

**REPORT TO CONGRESS ON  
THE INTERNATIONAL MONETARY FUND'S  
LOAN TO GREECE**



A Report to Congress

*consistent with*

Section 1501 of the  
Dodd-Frank Wall Street Reform and Consumer Protection Act, 2010

United States Department of the Treasury  
April 2012

## ***Introduction***

This report has been prepared consistent with section 1501 of the *Dodd-Frank Wall Street Reform and Consumer Protection Act, 2010*.<sup>1</sup> As required, the report provides an assessment of the likelihood that the recently-approved International Monetary Fund (IMF or Fund) loan made to Greece will be repaid in full, including Greece's debt status, vulnerabilities, and debt management strategy.

As directed by section 1501, and consistent with its longstanding practice with respect to all loans, the Office of the United States Executive Director (USED) at the IMF, in close coordination with the Treasury Department, conducted a careful and thorough evaluation of the proposal for the Greece program submitted to the IMF Executive Board given that Greece's debt-to-GDP ratio exceeded 100 percent and Greece is not eligible for assistance from the International Development Association.

The IMF program to support Greece has been carefully crafted to mitigate risks to the IMF and help ensure that the Fund is repaid in full. Greece faces significant challenges in the coming years in implementing economic reforms, and achieving sustainability. In order to merit the IMF's support, Greece was required to undertake a bold program of fiscal consolidation, legislated further adjustment measures and completed a large debt restructuring. The IMF's support will be disbursed only as Greece meets carefully designed reform targets on a quarterly basis. The financing for Greece's adjustment program is coming predominantly from Europe, and the European repayment schedule has a 25-year repayment schedule while the IMF will be repaid over 10 years. Europe has also provided assurances that it stands ready to finance the Greek government after the program is over until market access is restored. The IMF is regarded worldwide as having preferred creditor status, meaning that it is repaid first amongst all creditors, and Greece and Europe have reaffirmed the Fund's status as a preferred creditor in moving forward with the Greek program. In view of this, the Treasury Department and the USED assessed that the loan is likely to be repaid in full. As such, the Treasury Department instructed the USED to vote in favor of the program.

## ***Program Description***

On March 15, 2012, the IMF Executive Board approved a \$36.7 billion Extended Fund Facility (EFF) for Greece. Greece's economic reform program is a critical part of a broader European effort to promote EU and global financial stability – fiscal governance reforms, ECB actions, fiscal and structural reforms in Spain and Italy, and creating an effective financial firewall. Europe's stability is critical for avoiding global financial contagion and safeguarding the U.S. economic recovery. Given the IMF's wealth of experience designing credible economic adjustment programs, its engagement alongside the European Union to help restore macroeconomic and financial stability is very much in the best interests of the United States.

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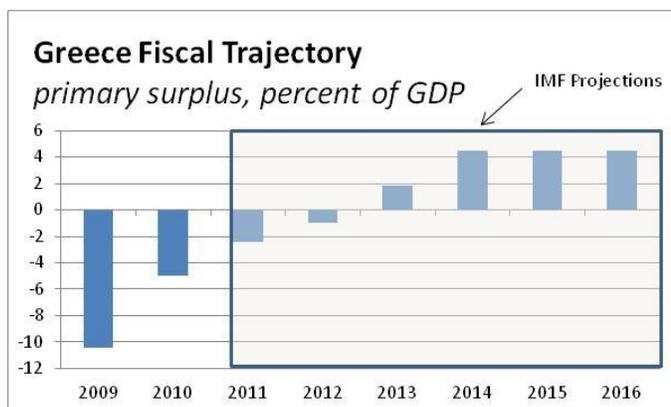
<sup>1</sup>P.L. 111-203; codified at 22 U.S.C. 286tt(b), section 68(b) of the Bretton Woods Agreements Act: "Within 30 days after the Board of Executive Directors of the Fund approves a proposal [to make a loan to a country whose public debt exceeds gross domestic product and is not eligible for assistance from the International Development Association] the Secretary of the Treasury shall report in writing . . . assessing the likelihood that loans made pursuant to such proposals will be repaid in full . . . ."

