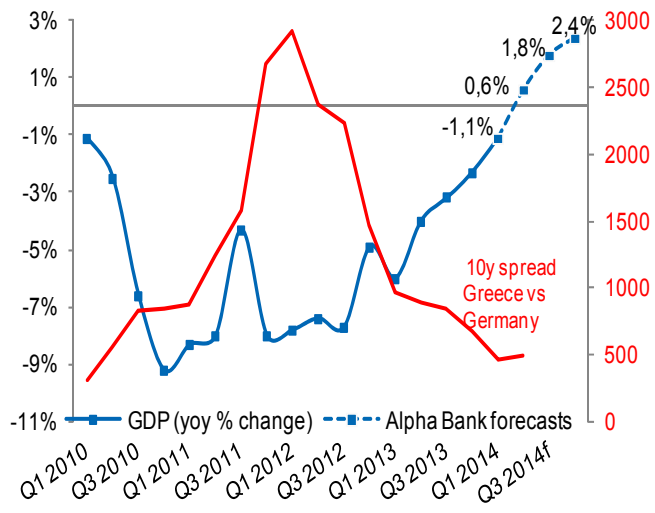
Source: Bank of Greece and Hellenic Statistical Authority (El.Stat.)

- In this context, the net exports of goods and services deficit has shrunk from -14.1% of GDP in 2008, to -3.3% of GDP in 2012 and to -1.4% of GDP in 2013. It is now expected (by the European Commission) to turn into a 0,0% of GDP surplus in 2014, +0.8% of GDP in 2015 and to a surplus of 2.1% of GDP in 2018. Also, Greece's current account (including net capital transfers) reached a surplus of 1.33% of GDP in 2013 and is expected to maintain a positive surplus in 2014, from a deficit of -2.2% of GDP in 2012, and -8.6% in 2011.

- The substantial progress in fiscal consolidation achieved in 2013, and which is expected to be extended in 2014, together with further advances in the field of structural reforms and the fast now implementation of the privatization program in much more favourable markets, set the stage for a sustainable and robust recovery of the economy from 2014 onwards. The economy's takeoff will be also assisted by the restart of works in Greece's major infrastructure projects and by fast improving liquidity conditions.

- The rapid implementation of the bank recapitalization program and additional share capital issues in March – May 2014 have made possible the inflow substantial amounts of much needed foreign capital in the Greek economy, culminated to the re-entry of the Greek sovereign in the bonds market, as well as of many Greek corporates. International investors bank in the much anticipated Greece's recovery, already pushing up prices in the Athens Stock Exchange. These developments have further contributed to improving investor's sentiment on Greece.

Growth and Confidence

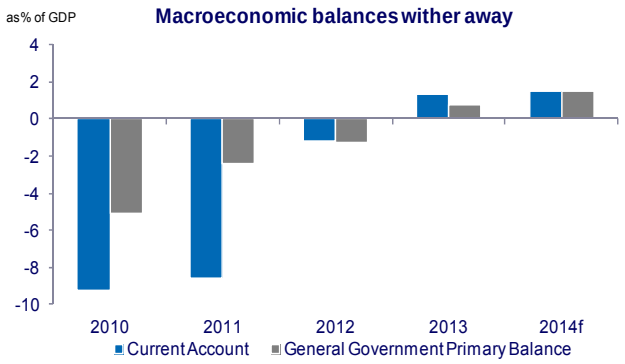


Source: Hellenic Statistical Authority, Alpha Bank Forecast

Twin Surpluses: A regime switch in economic policy making

Greece's remarkable adjustment in the last 4 years and especially in 2013 is considered as a milestone in the economic history of the country. The substantial progress in fiscal consolidation achieved in 2013 together with further advances in the field of structural reforms led to a regime switch in economic policy making. The new era of economic policy in Greece can well be characterized by the two great achievements: a) the operation of the Greek economy already from 2013 with **twin surpluses both in its general government primary budget and in its current account of the balance of payments and b) the timely recovery of the economy from 2014 onwards based on its drastically improved international competitiveness.**

Firstly, the unsustainable macroeconomic imbalances of the last three decades until 2009, the twin deficits (namely the fiscal primary deficit and the current account deficit) have been eradicated. This is evident by the significant improvement in the general government (GG) primary balance, which recorded a surplus of 0.8% of GDP in 2013, compared with a targeted zero balance, from a deficit of -1.3% in 2012. Also, Greece's current account balance (including net capital transfers) recorded a surplus of 1.33% of GDP in 2013 for the first time since 1948. In fact a current account surplus of € 413 million has been recorded even in Q1 2014, compared to a deficit of € 1.15 billion in Q1 2013. This was made possible through the implementation of the adjustment program which also led to a spectacular improvement in the international competitiveness of the country. Internal devaluation since 2009 has now recouped in full the competitiveness losses in the period 2000-2009, while the restoration of flexibility in the labour market and the expected strong economic performance in terms of GDP and productivity growth may imply further gains in competitiveness in the following years.



Secondly, the above significant developments set the ground for the improvement of macroeconomic stability, as the implementation of structural reforms have contributed to the economic recovery. In particular, after six years of deep recession (with a 23% cumulative decline in economic activity since the onset of the crisis) Greece is clearly on the road to recovery. The recession was milder than was first anticipated during 2013, supported by tourism activity and relatively resilient consumption, mainly in Q4 2013. Real GDP beat the consensus expectations (and Troika's forecasts) and showed a marked slowdown in the rate of output decline, falling by -3.9% in 2013, from -7.0% in 2012. From Q2 2013 the recession started to soften, as real GDP contracted at a decelerated pace: from -6.0% yoy in Q1 2013, to -2.3% yoy in Q4 2013 and then to -1.1% in Q1 2014 (See Diagram). Positive 2014 GDP growth prospects have already been confirmed by European Commission and the IMF, as well as by the substantial deceleration of the falling trend of GDP in Q1 2014. According to the European Commission, GDP is expected to increase by 0.6% in 2014 and further by 2.9% in 2015 and by 3.7% in 2016. Growth is expected to be supported by strong investment and exports on the back of the drastically improved competitiveness, as well as by further deceleration in the falling trend of private consumption, which is expected to turn to positive growth from 2015 onwards. Investment is projected to strengthen from 2014, led by the restart of the motorway projects in H1 2014 and faster absorption of EU structural funds (€4.2 bn in 2013 and €4.5 bn estimated in 2014).

Recent economic developments point to an even bigger increase of GDP by 1.0% in 2014. In fact, real GDP growth is expected to turn positive as early as Q2 2014. The positive prospects of the Greek economy are evident through the substantial improvement of the labour market and the resurgence of the tourism sector and manufacturing production from Q1 2014. It is also supported by the return of investors' confidence, the rapid deceleration of the 10year government spread, the increase of equity prices in the Athens Stock Exchange, the recapitalization and additional capital increases of Greek banks and more recently, the successful return to the bond market not only of the banks and the Greek state (Greece has raised €3bn in a five-year bond deal after attracting more than €20 bn in orders), but also of many big Greek businesses.

Growth dynamics point to a bottoming out of recession and to a healthy recovery from 2014 onwards

Key drivers on the resurgence of the Greek economy are expected to be the following: a) Greece's valuable comparative advantages in important sectors of the economy, which are already contributing to the recovery of the economy from its 5-years of deep recession. b) The drastic improvement of the country's international competitiveness and of its institutional and organizational structure, which, in combination with the projected fast implementation of Greece's far reaching privatization program, are expected to contribute to the attraction of the much needed business investments and in particular of Foreign Direct Investment (FDI). c) The implementation of the new EU co-financed development program of Greece, which has been branded as Partnership Agreement for the Development Framework (ESPA) 2014-2020 and provides for EU structural funds financing amounting to more than € 20 billion for the following 7-year period. d) The expected recovery of private consumption and of investment in housing from 2015 onwards, following their stabilization in during 2014. This is based on the already observed substantial

improvement of economic sentiment and of business – investment and consumer confidence on the prospects of the Greek economy, as well as the first signs for a fast increase in employment registered in 2013 and in Jan.–April 2014. More specifically:

Greece possesses valuable comparative advantages: a) in tourism, including medical tourism and its position as a place of permanent retirement residence for old people, b) in agriculture and in agriculture related manufacturing sectors, with high quality products favouring substantial increase in domestic value added, c) in industry, including energy and construction, d) in its geographical location which makes Greece an ideal logistics hub, in particular between Asia and Central-Eastern Europe, e) in other important services sectors, including shipping, and also health and education. These sectors are already registering positive growth contributing to the recovery of the economy from 2014:

Tourism: ***Despite the lingering economic challenges, tourism sector has shown a remarkable strength in 2013, which is expected to be widely surpassed in 2014.*** Greece's unique geographical characteristics, in combination with its highly developed and still fast developing transportation infrastructure and also the development and modernization of more specific tourist facilities, are expected to contribute to its development as a major tourist destination in Europe and also as an international transportation hub of European proportions.

In fact, tourism arrivals (including cruises) exceed expectations in 2013 and grew by 18.7%, reaching a record 20.1 mln arrivals, compared to a moderate increase by 3.2% in 2012. As a result, tourism receipts were also increased remarkably by 16.4% in 2013 to é 12.15 billion, compared to a fall by 0.6% to € 10.44 billion) in 2012.

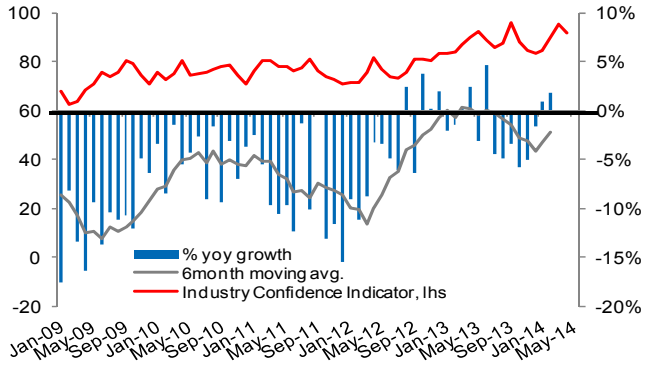
External Tourism

The positive results for 2013 and the expected economic improvement have set the scene for another positive year in tourism in 2014, fuelling growth and job creation. This is already on display, as tourism arrivals through air travel in the main Greek airports have recorded another significant increase by 30.1% yoy in January-April 2014, against a fall by -7.6% in January-April 2013. Also, external tourist revenues registered a 21.7% increase in Q1 2014, setting the stage for a substantial increase of these revenues in 2014 as a whole.

Except of tourism, some other leading indicators in January – April 2014 suggest that economic recovery has already gathered momentum. Such indicators are: a) the substantial increase also of the revenues from international shipping by +8.4% in Q1 2014, compared with their fall by -14.4% in Q1 2013, b) the already fast increasing employment in the private sector in Jan.-April 2014, c) the PMI in manufacturing forming above 50 and the consequent increase of manufacturing production, d) increasing retail sales - including car sales, e) the substantial improvement of the economic sentiment index (ESI) – including consumer confidence and even f) the stabilization (or small increase) of imports of goods and services in Q1 2014. These developments support the widely held prospects for the realization of the expected recovery of the economy from Q2 2014 onwards.

Industrial production registered an increase by 0.3% yoy in Q1 2014, versus a fall by -3.5% yoy in Q1 2013. In 2013 the General Index of Industrial Production registered a fall by -3.6% compared to a fall of -3.4% in 2012. Accordingly, production in manufacturing industry increased by 0.9% in Q1 2014, compared to a small fall by -1.0% in Q1 2013.

Manufacturing Production (2005=100)



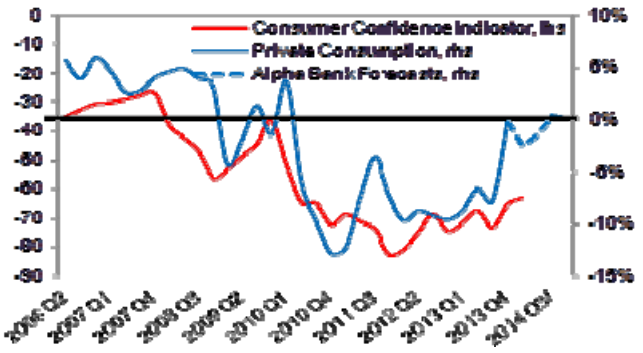
Moreover, the PMI index in manufacturing gained back its strength and climbed to 51.1 in April 2014, from a temporal fall to 49.7 in March 2014. In Jan 2014 the index stood above the 50 level for the first time since Aug 2013. PMI index is poised to reach higher levels, while the level of the index is consistent with a more permanent recovery in the industrial production.

This is also supported by the significant improvement of business expectations in industry (April 2014: 91.9, Jan 2014: 84.7, Dec.2013: 83.4) and therefore, points to positive growth of manufacturing production in 2014 as a whole. These developments in manufacturing production are taking place despite the fact that some sectors are still affected negatively by the continuing fall of activity in the housing market. In fact, it is important to notice, that the first signs of recovery of activity in other construction (excluding housing) have already implied an increase of production of non-metallic minerals by 2.0% in Q1 2014, following their increase by 17.3% yoy in Q1 2013 as well. Moreover, the turnover in the domestic market in this sector has registered an increase by 21.1% in Q1 2014. Also, production and turnover in the domestic market of basic metals have registered an increase in Q1 2014 by 9.5% and by 5.8% respectively. Also, production and domestic turnover of furniture have shown signs of

recovery in Q1 2014, from their very low levels in Q1 2013. This shows that the expected recovery of other construction from 2014 and of investment in housing from 2015 will have substantial positive effects on the manufacturing production as well.

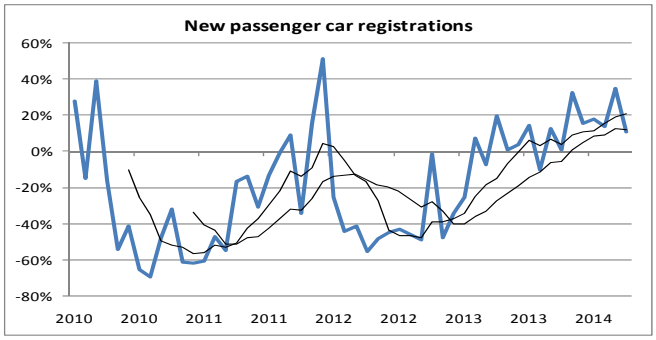
Retail Sales: The pace of decrease of the general index of the volume of retail sales has been markedly diminished to -1.8% in Q4 2013, from -9.1% in Q3 2013, and it has turned positive in Q1 2014. This index registered a small increase by 0.2% in Jan.-Febr.2014, on top of its fall by -15.5% in Jan.-Febr.2013. However, the volume of retail sales excluding sales of oil products fell marginally by -2.9% yoy in Jan.-Febr.2014, compared to its also big fall by -15.0 in Jan-Feb 2013. In 2013 as a whole, the volume of total retail sales fell by -8.1%, down from -12.2% in 2012. From early 2014, it has become evident that economic recovery is broadening to households, while the recent surge in consumer confidence further support this view. ***Consumer confidence indicator*** continued its upward trend for a third straight month to –55 in April 2014 (highest level since March 2010), from -59.7 in March 2014, -65.2 in Feb 2014 and -71.8 in April 2013. On quarterly basis, consumer confidence improved to the still low -63.1 in Q1 2014, from -71.5 in Q1 2013. Moreover, business expectations in the retail trade have improved substantially to 81.1 in April 2014, from 79.5 in March 2014 and from 65.4 in April 2013. On these grounds, household spending on goods is expected to pick up in the coming months, ***with the general index of the volume of retail trade expected to register an increase of the order of 1.2% in 2014,*** from its fall by -8.1% in 2013.

Consumer Confidence



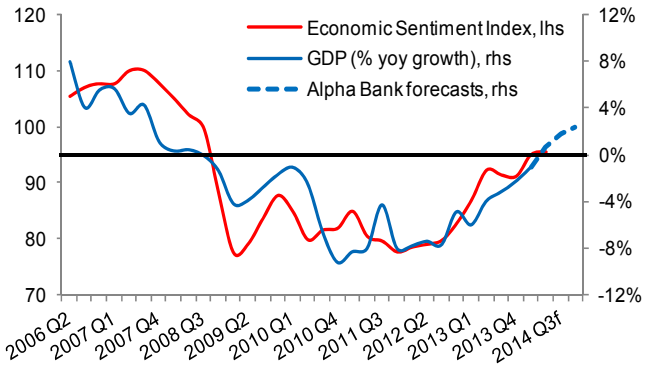
It is noteworthy that private consumption has stabilized in the Q4 2013, when it recorded a small decrease by -0.2% yoy, compared with a fall by -7.8% in Q1 2013. Consumer spending was recorded to be significantly weak in the first nine months of 2013, due to high unemployment and fiscal austerity, but also due to the extensive restructuring that took place in the retail trade market with some big businesses ceasing operations completely. Nevertheless, recent encouraging developments in the labour market and a relative relaxation in fiscal adjustment effort, imply that household spending will pick up further in the coming months. The above developments in the volume of retail sales and consumer confidence indicator point to an expansion in consumer spending from Q3 2014 onwards. Overall, the volume of retail trade has fallen by 39.7% in 2013 compared with 2008 and any recovery is considered from this very low level.

As a leading indicator to the recovery of private consumption may be considered the marked recovery *of new passenger cars registrations in H2 2013 and in Jan.-April 2014 (see Diagram).* In fact, new cars registrations registered a significant increase by 18.7% yoy in Jan.-April 2014, against a fall by -5.7% in Jan.-April 2013. The stabilization of car market started in H2 2013 and continued at a more robust pace in the first months of 2014. In 2013 new car registrations stood at 64.3 thousand, compared with 62.4 thousand in 2012 and 242.6 thousand in 2009. Finally, expenditure on imported cars increased at € 920 mln in 2013, from € 838 mln in 2012 and is expected to increase further in 2014.



The rise in the economic sentiment indicator (ESI) provides another indication that the economy is on track to recovery. The economic sentiment indicator for Greece, which is compiled by the Greek Institute of Industrial Studies (IOBE) and published by the European Commission, further improved in March 2014 to its highest level since Sep 2008, to 97.5, up from 94.8 in Feb 2014, but it fell back to 95.4 in April 2014. The level of the index is now consistent with positive annual GDP growth in Q1 2014. The rise in ESI reflects a broad-based improvement in sentiment across the sectors of the economy and mainly in the manufacturing industry, services and construction.

Economic Sentiment



The rise in the economic sentiment, from the very low levels of 2012, reflects the substantial decrease in uncertainty of businesses and households about their economic prospects and the prospects of the recovery of the economy. Recovery spells confidence, as indicated also by the substantial net inflow of investment capital and recent decline of Greek government bond yields to pre-sovereign crisis levels, around 400 bps.

Other Construction (excluding investment in housing) is expected to be a major contributor to investment and GDP growth from 2014 onwards. This is based:

a) On the reactivation of public investment projects most of which are co-financed by the European Union structural funds with the critical contribution of the European Investment Bank (EIB). Of particular importance in this respect is the restart from the beginning of 2014 of construction activity on the 4-big highways of Greece, which activity had stopped abruptly in 2011 due to disruptions caused by the crisis. More specifically, the Greek government has secured the agreement of the EU authorities to redirect structural funds financing towards the restart of works on these 4-main highways. The final approval of EU structural funds by the Greek government and the re-established contractors in each of the four projects are now coordinating their efforts to go fast forward in the process of implementation of the projects so as to be able to complete them on time, by the end of 2015 as planned. Total investment in these projects will reach € 4.8 bn, of which € 2.9 bn will be financed by the structural funds of the EU and the whole amount of this investment spending will be implemented in 2014 and in 2015 increasing value added and employment in the construction sector in these years, contributing to the expected recovery of the Greek economy. In addition to the above, in 2014 and in 2015 Greece is expected to absorb more that € 8 billion from EU structural funds for the financing of the remaining projects under the National Strategic Reference Framework (ESPA) 2007-2013.

b) On the implementation of ESPA 2014-2020 which provides for financing by the EU structural funds of investment projects in Greece of the order of € 20 billion.

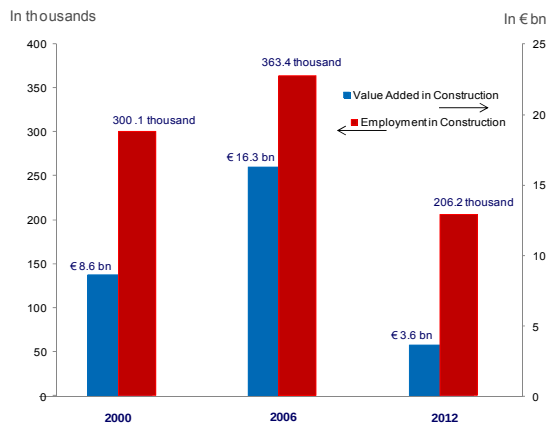
It is important to notice that investment in other constriction registered a positive increase by 3.2% in 2013 (Q4 2013Q +5.4%, Q3 2013: +3.9%), while Gross Value Added (GVA) in Construction (including residential construction) recorded an additional fall by -18.2% in 2013, following its fall by -20.7% in 2012, by -28.4% in 2011, by -32.3% in 2010 and by -24.6% in 2009. Therefore GVA in construction had fallen to € 3.15 billion in 2013 from € 16.2 billion in 2006. With the fast increase of investment in other construction and the stabilization and recovery from 2015 onwards of investment in housing, it is also justified to assume a fast growth of GVA in construction in the following years.

Business Investment: In addition to the above, substantial amounts of investment capital is projected to be attracted to Greece through the fast implementation of the privatization program from 2014 onwards and also through a high volume if investment in the tradable goods sector on the back of the substantial improvement of the international competitiveness of the country.

On the privatizations front, one of the most important developments in the beginning of 2014 was ***the appointment of the preferred investor for the acquisition of the shares in the landmark real estate project Hellinikon,*** following the significant improvement of the financial offer from the part of the selected investment consortium to € 915 million. The expected successful conclusion of this tender in the following months will imply that the selected consortium will undertake to implement an investment program of more than € 5.7 billion in the next 10-years, out of which € 1.25 billion correspond to the costs of building the necessary infrastructure projects in the area, as well as the costs of developing of a wide raging and world class metropolitan park with possibilities to be accessed from all over Athens mainly through the metro network. All these costs will be exclusively assumed by the selected consortium. This huge investment deal for Hellinikon follows the similar deal concluded a few months before with the privatization of Astir Palace resorts in Vouliagmeni, which is also going to imply a huge investment program in luxury tourist facilities and infrastructure in the following years. These two big privatization- investment projects aspire to a drastic upgrade of the Athens area as a high value tourist destination. It is estimated that they may contribute to a substantial increase of tourist arrivals in this area by more than 1.0 million yearly. In addition landmark projects, the process of auctioning and awarding concessions on the ports of Piraeus and Thessaloniki as well as on the Kasteli airport in Crete and a multitude of small airports and ports all over the country is under way. Finally, the privatization of the Independent Power Transmission Operator (ADMIE) and of high value real estate is also currently under way. These projects are of great importance, as it is estimated that are going to generate additional investment mobilizing the needed financial resources in the following years mostly through FDI.

The substantial improvement of the international competitiveness of the country, in combination with the existence of a highly flexible labour market with abundant supply of highly skilled and internationally competitive young personnel, will also contribute to attract FDI in Greece in the following years. Finally, the expected recovery of business investment will also contribute to increase employment and GVA in the construction sector in the following years, from its very low level in 2013, following its dramatic fall in 2009-2013.

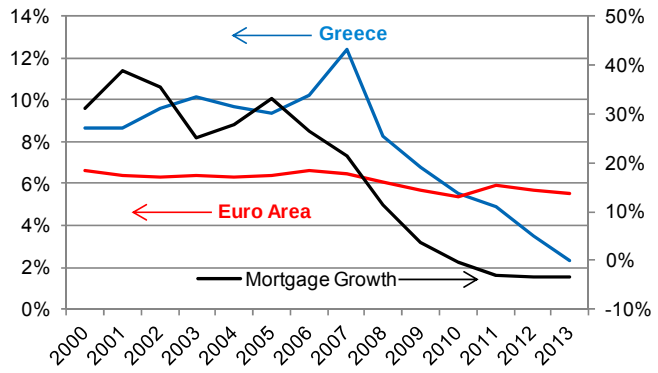
Value Added and Employment in Construction



The Housing market: The recovery of the new car registrations may also be a precursor for the eventual recovery of activity (transactions and investment) in the housing market as well, which until Q1 2014 operates at a dramatically low level of activity. For this recovery, it is assumed that bank lending for mortgages will also

recover from Q4 2014. In general, it is believed that the housing market has bottomed out in H1 2014 and it has the potential to enter into a recovery path, helping to reinforce the recovery of the economy as a whole from 2015. During the six years of recession, several factors led to the collapse of the housing market. The dramatic fall of incomes and of economic sentiment and in particular of consumer sentiment and the big increase and confusion caused in property taxes, contributed to a drastic fall of the demand for housing at abnormally low levels. This in combination with the tightening of credit standards by banks on mortgages, following the upward surge of their NPLs, have led to a decline in mortgage lending by -3.0% in the end of 2013.

Residential Investment (% of GDP)

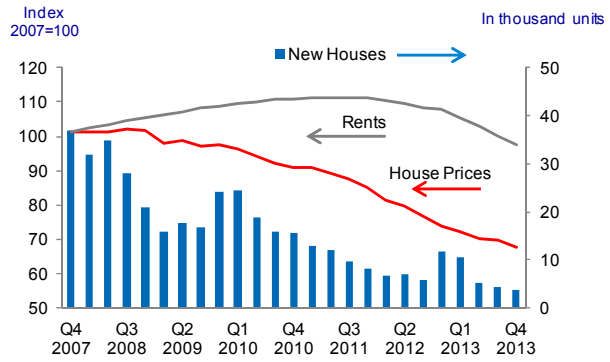


It is noteworthy that during the period 2010-2011 property taxes (mainly the yearly holding tax paid through the electricity bill) stood at 1.5% of GDP, These property tax revenues increased to 2.2% of GDP in 2013 when the government imposed retrospectively three additional property taxes designed initially, but not imposed, for the years 2010, 2011 and 2012. The fall in domestic demand for housing and, on the other hand, the substantial fall of housing investment are also attributed to high unemployment and the abnormally high losses in the disposable income. Therefore, residential investment declined to 2.3% of GDP in 2013, versus 3.5% of GDP in 2012 and 12.4% of GDP in 2007, when in Euro Area residential investment stands at 5.5% of GDP. Also, the number of transactions in new houses declined drastically to 3,841 in Q4 2013, from 4,321 in Q3 2013 and from 24.250 in Q4 2009. Moreover, the index of the value of these transactions (2007=100) fell to 12.1 in 2013, from 17.3 in 2012 and from 80 in 2008. House prices fell cumulatively by -31.2% in 2013 from 2008, with the yoy fall in Q4 2013 reaching –8.5%, from -9.2% in Q3 2013 and 11.7% in Q2 2013.

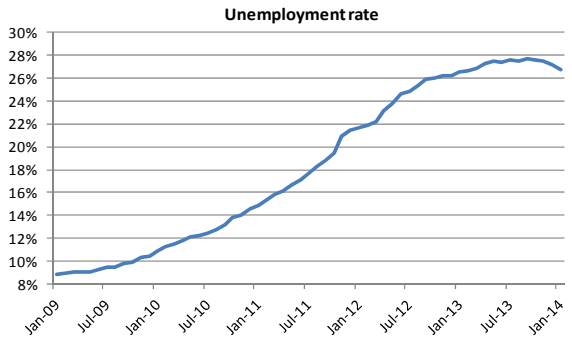
However, the housing market is expected to gradually stabilize in the course of 2014, as housing taxation has been rationalized to a great extend (especially with the drastic reduction of tax on housing transactions) and house prices have become particularly attractive following their 5–years falling trend. More specifically, following the expected recovery of the economy from 2014 onwards with a booming tourism season and substantial increase of the capital inflow for investment in housing, it is expected that the falling trend of house prices will decelerate substantially during 2014 (Q1 2014: -7.5%), with stabilization, or a small average increase, in these prices expected in 2015 and a relatively big increase in 2016. These developments are compatible with the expected GDP growth of 2.9% in 2015 and 3.7% in 2016. On the other hand, it is also expected that fixed investment in housing will stabilize in 2014 and it will have a positive contribution to GDP growth from 2015 onwards.

The above projections are taking into account the fact that ***the volume (in m^3) of building permits*** decreased again by -25.8% yoy in Jan-Feb.2014 (Febr.2014: -5.0%), following their increase by 2.2% in Q4 2013 and their big fall by -36.2% in Jan.-Feb.2013. It should be noted that the issuance of building permits in Dec.2013 and in Jan.-Febr.2014 was affected negatively by the fact that public notaries were on strike in order to register their disagreement concerning the Government's schemes for the implementation of the capital tax on sales of real estate assets. This disagreement has now been successfully resolved, pointing to a possible recovery of permits issuance from April 2014.

New Houses, Prices, Rents



Apart from the above developments, Greece's recovery from 2014 onwards is also supported by the significant improvement in the country's international competitiveness and also by the existing signs of recovery in its labour market, notably private sector employment. In fact, developments in these markets enhance the view that real GDP growth may increase even faster than the already favourable Troika's projection for an average 2.8% real GDP growth in the period 2014-2018. More specifically:



Increasing employment and stabilizing trends in unemployment already from Q1 2014, indicate that the trend of positive GDP growth from 2014 onwards will by based to a substantial degree to a relatively fast increase in labour employment.

The 23% decline in real GDP over 2008-2013 period was accompanied by an almost equal decline in employment by 20.7%. Within 2013 the unemployment rate peaked to 27.7% in Sep 2013, from 26.5% in Jan 2013. However, from October 2013 the unemployment rate registered a gradual fall to 27.1% in Dec.2013, 26.6% in Jan.2014 and 26.5% in Febr.2014 (See Diagram). The sectors affected most by the crisis are construction (cumulative decrease in employment by 54.9% in 2009-2013), manufacturing industry (-34.5%) and trade (-20.5%).

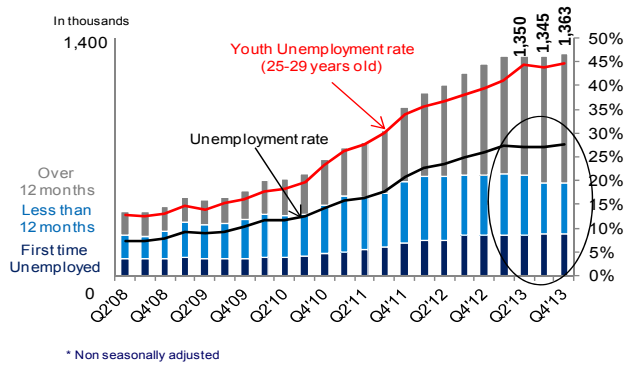
Progress though has been made as a result of the new legal and institutional settings of the labour market, such as a wider use of decentralised wage bargaining, a lower minimum wage and substantial reductions in other non-wage labour costs. These reforms have contributed to a more efficient functioning of the market (both in the private and public sector entities), but also to the rapid improvement of Greece's international competitiveness. In fact competitiveness has improved both through the drastic reduction of statutory minimum salaries and wages and through the abolition of rigidities in the wage setting process, and also through the established full flexibility of management of human capital in domestic businesses, leading to increases in labour productivity.

Gains in employment and international competitiveness is the result of far-reaching labour market reform

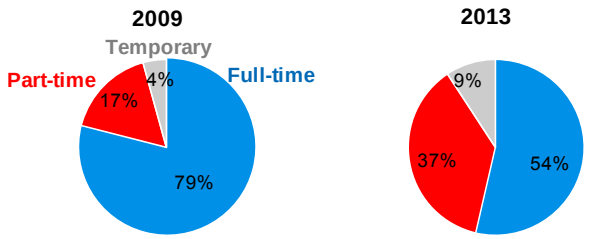
The adjustment programme has been a driving force in restructuring and rationalizing the labour market in Greece and, especially, labour relations in the public sector. Therefore, there has been a substantial fall of employment in the public sector and the Government is on track to deliver a decrease in public employment by 150,000 ahead of schedule, and most likely until the end of 2014. The reduction of ordinary employees in the public sector has been already strong at the end of 2013, as the application of the rule of 1:5 (1 employee can be hired for every 5 retirements) has been pursued consistently. The application of this rule has contributed to significant reduction of the civil servants to 691.1 thousand in 2013, compared to 908.3 thousand in 2009. A further reduction 621.8 thousand employees is projected to take place until 2016. With these trends, it is now essential to hire new high-skilled employees to boost productivity and effectiveness in essential public services.

Greece, exhibited the most significant reductions in the ULC among all countries in the European Union. This was the result of a substantial decline in compensation per employee (2012: -4.2%, 2013: -7.8%) and at the same time an increase in labour productivity (2012: 2.1%, 2013: 0.2%). ***The drastic fall of wages and salaries in the public and the private sectors and the ULC in the economy as a whole is the real evidence of the magnitude of the labour market reforms in Greece.*** These reforms imply that the falling trend of ULC in Greece is bound to continue in the following years as well, mainly through increases in labour productivity at a relatively high rate in 2014-2015. ***ULC is expected to continue to fall in 2014 also as a result of the legislated reduction of employers' contributions in the private sector by 3.9% as of July 2014. L***ooking forward though, labour reforms will have to be safeguarded, securing the already established high degree of flexibility in this market, following the abolition of employment obstacles existing until 2009. This flexibility has allowed a substantial increase in employment in 2013 and in Jan.-April 2014 as will be analyzed bellow. This newly acquired flexibility is expected to also allow today's high unemployment to fall rapidly in the following years.

Unemployment*



New Employment Contracts

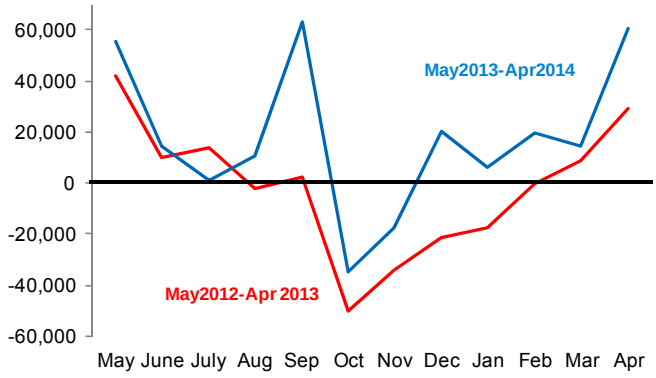


The above reforms in labour market have underpinned recovery in the sector, while there are positive signs for a faster decline in unemployment from 2014 onwards, In this business friendly environment, the fast implementation of the privatization programme will also boost investment and create jobs and thereby lead to the increase in real and potential output of the economy.

As pointed out above, the unemployment rate declined for a 5th straight month to 26.5% in February 2014, after being on the rise until Sept.2013. However, unemployment rate remains high, with an additional worrisome fact that the share of long term unemployed has increased to 72% in Q4 2013, from 65.3% in Q4 2012 and 47.7% in Q4 2010. Moreover, unemployment has reached alarming levers for the youths, as it is elevated at 56.8 % in Jan 2014 (though from a peak of 60.3% in Feb.2013). Additionally, in the end of 2013, 960.000 unemployed personnel was less than 44 years old and about 410.000 of them was less than 29 years old. The institutional changes in the labour market affected also the employment contracts, as it is evident by the increase in the part-time employment in total new employment contracts to 37%, compared to only 17% in 2009. At the same time, full-time employment contracts decreased to 54% of total new employment contracts in 2013, versus 79% in 2009. The recent fall in number of unemployed and the increase in the number of employed by 1.1% mom in Jan 2014 are now concrete signs of substantial improvement in the labour market.

More positive signs emerge from the employment in the private sector, according to the Manpower Employment Organization (ERGANI). New hirings in Jan-April 2014 increase by 178.6 thousands compared to Jan-April 2013 and reached 423.17 thousands. This is a huge improvement bearing in mind that the first months of the year are not favoured by high tourism activity (notwithstanding the big increase in tourist activity in Ian.-April 2014) and also construction activity is law in these months. Most of these hirings use flexible labour contracts and offers low wages and salaries. At the same time, dismissals also increased by 97.6 thousands, though mainly due to an increase by 76.0 thousands in resignations. As a result, employment registered a net increase of 101.5 thousands in Jan-April 2014, compared to a small net increase by 20.46 thousands in Jan-April 2013 and a substantial fall of net employment in the first four months of the year in 2012 and 2011.

Net Hirings Over Dismissals (Private Sector)



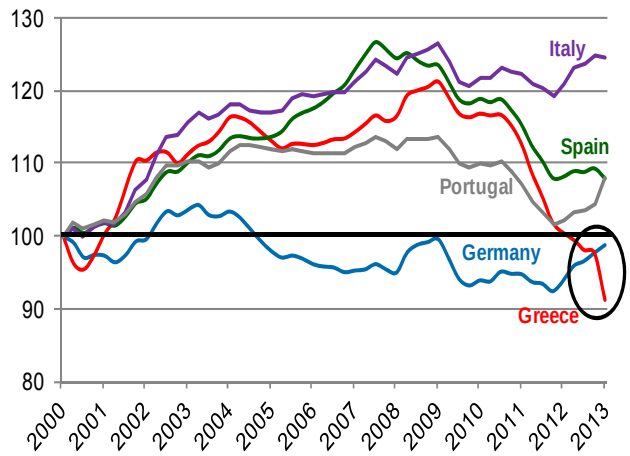
Due to the aforementioned positive developments in labour market, unemployment rate (based on Labour Force Statistics data) is expected to recede to 26.6% in 2014 and further to 25% in 2015. In fact, developments in the labour market in 2013 and in Jan.-Apr.2014 indicate that it is possible for the unemployment rate to decline at a much faster pace than it was anticipated until now.

Full reversal competitiveness losses of 2000-2009

Based on data from the European Commission (Price & Cost Competitiveness and European Economic Forecast, Spring 2014), the internal devaluation, measured as the devaluation of the relative (against 35 trading partner countries) Unit Labour Cost based real effective exchange rate (REER) of the Euro for Greece, had reached the 19.0% in 2013 versus 2009, leading to complete reversal of losses in competitiveness from 2000 until 2009. Comparing to other Euro area countries in the periphery that also experienced prolonged period of recessions, Spain's internal devaluation reached 12.5% and Italy's internal devaluation in the same period 2013/2009 reached a mere 1.2%.

According to the European Commission Spring Forecasts, the Euro REER for Greece decreased by 6.3% in 2013, while an additional fall by 2.2% and 1.8% is expected for 2014 and 2015 respectively. This is a huge adjustment, which could not easily be achieved even if Greece had its own currency and had the ability to apply its own independent monetary and exchange rate policies. This spectacular improvement in the international competitiveness of the country and its upgrading as a place of establishment of internationally tradable industries, is expected to continue in the near future through the maturing of already implemented, or in the process of implementation, structural reforms.

Competitiveness

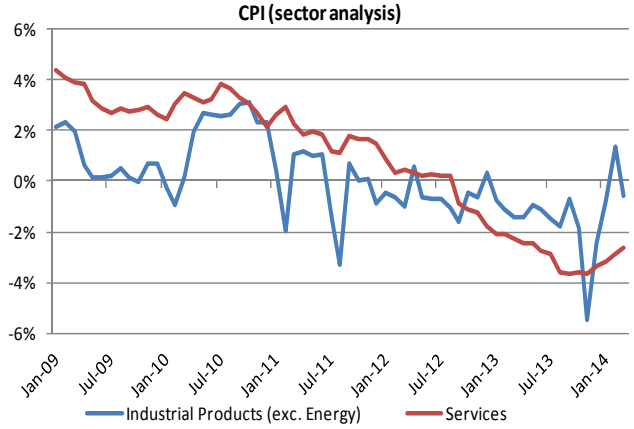


This significant improvement of Greece's international competitiveness led to a spectacular current account adjustment, when in 2013 Greece actually ran a surplus of 1.33% of GDP, against a deficit of 2.2% of GDP in 2012. Most of the improvement that started in 2010 is due to the substantial fall in the trade balance deficit, i.e. an increase in exports of goods (2012: +8.9% 2013: +2.3%), and a corresponding decrease in imports of goods (2012: -12.3%, 2013: -4.5%), as well as the improvement in services surplus. The case of Greece has proved beyond doubt that restoring competitiveness sustainably through internal devaluation is possible, even under the most unfavourable economic and political conditions. It is true that the implied cost of adjustment in terms of lost output and employment (from the peak of the macroeconomic bubble of 2009) was substantial, but this cost would have been dramatically higher, had Greece opted to pursue the needed adjustment through an unrequited exodus from the Euro.

Looking forward, the current account surplus is expected to show further improvement in 2014. This is already evident by the surplus in the current account (including capital transfers) of €450 mln in Jan-Feb 2014 versus a deficit by €367 mln in Jan-Feb 2013. Positive effects stem from tourism (tourism receipts increased by 17.3% yoy in Jan-Feb 2014), as well as shipping (shipping receipts increased by 5.6% yoy in Jan-Feb 2014). On the other hand, capital account is expected to be in a surplus in 2014, due to capital inflows concerning banks' capital increases and to many businesses borrowing from the international capital markets and due to the interest of foreign investors to invest in Greece.

As mentioned earlier, the unprecedented fiscal adjustment led to substantial and prolonged fall of domestic demand and ULC affecting negatively non-traded goods prices as well. These significant declines in

domestic demand and labour costs started to affect the market prices of domestic goods and services as soon as the impact of indirect taxation on these prices and also the impact of rising cost of energy started to wane. As a result, inflation dropped in 2012 and continued its steady decelerating trend in 2013, falling actually to a negative territory from February 2013 until now. Therefore, CPI inflation reached -2.9% in Nov.2013 and continues to register negative figures -1.3% in April 2014, from -1.5% in March 2014 and from -1.1% in Feb 2014.



The advent of negative inflation was unavoidable, as the prices of most non-tradable products had reached exuberant levels rising at abnormally high and unsustainable rates in the period 2001 – 2009. It is a true that in the beginning of the application of the adjustment program in 2010 and in 2011, inflation remained elevated. This was mainly due, first to the significant increase of crude oil prices in this period and, second, to the explosive increase of the prices of many services, as administered prices of state-controlled entities were rising for the purpose of trimming their deficits and turn them into surpluses. Moreover, the substantial increase in indirect taxation (VAT increase, excise tax on fuels and tobacco, electricity and car circulation fees) had a temporary positive effect on Inflation. Therefore, inflation remained in this period at higher levels for non-tradable goods compared to tradable goods (excluding energy). This trend was completely reversed in 2012 until now. Deflation intensified to the prices of services-non tradable goods (Mar 2014: -2.6%), more than in the industrial products (Mar 2014: -0.7%).

Negative inflation in Greece is not necessarily a negative development, especially if it is considered as temporarily, that is as long as expectations about the continuation of negative inflation remain timid. In the current period, negative inflation in Greece serves as stabilizing factor of real income and of purchasing power of households, as well as contributors to the improvement of international price competitiveness of the country, especially concerning the tradable goods sectors. The current nuisance is that the abnormally high fall of GDP deflator (Q1 2014: -2,43%), implies a slower fall of the headline general government debt to nominal GDP ratio, a development that reinforces the arguments of those who want to support their view according to which the sustainability of today's Greek GG Debt is still not certain. However, even this uncertainty is likely to end in the following months in Greece as the country recovers from its 6-year recession. CPI inflation is expected to remain negative of the order of -1.0% in 2014, contributing to a further improvement of Greece's international competitiveness, but it will turn positive again from 2015, following, of course, inflation developments in the Eurozone. On the other hand, inflation in Greece may remain low as a result of the low inflation in the Eurozone. Euro Area's sluggish recovery may fail to erode existing spare capacity in many productive sectors and, also, high unemployment and this may intensify, or fail to eliminate, deflationary pressures in the common currency area. The ECB is now ready to combat such unfavourable developments and its possible to apply monetary policy measures which will both maintain drastically low interest rates, a fairly valued exchange rate for the euro and overall increased liquidity in the Eurozone. Such a turn of events will also be beneficial for Greece's recovery.

Institutionalizing an unprecedented extensive array of fundamental structural reforms

Greece has made significant progress in structural reforms, which are analyzed, in great detail, especially in the latest report of the European Commission (The Second Economic Adjustment Program for Greece, Fourth Review – April 2014). These fundamental reforms have contributed greatly: a) to the unprecedented fiscal adjustment, amounting in 2014 to 17.1 percentage points of GDP on cyclically adjusted basis, from 2009, b) to the huge (by any international standards) improvement of Greece's international competitiveness, also presented above, c) to the substantial increase in wage employment in the private sector of the economy already from 2013 and early 2014, that is from the very early stages of the recovery of the economy with the help also of the spectacular performance of the tourist sector in the last two years.

Moreover, these reforms, especially concerning product market regulation, are already contributing greatly to the far reaching and fundamental restructuring of some very important sectors of the Greek economy, although with considerable social disruption and resentment from the part of vested interests in these sectors, in the short run. It has now become more obvious that these sectors had been operating until recently under excessively protective - government imposed - walls, disallowing any form of competitive action between the economic units operating in these sectors and also imposing considerable barriers to entry to outsiders. And these protective walls, which were imposed by a complicated and opaque state legislation, were mainly at the great expense of consumers and of other domestic businesses and also at the expense of the economy as a whole. These walls have now been abolished completely in almost all previously closed professions and sectors both through the abolition of all relevant legal provisions imposing them, as well as through the effect of the substantial fall of domestic demand, which has imposed the need for competitive and entrepreneurial practices from th part of businesses and professionals operating in these previously closed to competition sectors. Today, competition is reviving in most sectors of the Greek

economy, especially in sectors producing goods and services not exposed to competition from abroad. This has contributed to the substantial fall of the relative price of non traded goods in the domestic economy, which is the main indicator of the improved competitiveness of the internationally competitive goods and services of the country, including tourism.

Therefore, reforms aiming to modernize product markets and improve international competitiveness have already started to bear fruits in a big way. In fact ***a great number of supplementary but still significant institutional reforms were ratified by the Greek parliament in April 2014,*** which included the removal of remaining regulatory restrictions in sectors as food processing, retail trade and in particular pharmacies, building materials and tourism, which had been identified and assessed as disproportionate by the Competitive Assessment Toolkit of the OECD. Following this legislative action, the Greek Government has actually achieved in implementing almost the total of the 329 OECD recommendations included in the aforementioned toolkit.

Finally, concerning efforts to drastically reduce the rigidity of Greece's product market regulation, OECD indicators show that Greece has achieved the sharpest reduction of restrictions in this field among all OECD countries in the period 2008-2013. Therefore, even in early 2013 Greece was ranked in a better position concerning its degree of product market regulation than Germany, Belgium, Austria, the Czech Republic, Hungary, Canada, Portugal and Israel. Moreover, Greece was ranked in the same level of regulation with France and the Slovak Republic. Moreover, However, It is now almost certain that taking into account the deregulations which were implemented by the Greek government in H2 2013 and in Jan.-April 2014, Greece will most possibly be ranked between the most deregulated countries in the world in the new reports of the OECD for 2014 and for 2015 concerning product market regulation.

In the energy sector, the legislation of reforms needed for the increase of competition in the sector, with the restructuring and privatization of the Public Power Corporation (PPC), are already well under way. In this process, in February 2014 the Greek Parliament has voted for the legislation which provides for the unbundling of full ownership of ADMIE from PPC in order to facilitate the sale to the private sector of the 66% of the share capital of ADMIE (where the relevant auction is already under way, with expressed interest from world class grid operators and investment consortiums), with the rest 34% to be maintained by the Greek state. In addition, the Government has transferred 17% of the shares of PPC to the Hellenic Republic Asset Development Fund (HRADF) to start preparing the privatization of the company. Also, the Government has already submitted to Parliament legislation foe the privatization of small PPC.

Concerning the tax system of the country and the tax administration system, major reforms have been undertaken and legislated in H2 2013 and continued into 2014. These reforms aim to broaden the tax base of the country, to simplify and codify tax legislation, and to improve tax collection rates. These reforms are analyzed extensively in the recent Report of the European Commission (April 2014), which also evaluates them as follows: ***"These reforms represent a major simplification and modernisation of the tax system and are expected to bring in considerably higher revenues from the widening of the tax base.*** The success of these reforms will allow a period of stability in the tax system for many years to come that will favour new investment and address the concerns of foreign investors about the instability of the tax system". No further comment is required here.

In the field of labour market reforms the European Commission (EC) has estimated that: a) Greece was at the top of the countries in adopting reforms that decreased the stringency of labour market regulations. b) In the area of wage setting, Greece has been by and large the country most active in making wage formation more adaptable. c) In the areas of employment protection legislation (EPL) and working time, Greece has also been a very active reformer even if other countries have been changing their institutions too. Overall the EC recognizes that the favourable effects of the drastic reforms implemented in the Greek labour market in the last four years are remarkable in all areas intended to improve, namely in increasing employment even before the recovery of the economy and in achieving an unprecedented improvement in the international competitiveness of the country. Moreover, the labour market reforms contributed in achieving positive increase in labour productivity for the economy as a whole even in 2012 and in 2013, despite the substantial fall of GDP in these years. However, the most important positive effect of the labour market reforms is expected to appear in the following years in terms of fast increasing of both employment and productivity, which is equivalent to high growth of Greece's potential output. The Troika has now turned its attention to needed further improvements in the Greek labour market trying to make certain: (i) that the maintenance in force of an artificially high minimum wage for long term unemployed will not constitute an unsurpassed impediment for these workers to return to employment, and (II) that the needed programs and measures are in place for the upgrading and expansion of vocational education, training and apprenticeships for improving the employability of people already in employment, as well as of the unemployed, and for fostering sustainable and competitive employment and overall efficient use of human capital in the country. As the EC points out, an outline roadmap has already been adopted by the Greek government and the legal framework has been revised. But, according to EC, collaboration between the Ministry of Labour, the Ministry of Education, and OAED has so far been insufficient. Therefore, substantial additional work is needed for the implementation of a really effective and comprehensive program in this crucial sector.

All these changes in the market and growth enhancing structural reforms are also reflected to the significant improvements recorded in the ranking of Greece in the Doing Business Index comprised by World Bank. According to the latest report, Greece achieved to jump to the 72nd position in overall ranking in 2013, versus the 109th ranking in 2010. In particular, regarding the ranking

of starting a business, Greece managed to jump 113 ranks from 149 to 36 in 2013.

Doing Business, World Bank	2013	2012	2010
Ease of Doing Business	**72**	**78**	**109**
Starting a business	36	146	149
Protecting investors	80	117	154
Getting credit	86	83	89
Dealing with constuction permits	66	31	51
Registering property	161	150	153
Paying taxes	53	56	74
Trading across borders	52	62	84
Enforcing contracts	98	87	88
The Global Competitiveness Report, WEF	**2013**	**2012**	**2010**
Global Competitiveness Index	**91**	**96**	**83**
Infrastructure	38	43	42
Health and primary education	35	41	40
Technological readiness	39	43	46
World Competitiveness Ranking, IMD	**2013**	**2012**	**2010**
Competitiveness Overall Score	**54**	**58**	**56**
Business efficiency	47	56	48
Government efficiency	56	58	54

Regarding the privatization program, notwithstanding the developments in the energy sector and the selection of preferred investors for Hellinikon AE and Astir Pallas analyzed above, the following developments are also important:

In the field of real estate assets, t**he Government has now defined a roadmap for alternative sale methods of real estate assets. These methods include now asset securitisation and monetisation in order to raise additional revenues beyond what is currently foreseen in the privatisation plan.** Such efforts will be targeted at the private sector, in particular international investors and will complement the direct sale of assets currently on-going. This project, combined with improving investor interest in Greece, can help raise additional proceeds in the medium term. The Government will assess the progress in this field in the coming months and will, if needed, revise upwards the estimated proceeds from privatisation presented in the above Table. The 1st progress report in this field will be submitted by the Government by end-June 2014. The 1st transaction in this category of privatization should have been completed by end-November 2014. Until now, the transaction for the sale and lease-back of 28 buildings of the Greek state, amounting to € 261 million has now been completed as it has been approved by the Court of Audit. Moreover, preparatory work is advanced to secure the transfer of full and direct ownership of 1,000 commercially viable real estate assets to the HRADF.

For the privatization of the Piraeus Port Authority (OLP), Thessaloniki Port Authority (OLTH) and of peripheral ports the Government has passed the Law related to the establishment and staffing of port regulatory authority. The new regulator will oversee the ports market in Greece, after the privatisation of a large array of ports, in particular those of Piraeus and Thessaloniki. The Government proceeded to strengthen the effectiveness and autonomy of the port regulator by appointing the Board of Directors of the new authority. In addition, it remains committed to adopt and implement the secondary legislation aiming to have a fully functioning regulatory authority in the sector by the end of the tender process for the ports. In fact, the tender process for the Port of Piraeus is well under way.

For the privatisation of EYDAP and EYATH, the water companies, the Government has already legislated measures to strengthen the independence and operational capacity of the Special Secretariat of Water (the water regulator) by revising legislation enabling the Special Secretary to issue formal decisions on all regulatory matters. The new legislation provides for fixed–term contract for the water regulator, which will ensure its management continuity and independence. The new water regulator has already been staffed with needed personnel, which was transferred from existing government services. Also, additional preparatory work for making possible the privatization of these two companies has progressed according to plans. Nevertheless, the launch of tender for EYDAP depended on the decision by the Council of State regarding the legality of the transfer of the shares of the company to HRADF. In fact, the decision of the court appears to be negative for the continuation of the privatization process in the form that has been designed until now.

Nevertheless, the following developments are important: (i) concerning EYATH, ***the issue of the five year pricing policy*** (for the period 2014-18) has been settled. The Government has passed through Parliament an amendment to article 21 of Law 2937/2001, in order to align the process of the pricing policy of EYATH SA with that of the other water and sewerage services providers as provided for by Law 4117/2013 and the complementary Ministerial Decisions. (ii) the needed legislative acts permitting the payment of arrears owed to EYDAP and EYATH directly from the arrears clearance program have been implemented. As the European Commission points out (Report on Greece's compliance, 16 December 2013), water arrears have been validated and paid to the water companies. Moreover, other investment-related arrears have also been validated and the decision to pay them has been issued through a Ministerial Decision, with the remainder being off-set against obligations by the water companies to the state, or written off with all relevant parties in agreement. The Board of EYDAP has recommended to its General Assembly, meeting on 27 December 2013, to accept the settlement with the government laid out in a Joint Ministerial Decision issued on 3 December 2013, and hence recognise that there is no outstanding debt. At the GA meeting on 27 December 2013, HRADF endorsed the above recommendation by the EYDAP management.

For the privatization of TRAINOSE/ROSCO the Government has passed legislation which is specifying licenses and permits for the railway properties and real estate assets than will be included in the privatisation perimeter of TRAINOSE and ROSCO. Moreover, the Joint Ministerial Decision has been issued for the transfer of the rolling stock ownership from OSE to Hellenic Republic (HR) and a tender has been launched for the valuation of rolling stock not in use owned by OSE of HR. In July 2013, the HRADF requested pre-qualification bids for TRAINOSE, the rail operator in Greece.

Overall, the implementation of the privatization program is on track, on the back of restoring

confidence and strong interest by foreign investors, contributing to the recovery of the Greek economy, expected to record positive growth from Q2 2014. European Commission estimates privatization revenues of the order of € 1.5 bn 2014 which may easily be surpassed, as the revenues from DEPA and DESFA are transferred in 2014, and 2014 will be a year of positive growth and lower cost of money in the economy. For the following years, privatisations and the recovery of the real estate market will be two of the main drivers of growth for the Greek economy. The latest estimates of the revenues expected to be achieved in the period 2013-2020 are shown in the following Table.

Expected Privatisation Receipts

By the end of:	Yearly proceeds	Cumulative receipts since 2011 (EUR billion)	
2011	1,6		Outcome
2012	0,0	1,6	
2013	1,0	2,6	
2014	1,5	4,1	Forecast
2015	2,2	6,3	
2016	3,4	9,6	
2017	2,9	12,4	
2018	3,0	15,4	
2019	3,4	18,7	
2020	3,6	22,3	

Source: European Commission services.

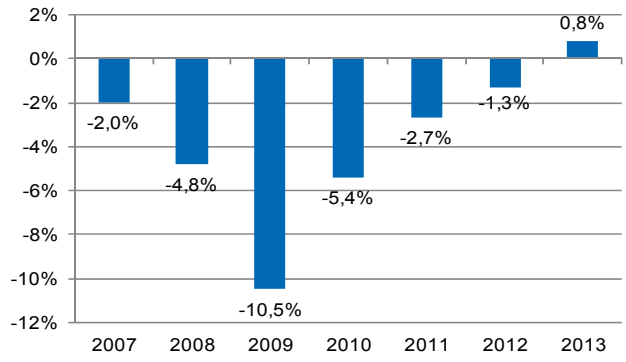
Note: Cumulative receipts are considered within the 2012-2020 period, including the EUR 1.6 billion generated since 2011.

Fiscal Adjustment continued to be strong

Fiscal performance continued at an unabated pace in 2013, when Greece exceeded its fiscal target and recorded a primary surplus of 0.8% of GDP. Overall, Greece has accomplished a significant improvement in its fiscal position since 2009, as it managed to eliminate the primary government budget deficit of € 24 bn in 2009 and to record a surplus of € 1.4 bn in 2013. This constitutes a fiscal adjustment of 11.2 percentage points of GDP, or more than 16 pps of GDP on a seasonally adjusted basis, within 4-years. This impressive adjustment was achieved on the back of extremely adverse economic, political and social conditions, depressing projections about the prospects of the Greek economy, and subsequent dramatic downgrades by credit rating agencies. The above depressing economic environment was triggered by scenarios about Greek exit that prevailed from mid-2011 until 2013. Now that the risk about Greek exit has been eliminated, the political environment is stable and confidence has been restored, the ground has been set for a continuation in fiscal adjustment without any obstacles that could derail the programme.

The strong fiscal result in 2013 largely reflects a better than planned outcome from the implementation of the State Budget. In particular, on the expenditure side, primary current expenditure recorded a much steeper fall by -6.9% in 2013, as compared to -5.2% that was planned in the Budget2014. Social welfare spending recorded notable under-execution compared with the budgeted amounts by €549 mln. As regards revenues, tax collection turned out to be better than anticipated, as the collection of direct taxes in H2 2013 and especially Q4 2103 was robust. Property tax collection was strong, amounted to €2.99 bn, despite the fact that four new property taxes were imposed, as well as personal income taxes which amounted to €7.98 bn and VAT taxes-excluding fuel and tobacco at €10.9 bn.

General Government Primary Balance (as % of GDP)



As a result of the completion of the prerequisite actions of Greek authorities and the confirmation of the general government primary surplus at 0.8% of GDP, Eurogroup Ministers approved the next EFSF installment of € 8.3 bn, to be disbursed in three tranches. Moreover, in accordance with the Eurogroup statement on November 2012, the authorities will transfer 30% of the € 1.4 bn to the segregated account concerning debt reduction. On the other hand, the authorities are already in the process of distributing €524 mln as a one off payment to the most vulnerable social groups such as long term unemployed, low-income families and pensioners, as well as military servants. Finally, another part of the over performance of the budget is expected to be used for arrears payments.

It should be noted here, that the GG primary surplus of 0.8% of GDP in 2013 excludes expenditure related to banking support of 10.8% of GDP (which was used in 2013 in the process of restructuring and recapitalization of the domestic financial institutions). In addition, it excludes Greece's revenues of 1.5% of GDP from the return of profits of NCBs from GGBs purchased by the ECB under the SMP program.

The above positive developments set the ground for the beginning of talks, to take place after the European elections, over whether it should be decided additional debt relief measures. As it was stated by Eurogroup chairman, in the Eurogroup in April 2014, relative merits of possible debt sustainability would be considered in Greece's next bailout review this coming fall.

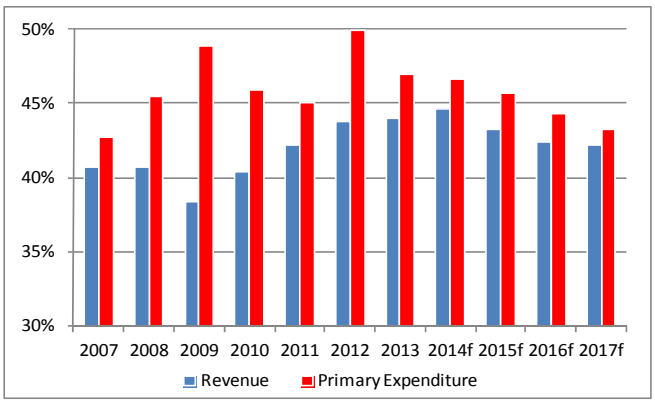
In the following years, the authorities reaffirmed their commitment to comply with the fiscal targets, i.e. a primary surplus of 1.6% of GDP in 2014, 3% of GDP in 2015 and 4.5% of GDP in 2016. Regarding 2014, the implementation of the Budget in Jan.-April 2014, reaffirms that the fiscal target for a primary surplus of 1.6% of GDP in 2014 remains within reach and even reflects the strong possibility for better than planned outcome.

In particular, European Commission expects the GG revenues to reach 44.6% of GDP in 2014, versus 44% of GDP in 2013, and decline to 43.2% of GDP in 2015 and

further to 42.4% in 2016. With these assumptions the primary surplus may turn out to be a little lower than the targeted surplus in the period 2015-2017. However, the series of administrative measures that the government has already adopted and is in the process of implementation, including the improvement in tax collection, and social security contributions, in accordance with the robust economic growth, do not validate the assumptions for the substantial fall of GG revenues as a percent of GDP. Therefore, in the event that the GG revenues will be maintained at the level of 44% of GDP in 2015-2017, then the target for a GG primary surplus of the order of 4.5% of GDP is attainable. Nevertheless, the sustainability of the Greek GG debt may also be secured even with a primary surplus of around 4.0% of GDP, if this is combined with an average growth of GDP of the order of 3.0% in 2015-2021, as Troika is projecting.

General Government Budget: European Commission forecasts						
	2012	2013	2014f	2015f	2016f	2017f
Revenues (% of GDP)	43,8	44	44,6	43,2	42,4	42,2
Primary Expenditure (% of GDP)	45,2	43,2	43,0	41,3	39,8	38,6
Primary Surplus (% of GDP)	-1,4	0,8	1,6	1,9	2,6	3,6
Revenues (€ bn)	84,7	80,2	81,1	81,2	83,6	87,2
Primary Expenditure (€ bn)	87,3	78,7	78,2	77,6	78,6	79,8
Primary Surplus (€ bn)	-2,6	1,5	2,9	3,6	5	7,4

General Government Primary Balance (as % of GDP)



Regarding implementation of the Budget in 2014, it is expected (i) a decrease in revenues from the income tax on Individuals that will be offset by a higher increase in the corporate income taxes, as a result of a substantial redistribution of income in these two key categories (ii) an increase in revenues from property taxes of the order of € 3.9 bn in 2014, up from €2.9 bn in 2013, which is considered feasible, as a big part of the property taxes imposed in 2013, will actually be collected in 2014. In fact, revenues from property taxes reached already € 0.932 billion in Q1 2014, almost exclusively from taxes imposed in 2013 as substantial instalments from the special levy on buildings collected through the electricity bill (EETHDE) and of the property taxes (FAP) of the years 2011, 2012 and 2013 are scheduled to be paid in 2014. Overall, net current revenues in 2014 are expected to increase by 2.6% and reach € 49.7 bn. One can argue that in 2014, the measures that the government is going to take to support employment, such as a cut in social security contributions of IKA by 3.9 bps, may take a toll on the GG revenues. However, the shortfall in social budget revenues is expected to be fully compensated by other actions that the government has already implemented, such as elimination of OAED, rationalization of OAEE exemptions, etc.

On the expenditure side, it is noteworthy that fiscal adjustment in 2012 and 2013 was mainly due to ***the substantial fall of the GG primary expenditure, which reached*** -5.8% in 2012 and -6.9% in 2013. This huge decline in primary expenditure is the most prominent characteristic of Greece's spectacular fiscal adjustment. It has contributed to the fall of Greece's GDP in 2010-2013 not only through the required fall of excessive government consumption, but mainly through the substantial continuous fall of government investment.

According to European Commission, GG primary expenditure is expected to fall only marginally by -0.6% in 2014. However, this is not supported by the execution of the Central Government budget in Jan.-April, where the fall current primary expenditure was -10.1% yoy. Moreover, further steps have been taken on the rationalisation of public expenditure such as reducing military procurement programmes, eliminating OAED family benefits, reducing OAED training programs, rationalizing OAEE exemptions.

The better than planned implementation of the 2014 budget in Jan-April 2014 points to a GG primary surplus of more than 1.6% of GDP in 2014. According to the Medium Term Fiscal Strategy (MTFS) 2015-2018, the GG primary surplus is expected to be 2.5% of GDP in 2014.

More specifically, developments in the Central Government in Jan.-April 2014 are as follows. Primary surplus of the central government reached €1.05 bn (Jan.-Apr.2013 deficit of € 0.31 billion), compared with a planned surplus of € 1.96 billion in 2014 as a whole. This was due to an increase in total current budget revenues by 3.2% and to a new substantial fall in current budget primary expenditure by -9.6% (Jan.-Apr.2013: -12.3%). Net current budget revenues registered a fall by -1.3%, but this was due to the exceptionally high increase of tax rebates to € 906 billion in Jan-Apr.2014, from € 325 million in Jan.-April 2013. On the other hand, the surplus of Public investment budget (PIB) was at the same level as in Jan.-Apr.2013, despite the substantial increase of PIB revenues and expenditures in the first four months of 2014. Overall, the implementation of the Central Government Budget in Jan.-April 2014 (presented in the Table bellow) was again satisfactory and paves the way for the better than planned implementation of the GG budget for 2014 as a whole.

Regarding the planned fiscal adjustment for the period 2015-2017, Troika's projections in April 2014 point to a possible fiscal gap of the order of € 2.0 bn in 2015 and for additional € 1.8 bn in 2016. With these measures Greece will be able to achieve the planned primary surplus of 3.0% of GDP in 2015 and 4.5% of GDP in 2016 and a surplus higher than 4.5% of GDP in 2017. However, no fiscal gap for the period 2015-2017 is envisaged in the new MTFS 2014-2018, which has been published by the Greek Government. Also, as analysed below, Greece may not need additional measures to cover its fiscal targets and financing needs in 2015-2016:

With respect of the fiscal targets, the execution of the Central Government Budget in Jan.-Apr. 2014 shows that

the primary surplus in the Central Government amounted to €1.05 bn, against the target for a surplus of €0.74 bn. Considering this development and taking account the recovery of the Greek economy, it is estimated that the GG primary budget surplus may be higher than planned in 2014 and it also may surpass in the surpluses projected be the Troika in 2015-2017.

Central Government Balance

(in € bn)	Jan-Apr 2013	Jan-Apr 2014	Actual % change	2013	2014B	% change
Revenue	15,743	16,136	2.5%	51,018*	52,095*	2.1%
Primary Expenditure	16,048	15,090	-6.0%	52,415	50,098	-4.4%
Primary Surplus (+)	-0,305	1,046		-1,397*	1,997*	

*Excluding one-off transfers of €2.7 bn in 2013 and €2.6 bn in 2014 revenue as officially budgeted (B2014)

With respect of the financing needs of the country, these have already been lowered by € 3 bn with the government 5-year bond issuance in April 2014. Moreover, Greece's financing needs may be reduced further, as the substantial bank capital increases through private investors gives the opportunity to the banks to buy back their preference from the State, reducing the State's financing needs by about € 5.0 billion. In addition to the above, the authorities estimate that part of the amount of government bonds that still is held by ETEAN will not be needed, thus reducing financing needs for August 2014.

In fact, according to the European Commission, in 2014 and until May 2015, financing gap does not exist, as the program schedule completely covers all financing needs.

In 2015, total financing needs are estimated at € 21.1 bn. This amount derives from maturities concerning debt towards European Central Banks (€ 8.0 bn) and the IMF (€ 8.6 bn), GG interest payments of € 5.3 bn and arrears payments of € 2.5 bn. The financing requirements in 2015 are scheduled to be financed: α) by the trances of the existing financial support package from the IMF amounting to € 7.2 bn, b) by interest payments deferrals € 2.6 bn, c) by the return of GGBs related profits of NCB of the Eurozone (SMP plus ANFA) € 2.0 bn, d) by the primary surplus of 2014 which is estimated by the EC to reach to € 3.3 bn (compared with a planned surplus of € 5.6 billion) and e) by privatizations amounting to €2.2 bn. According to this analysis of the EC, additional financing needs amounting to €12.4 bn are estimated for 2015. However, in financial sources of the Greek government existing in 2015, the EC appears to have underestimated the following: First, the possibility of additional financial resources amounting to € 4.5 bn to be obtained from government bond issuance. Second, the resources that have already become available from the redemption of pillar I bonds issued for the purchased of preference shares from the banks and for other purposes. Third, the privatization revenues may exceed substantially the assumed € 2.2 billion in 2015. Fourth, the GG primary surplus may indeed be higher than € 3.3 billion.

In the above Table it is shown that the alleged financial gap for 2015 may easily disappear, assuming that developments in the Greek economy in 2014 and in 2015 will evolve as its is currently projected. Overall, Greece is now well positioned for the successful completion of its fiscal adjustment program in 2014-2017, with GG primary surpluses of about 4.0%-4.5% of GDP and GG deficits below 2.0% of GDP from 2016 onwards.

Financing Needs in 2015		
	E. Commission Estimates	**Alpha Bank Estimates**
Primary Surplus	3,3	5,6
Interest Payments	5,3	5,3
Govenrment Cash Deficit	-2,0	0,3
Arrears	-2,5	-2,5
Maturing Debt	-16,6	-16,6
Financing Needs	-21,1	-18,8
Financing Sources in 2015		
Preferred Stock	0,0	3,0
Privatizations	2,2	2,8
Repos	-0,7	0,0
ANFA & SMP profits	2,0	2,0
IMF disbursement	7,2	7,2
Recapitalization	0,0	1,5
Buffer	-2,0	-2,0
Bond markets	0,0	4,3
Financing Sources	8,7	18,8
Estimated gap	**-12,4**	**0,0**

On debt sustainability

According to the European Commission, the debt sustainability analysis based on baseline and stress scenarios points to a slight deterioration in the debt-to-GDP ratio by the end of 2020, in comparison with the previous report in July 2013. In particular, debt-to GDP ratio is estimated to gradually decline to 125% in 2020 and around 112% in 2022, from a peak of 177% in 2014.

This outcome is based on several factors: a) a lower forecast for nominal GDP change in 2014, when a decline of -0.7% is projected now, compared to -0.4% that it was estimated in July 2013, b) a new forecast for less privatization revenues of € 22.3 bn cumulatively in the period until 2020, versus €24.2 bn that it was previously projected and c) a higher level of arrears clearance by € 2.1 bn compared to the previous review. During 2013, €6bn of arrears were repaid while the total stock of arrears amounted to €4.7 bn. Clearance of arrears will be completed in 2014 and may lead to deterioration in the debt ratio temporarily in 2014, though in the medium-long term, this procedure has positive effects in the economic activity and in the debt.GDP ratio.

In the above scenario of the European Commission is again not taken into account the return of capital to the government following the buy back of preference shares by the banks, as well as the repayment of HFSF capital through the exercise of the warrants that International and domestic Investors maintain in their portfolios to buy bank shares from the HFSF. If this is taken into account, then the GG debt/GDP ratio falls bellow 120% in 2020. To this effect one must also take into account that the buffer capital of € 11 billion of HFSF may not be used after all to recapitalize the already fully capitalized banks.

Healthy and well capitalised banking sector

The first recapitalization of the four core Greek banks took place in May-June 2013. The Greek banks had suffered heavy losses on both their investments in GGBs and on their loans due to the protracted recession of the Greek economy. Their recapitalization was based on the viability assessment exercise conducted by the Bank of Greece (BoG) in 2012 with the assistance of Bain & Co, which determined the capital needs of all Greek banks. These needs comprised the valuation losses of Greek banks from GGBs and also the expected losses that the banks would safer in a 3-year horizon under the basic and the adverse scenario (concerning economic developments in the country) of a stress test exercise. Credit loss projections under this test were calculated by BlackRock and also projections of bank's balance sheets and income statements. Therefore, already from November 2012 the BoG had informed all banks of their individual capital needs.

After substantial delays due to protracted negotiation with the Troika all through 2012 for the conditions under which the financing of the Greek Adjustment Program would continue, the four systemic banks were finally obliged to proceed with their recapitalizations in May-June 2013, in the unfriendly investment environment that was created immediately after the eruption of the Cyprus crisis (March 2013). Nevertheless, the 3 of the 4 core banks succeeded to complete their recapitalisation exercise according to the requirements of the BoG and along the recapitalization framework prescribed in Law 3864/2010 and the Cabinet Act 38/2012, managing also to attract at least 10% of their required capital increase from private sources. Therefore, collectively they managed to attract more than € 3.0 billion share capital mainly from international investors in the still difficult early 2013.

Therefore, by the end of June 2013, all four core banks had completed their recapitalisation exercise, while Alpha, NBG and Piraeus bank had also managed to raise more than 10% of their required capital increase from the private sector, thus maintaining their capability to be managed by their existing management. The remaining amount of the needed share capital was provided by HFSF, which, however, has restricted voting rights. Moreover, the shares of HFSF are set to be bought by the private investors who have in their possession the warrants issued to those that participated in the capital increase. Eurobank on the other hand was fully recapitalised through the absorption of € 5.8 billion from the HFSF, which became its main (more than 95%) shareholder with full voting rights.

In addition to the above the Greek authorities proceeded to develop a new comprehensive strategy for the development of the Greek banking sector. The aim of the strategy was to create a leaner, cost efficient, competitive and well capitalised banking sector, with rationalised foreign presence and divestments in non-core assets and with stable local funding with sustainable cost and lower reliance on central bank funding. **The new structure of the new banking system was quickly formed around the recapitalized 4-systemic banks.** In the new system m**anagement of non-performing loans and procedures of liquidations needs had to be drastically improved, with the government contributing to this important work** with an improved regulatory, legal and judiciary environment. The legal framework should be adjusted so that to enable banks to facilitate the settlement of borrower arrears using standardized protocols. Regulations were also to be amended to improve the liquidation process of resolved banks.

And as soon as the first recapitalization of the Greek banks had finished, new preparatory work started for a new stress test for the Greek banks, which was set to be conducted in H2 2013 and to be completed by end-2013. The BoG, in consultation with the Troika, drafted a new reference framework methodology for the diagnostic analysis of Greek banks' asset quality, including an asset quality review (AQR) and credit loss projections over a 3-year and a life-time horizon. In addition, the 2013 exercise would include an assessment of banks' policies and procedures to deal with troubled assets and loan loss provisioning. For this, the BoG hired again BlackRock, with a view to establishing the Terms of Reference (ToR).

This new diagnostic analysis of Greek banks' asset quality and possible additional capital needs was dully conducted in August-November 2013 and in December 2013 the Black Rock submitted its final report containing the results of the new stress test exercise applied on Greek banks and a detailed description of the methodology used. However, the Bank of Greece (BoG) was able to publish its own calculations concerning the additional capital needs of the banks, after extensive discussions with Troika, only in Match 2014. In fact, the BoG, utilizing the Credit Loss Projections (CLP) estimated by Black Rock, also applied additional prudential filters in order to arrive to its own estimate of CLP, which was usually much higher than Blackrock's CLP. For example for Alpha Bank Blackrock had estimated that according to its 2013 diagnostic analysis, its 3.5 years CLP was € 6.96 billion and its Lifetime CLP was € 11.57 billion. Instead of these projections of Blackrock 2013, the BoG chose to use the Lifetime CLP that was estimated (for Alpha Bank + Emporiki Bank) from the adverse scenario of Blackrock's 2011 diagnostic analysis. This gave an estimated CLP for Alpha Bank Greece of € 14.72 billion, which was by € 3.2 billion higher the Blackrock's 2013 lifetime CLP. The evolution of balance sheet and P&L items (e.g. pre-provisioning profitability) was based on a conservative adjustment of banks' restructuring plans under the baseline and the adverse scenario by the BoG supported by international consultants – Rothschild and Ernst&Young. And with these calculations the additional capital needs of Alpha Bank were calculated to the level of € 0.26 billion. Overall, for the four systemic banks, plus the Attica Bank plus Panellinia Bank, the additional capital needs under the baseline scenario were estimated at € 6.38 billion, while under the adverse scenario these capital needs would reach the level of € 9.4 billion.

According to the EC, in line with the approach taken in the upcoming ECB/SSM Comprehensive Assessment, the above capital needs of the Greek banks, which were determined according to the base line scenario were binding and had to be covered in a nearer term. The banks could use for this purpose also mitigating actions

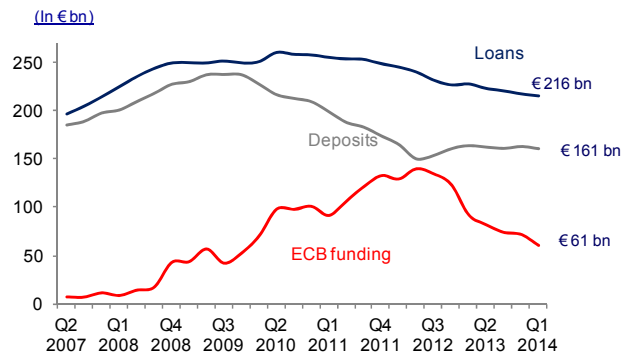
(e.g. divestments). Such actions that were already included as a commitment in the restructuring plan of each bank were taken into account in the capital needs estimation analyzed above. Additional mitigating actions not yet included in the restructuring plans could be used by banks in their capital raising plans to offset part of their capital needs. **The capital needs under the baseline scenario were to be primarily covered by capital raisings from the private sector and to a lesser extent by banks' supplementary mitigating actions.** The additional mitigating actions could include the potential sale of assets such as foreign and domestic subsidiaries and other possible measures included in their restructuring plans. The BoG asked banks to submit by mid-April 2014, their capital raising plans to address the additional capital needs under the Baseline Scenario. Moreover, banks had until end-May 2014 the obligation to submit capital-raising plans addressing the capital needs arising by the Adverse Scenario.

In response to the above, Alpha Bank and Piraeus Bank proceeded immediately to launch very successful share capital increases in March 2014, amounting to € 1.2 billion and € 1.75 billion respectively, which were not only covered but also substantially oversubscribed by a multitude of international investors. These capital increases were enough to cover not only the capital needs arising from the baseline and the adverse scenario of the end 2013 BoG diagnostic analysis, but also enough to cover the buy back from the Greek state of their preference shares, amounting to € 940 million and € 750 million respectively. Moreover, these capital increases were fully funded through international private investment and constituted a significant step toward returning the two banks to the private sector. Following these share capital increases the percentage of HFSF in the share capital of Alpha Bank was reduced to 66.9% and its percentage in the share capital of Piraeus Bank was reduced to 67,3%. It should be noted that this HFSF participation in the two banks is now fully covered by the warrants in the hands of private investors, which can be exercised in specified dates in order to buy the shares that are still owned by the EFSF. On the back of these successful transactions, the two remaining systemic banks proceeded also with substantial share capital increases, with the consent of HFSF and following the adoption by Parliament of the amended recapitalisation framework. Therefore, by March-April 2013, the four Greek systemic banks had managed to raise an amount of € 8.4 billion of share capital, covering almost the total amount of their capital needs even under the adverse scenario, which has been conservatively estimated. These developments imply that almost the total of the € 11 billion of reserves maintained by HFSF, which have already been recorded in the Greek GG debt, will not be used for the recapitalization of the Greek banks and sooner or later are going to be recorded as a reduction of the Greek GG debt.

In addition to the above, and following the successful return of the Greek state to the bonds market through the issue of 5-year GGBs at relatively low cost, the Greek banks (and also Greek businesses) have also regained beneficial access to the bonds markets. Moreover, the issuance of government treasury bills are now been subscribed by many foreign banks as well freeing financial resources to the Greek banks.

All these have contributed to a substantial decrease of the reliance of the Greek banks on the Eurosystem funding mechanism (ECB borrowing and Emergency Liquidity Assistance–ELA). In particular, in Q1 2014 the funding of the Greek banks through ECB and ELA fell i to € 57.8 bn and € 2.88 bn respectively, from its peak level of € 30.26 bn and € 100.64 bn respectively in Q2 2012. The most recent successful resource to international debt and equity capital markets will further improve the liquidity position of Greek banks, helping them to return in positive rates of bank lending expansion, in combination with the further reduce their reliance on central bank funding.

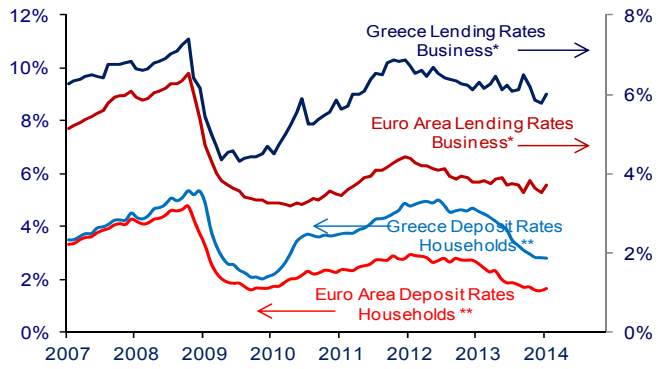
Funding Gap



Finally, the normalization of operation of the Greek banking system is also supported by the following developments: a) The successful resolution of three non-viable co-operative financial institutions, with the transfer of their deposits to one of the core banks and the coverage of the corresponding funding gap (of around EUR 430 million) by the HFSF. b) The utilization of the report of Blackrock on the management of troubled assets (TAR) burdening the balance sheets of the Greek Banks in order to make a brake through in the management of their non-performing loan (NPL) portfolios. The regulatory, legal and judicial environment has been adjusted with the purpose to support banks' NPL management. c) **Further amendments to the household insolvency framework were adopted in the second half of 2013 and the moratoria on auctions expired in December 2013.** With the Law 4224/31.12.2013, a temporary scheme regarding auctions of debtors' primary residence was introduced in order to protect the low income households. The temporary scheme, which will be in operation until end-December 2014, is targeted at the debtors who fulfil certain specific criteria related to the income and the property value and obliges debtors falling within this temporary scheme to pay 10-20% of their net monthly income to service their debt. The new temporary arrangement was introduced following the expiration of the moratorium on the auction of the debtors' primary residence on December 2013. This was one of major impediments for improving the payment culture among Greek citizens. d) **A road map to deal with the outstanding private debt and ensure a smooth transition to a permanent debt resolution mechanism is going to be followed in 2014. A** Government Council for the Management of Private Debt was established by an Act of the Council of Ministers to oversee and foster

the process for the establishment of a debt resolution (of non-performing debt) mechanism.

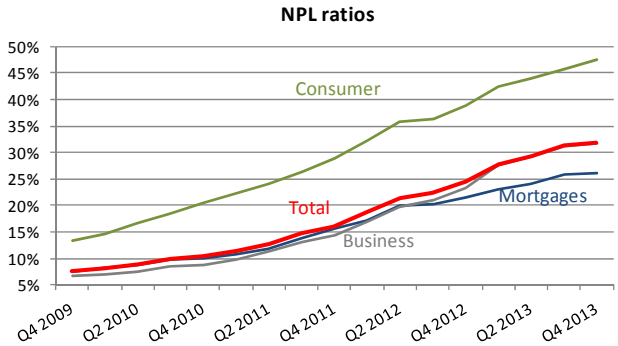
Credit Expansion – Deposit Growth (yoy % change)



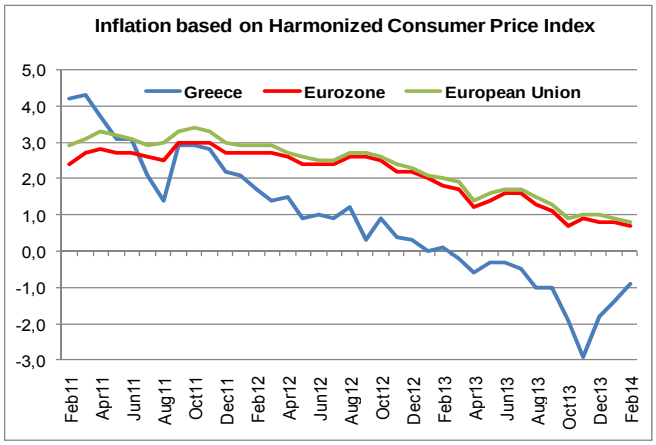
Financial conditions in Greek banking system have entered a gradual normalization course, as investors are no longer concerned about the long term sustainability of the Greek banks. Investors are now envisaging a healthy Greek banking system, which is fast exiting the stage in which their viability depended on abnormally high support by the ECB and the BoG. The banks still face the consequences of the recession, as indicated by the surge in non-performing loans (NPL), as analysed below to Box1, and the decreasing lending ratios. The bank credit expansion to the private sector remained negative at -3.9% in the end of 2013, on top of a -4.0% fall in 2012 and -3.1% in 2011. Loans amounted to €217.5 bn in the end of 2013, while in 2014 it is projected to increase only gradually, to €220 bn, as tightening conditions in the banking sector continue to unwind. The annual pace of contraction in business lending accelerated form -4.4% in 2012 to -4.9% in 2013, while the declining pace of contraction in the households has been diminished (2013: -3.5%, 2012:-3.8%). And although interest rates for firms and households are on a downward trend, they still remain at elevated levels relative to the Euro Area.

Deposits from households and businesses remained stagnant in the period between April 2013 and February 2014, but appear to have entered again an upward trend from March 2014. Overall, their level is around the € 161 billion in March 2014, from € 160.5 billion in Feb.2014 and from their historical low level of €150.6 bn in June 2012. As the economic sentiment improves further, deposits is expected to continue to return to the fully capitalized Greek banking system.

Non-performing loans (NPL) trends and prospects: The NPL ratio rose to 31.7% in Q4 2013, from 24.5% in Q4 2012 and 10.4% in Q4 2010. The NPL ratio for consumer lending increased to 47.6% in Q4 2013, from 36.3% in Q4 2012, while NPL from businesses marginally increased to 31.6% in Q4 2013, from 31.2% in Q3 2013 and 23.4% in Q4 2012. However, the rate on new NPL formation on a quarterly basis has decelerated, with the NPL ratio increasing by only 0.5 bps in Q4 2013 as compared to 1.9 bps in Q3 2013 and 2.0 bps in Q4 2012. It is expected that NPL ratio will peak towards the end of this year to 33.0% and gradually decline in the following quarters expected to fall to 31.3% in Q4 2015. However, the NPL ratio may fall faster, on the back of ongoing legislative improvements, which could enable banks to better target strategic defaulters and enhance their ability for effective decision making concerning either loan restructuring and/or improved collection techniques.



Regarding the loan restructuring strategies, the Greek banks intensively aim to the adoption of tailor-made strategies and improved collection techniques in order to positively affect their delinquent loan volumes. Concerning the establishment of more permanent debt resolution mechanisms, creditworthiness is necessary to be commonly defined, as a key stage of the restructuring assessment process.



INFLATION: CPI Inflation was negative at -1.35% in April 2014, as in March 2014, from -1.5% in Jan.2014,-1.7% in Dec.2013, -2.9% in Nov.2013, -2.0% in Oct.2013 and +0.8% in Jan.2013. Average CPI inflation is fell to -0.9% in 2013 from 1.5% in 2012, 3.4% in 2011 and 4.7% in 2010. Therefore, Greece has now the lower inflation in the EU-27, while it is true that inflation in the country remained elevated until December 2012. This evolution of inflation until 2012 was mainly due to the fact that fiscal adjustment in Greece initially took the form of raising VAT and excise taxes, as well as through tariff hikes by deficit-ridden public sector entities. Overall, inflation is expected to remain negative even in 2014, with average inflation maintained at -1.0% in the current year, with positive inflation of the order of 0.5% expected for 2015.

Harmonized inflation was -1.5% in March 2014, from -1.4% in Jan.2014, -1.8% in Dec.2013, -2.9% in Nov.2013, -1.9% in Oct.2013 and the average harmonized inflation was -0.9% in 2013. ***Core inflation*** was -1.3% in Apr.2014, from -1.4% in Jan.2014, -1.8% in Dec.2013, -2.9% in Nov.2013, -1.8% in Oct.2013 and -1.2% in Jan.2013.

BALANCE OF PAYMENTS: The ***capital account balance (CAB)*** recorded a surplus of 0.23% of GDP in Q1 2014, versus a deficit of -0.63% in Q1 2013. In fact, this was the first time in the post WW2 that a surplus was recorded in Q1 of any year. It followed the year 2013, where the CAB was in

surplus of the order of 1.33% of GDP again for the first time in many decades. Specifically ***in Q1 2014 the following developments were recorded in the Greek BoP:***

Greek Balance of Payments (€ billions)		
	Jan-Mar 2014	Jan-Mar 2013
Trade Balance (TB)	-4.56	-4.52
Exports	5.45	5.45
Imports	10.00	9.97
Services Balance	1.94	1.48
Tourism Receipts	0.49	0.40
Shipping Receipts	3.13	2.88
Income Balance	-0.64	-0.88
Payment of Interest, Divid. & Profits	1.43	1.65
Transfers' Balance	3.67	2.78
Current Account (CA)	0.41	-1.15
CA (% of GDP)	0.23	-0.63
Capital Account	-0.18	0.35
Source: Bank of Greece		

The ***trade balance*** showed a slightly higher deficit of € 4.56 billion, from € 4.52 billion in Q1 2013, mainly due to a significant increase in imports of ships by € 188.6 million and a corresponding increase of the deficit of the ships balance by € 212.4 million, or by 70.8%. On the other hand, the falling trend of imports excluding oil and ships decelerated to -1.7% in Q1 2014, from -5.6% in Q1 2013 and also there was a small fall of exports excluding ships and oil by -0.7% in Q1 2014, compared with an increase by 4.1% in Q1 2013. On the other hand, the trade deficit excluding oil and ships decreased to € 1.86 billion in Q1 2014, from € 1.92 billion in Q1 2013, a decrease of -3.3 % yoy. Oil imports also registered a small fall by -1.5% (due mainly to the fall of consumption of heating oil), following their fall by -8.5% in Q1 2013. By contrast, revenues from oil exports rose by 2.6% in Q1 2014, on top of their increase by 30.6% in Q1 2013.

The ***services account surplus*** increased noticeably by 31.4% in Q1 2014, following its fall by -2.9% in the first quarter of 2013. The total receipts from services exports rose by 11.8%, versus a fall by -12.1% in the first quarter of 2013. Also, payments for services imports increased only by 1.0%, compared with a fall of -16.5% in the first quarter of 2013. In more detail:

More specifically, receipts from external tourism (including revenues from cruises) rose by 21.7% in Q1 2014, after their reduction by -2.6% in Q1 2013. At the same time, shipping receipts increased by 8.4% in Q1 2014, compared with their substantial fall by -14.4% in Q1 2013. Moreover, even revenues from other services increased remarkably by 18.8%, after their fall by -8.1% in the first quarter of 2013. At the same time, payments for other services were also higher by 5.4% after their reduction by -20.9% last year.

Regarding the ***income balance***, payments for interest, dividends and profits abroad fell by -13.4% in Q1 2014, after their significant reduction by -28.3% in Q1 2013, while receipts from investment income increased by 3.1%.

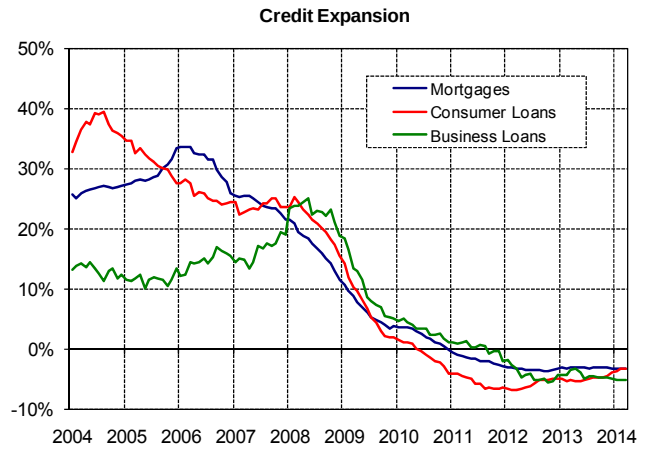
The ***current transfers*** showed a surplus of € 2.21 billion, compared with a surplus of € 1.69 billion in Q1 2013. The remittances inflows declined by -23.0%, after their significant rise by 46.3% in Q1 2013. Additionally, remittances payments fell by -9.6%, compared to a fall by -47.8% in the first quarter of 2013. Transfers from EU-28 amounted to € 2.87 billion from € 2.38 billion in the first quarter of 2013. Respectively, payments to EU-28 amounted to € 816.0 million, compared to € 917.9 last year. The ***capital transfers balance*** was positively impacted by higher capital inflows from the EU Structural Funds (+29.6%), which contributed to the creation of a significant surplus.

The capital account recorded a small deficit of € 180.3 million, compared to a € 353.9 million surplus in the first quarter of 2013. In detail:

As regards foreign direct investment a net inflow of € 93.4, million was recorded, versus an outflow of € 29.6 million in the first quarter of 2013. In particular, direct investment by non-residents in Greece showed a net inflow of € 288.3 million, while domestic firms showed a net outflow of € 194.9 million. According to the Bulletin of the Bank of Greece, the most important transaction was the inflow of € 200 million due to the involvement of the parent company Crystal Almond (Luxembourg) in the capital increase of its subsidiary Wind Hellas. Direct investment abroad by residents showed an increase (outflow) of € 36 million without any remarkable transaction. The inflow of FDI from abroad will be larger after March 2014, due to significant capital inflows from foreign investors for investment in domestic banks.

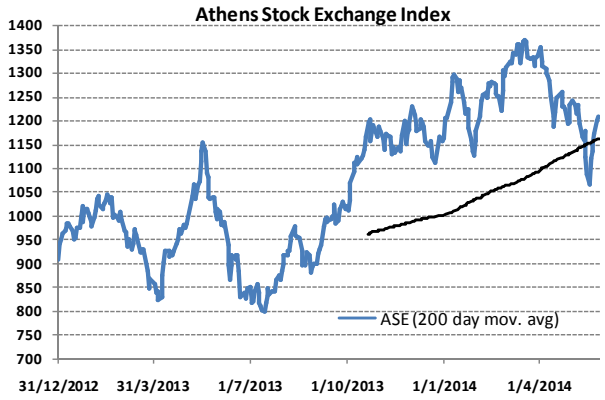
Under portfolio investment a net inflow of € 309.9 million was recorded, compared to a net inflow of € 2.47 billion in the first quarter of 2013, mainly on account of a rise in non-residents' purchases of shares of Greek firms and a decline in residents' investment in foreign bonds and Treasury bills. These developments were partly offset by a drop in non-residents' holdings of Greek government bonds and Treasury bills (outflow).

Under other investment, a net outflow of € 583.6 million was recorded, mainly due to non-residents' decreased holdings of Greek deposits and repos.



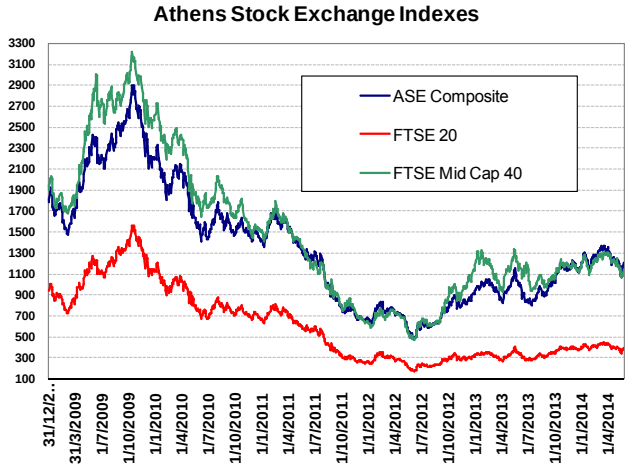
MONEY & FINANCIAL MARKETS: Credit expansion to businesses and households fell by -3.7% at end-April 2014 from -4.1% at end-March 2014, -4.0% at end-February 2014 and -3.4% at end-April 2013. In particular, the annual rate of change of mortgage and consumer lending fell to -3.3% and -2.9% respectively at end-April 2014 from -3.2% and -5.4% respectively at end-April 2013. Moreover, lending growth to businesses decreased to -4.8% at end-April 2014 from -5.3% at end-March

2014, -5.2% at end-February 2014 and -3.3% at end-April 2013.



The Stock Market: So far in 2014 (end of Apr.2014), the ASE general index outperformed most global indexes as it happened during 2013 as well. The performance of ASE can be explained by the return of investment confidence in the prospects of recovery and growth of the Greek economy, which is also reflected to the gradual access by both the State and other Greek companies like banks and major enterprises to the world markets for the first time since 2010. In a rapidly falling Greek interest rate environment, Greek banks managed to raise their capital base by € 8.3 billion and also improved their liquidity by raising €1.75 billion via successful bond issuance. The same path, follow other major Greek enterprises. According to analysts consensus cited in Bloomberg, the 12-month horizon of the ASE general index will be higher compared to current levels.

The main ASE composite index was up by 28.1% yoy (as of 31.12.2013) on a yoy basis (FTSE-20 stocks: +24.3%, FTSE-40 mid-cap: 16.9%), from an increase of 33.4% at end-2012 (FTSE-20 stocks: 3.0%, FTSE-40 mid-cap: -77.2%). Following these developments, at end-December 2013 49.6% of the total stock exchange value of listed firms was in the hands of foreign investors, up from 50.1% at end-December 2012.



9. Economic Data – Greece

(% change unless otherwise noted)

Yearly Data	2008	2009	2010	2011	2012	2013	2014*
Real GDP Growth	-0.2	-3.1	-4.9	-7.1	7.0	-3.9	1.0
Gross Fixed Capital Formation	-14.3	-13.7	-15.0	-19.6	-19.2	-12.8	7.4
- Equipment	-4.7	-18.0	-8.4	-18.0	-17.1	-7.2	7.1
- Residential	-33.6	-20.7	-21.6	-18.0	-32.9	-37.8	1.0
Unemployment (percent)	7.6	9.5	12.5	17.7	24.2	27.3	26.8
Employment	1.2	-0.6	-2.6	-5.6	-8.3	-3.7	0.6
Consumer Price Index (year average)	4.2	1.2	4.7	3.3	1.5	-0.9	-1.1
Unit Labor Costs	4.9	5.2	-0.1	-1.8	-6.2	-7.8	-1.5
Credit Expansion (Private Sector)	15.9	4.1	0.0	-3.1	-4.0	-3.9	0.8
Government Deficit (as % of GDP)	-9.8	-15.7	-10.7	-9.5	-6.1	-2.0	-2.0
Current Account (as % of GDP)	-13.3	-10.1	-9.2	-8.6	-1.2	1.3	0.5

Source: Hellenic Statisticsl Authority (ELSTAT.)

* Projections of Department of Economic Analysis, Alpha Bank

Quarterly Data	2012	2013				2013	2014
	year	Q1	Q2	Q3	Q4	year	available period
Economic Activity (average)							
Retail Sales Volume	-11.8	-12.4	-8.8	-9.8	-2.9	-8.4	-2.9 (Jan-Feb)
Construction Activity	-30.6	-43.5	-30.7	-21.9	4.2	-26.6	-41.1 (Jan)
Industrial Production (Manufacturing)	-4.2	-1.0	1.4	-3.8	-3.9	-2.0	0.9 (Jan-Mar)
PMI (manufacturing)	41.2	42.3	45.2	47.7	48.7	46.0	51.1 (Apr)
Economic Sentiment Indicator	80.3	86.9	92.2	91.3	91.1	90.8	95.4 (Apr)
Index of Business Expectations in Manufacturing	77.2	85.0	90.6	90.1	85.4	87.8	91.9 (Apr)
Consumer Sentiment Index	-75.0	-72.0	-67.0	-73.0	-65.0	-69.3	-55.0 (Apr)
Credit Expansion (end of period)							
Private Sector	-4.0	-3.5	-4.1	-3.9	-3.9	-3.9	-3.7 (Apr)
Consumer Credit	-5.1	-5.3	-5.2	-4.8	-3.9	-3.9	-2.9 (Apr)
Housing	-3.4	-3.2	-3.2	-3.2	-3.3	-3.3	-3.3 (Apr)
Business	-2.1	0.7	-1.1	-1.9	-2.8	-2.8	-4.8 (Apr)
Tourism	1.1	0.2	-0.7	-1.5	-2.6	-2.6	-1.7 (Apr)
Prices (end of period)							
Consumer Price Index	1.5	0.0	-0.5	-1.0	-2.2	-0.9	-1.3 (Apr)
Core Inflation	0.3	-1.3	-1.5	-2.0	-2.1	-1.7	-1.3 (Apr)
Interest Rates (end of period)							
Savings	0.42	0.42	0.39	0.37	0.33	0.31	0.28 (Mar)
Short-term Business Loans	7.61	7.46	7.41	7.29	9.24	7.24	7.18 (Mar)
Consumer Loans (with charges)	11.16	10.45	9.78	10.83	10.87	10.77	10.72 (Mar)
Housing Loans (with charges)	3.60	3.23	3.07	2.99	2.99	3.03	2.94 (Mar)
10 year Bond Yield	22.50	11.14	10.24	10.23	8.60	10.05	6.67 (Mar)
National Accounts							
Real GDP	-7.0	-6.0	-4.0	-3.2	-2.3	-3.9	-1.1 (Q1)
Final Consumption	-8.9	-8.9	-6.4	-6.1	-0.8	-5.6	…
Investment	-19.2	-11.4	-11.5	-12.9	-15.3	-12.8	…
Exports of goods & services	-1.7	-2.2	1.6	5.2	0.5	1.8	…
Imports of Goods & services	-13.8	-7.0	-11.1	2.7	-5.6	-5.3	…
Balance of Payments (in € bn - Cumulative)							
Exports of Goods	22.0	5.4	11.1	16.8	22.5	22.5	5.4 (Jan-Mar)
Imports of Goods	41.6	10.0	19.3	29.7	39.8	39.8	10.0 (Jan-Mar)
Trade Balance	-19.6	-4.5	-8.3	-12.9	-17.2	-17.2	-4.6 (Jan-Mar)
Invisibles Balance	16.3	3.3	6.5	18.2	19.5	19.5	5.0 (Jan-Mar)
Invisibles Balance / Trade Account	83.4	72.3	78.5	141.4	113.3	113.3	109.0 (Jan-Mar)
Current Account	-3.3	-1.3	-1.8	5.3	2.3	2.3	0.4 (Jan-Mar)
Direct Investments	2.30	1.3	1.1	0.9	2.4	2.4	0.1 (Jan-Mar)
Portfolio Investments	-99.1	0.5	-9.8	-7.5	-6.6	-6.6	0.3(Jan-Mar)
Athens Stock Exchange (end of period)							
Composite Index	908.0	869.2	847.6	1,014.1	1,162.7	1,162.7	1,232.1 (Apr)
% change	33.4	19.2	38.7	37.2	28.1	28.1	53.7 (Apr)
Market Capitalization ASE (% of GDP)	17.7	14.8	29.3	31.6	39.6	39.6	39.0 (Apr)

Source: Hellenic Statisticsl Authority (ELSTAT.), Bank of Greece