Greece's IMF program contains extensive features to mitigate risks to the IMF. Under the new program, if all disbursements were to be made as scheduled, the IMF's peak exposure to Greece would be only \$2.9 billion more than under the previous program, at current exchange rates. In addition, IMF disbursements will be evenly phased over the program horizon while the European disbursements will be made primarily at the beginning of the program, in part due to the upfront costs associated with Greece's debt restructuring. This approach for IMF disbursements links Fund exposure with performance on the program's conditions.

The IMF program requires significant policy and reform measures. The Greek government's primary surplus is projected to reach and be maintained at 4.5 percent of GDP over the medium term. The Greek authorities have committed to implementing structural reforms aimed at improving public financial management—reforming social transfers while strengthening the core safety net to protect the most vulnerable, together with tax administration and enforcement reforms. The program also includes a range of measures to enhance growth potential and job creation. The authorities will undertake significant labor market reforms to make collective bargaining more conducive to labor market flexibility, reduce the minimum wage, and lower nonwage labor costs. Measures to liberalize services also will help improve competitiveness.

Euro area member states have committed to contribute \$190.8 billion to the overall financing package through end-2014, and have committed to provide adequate support to Greece for as long as it takes for Greece to regain market access, provided that Greece fully complies with the requirements and objectives of the program. In addition, maturities for the new financing from the Euro area will be 25 years, with a 10-year grace period, compared to 7.5 years under previous loans made from the European Financial Stability Facility (EFSF) and 10 years maturity under the EFF. Euro Area member states also agreed to an additional retroactive lowering of the interest rates of the Greek Loan Facility from the previous program, which is expected to lower Greece's debt to GDP by 2.8 percentage points by 2020. Euro Area Central Banks that hold Greek government bonds in their investment portfolios did not participate in the debt exchange but committed to pass on to Greece any future income stemming from the difference in their purchase price and par value over the next 10 years. This is expected to lower the debt ratio by a further 1.8 percentage points of GDP by 2020. Europe is also providing significant technical assistance to Greece through a European Union Greek Task Force of experts to help Greece design and implement specific measures on the ground.

The Greek government has made progress in addressing its fiscal imbalances. Based on policies already implemented, the 10.4 percent primary deficit in 2009 was brought down to a primary deficit of 2.4 percent of GDP in 2011. Assuming continued policy implementation, a primary surplus of 1.8 percent of GDP would be achieved in 2013 and future primary surpluses are expected to average about 4.5 percent of GDP over the medium-term. These impressive adjustment and reform efforts, while necessary, would not have returned Greece to a sustainable debt path on their own, given the



large debt overhang. For this reason, the Greek government has undertaken a significant debt restructuring with its private creditors. The IMF expects that, through these combined initiatives, Greece can reduce its debt-to-GDP ratio from 165.3 percent of GDP at end-2010 to roughly 116.5 percent of GDP by 2020.

### ***Debt Status***

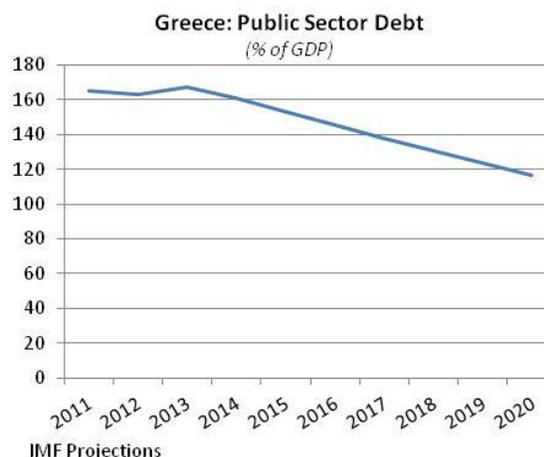
As of December 2011 (the latest date for which data are available), the Greek government's debt was \$470 billion, equivalent to 165.3 percent of 2011 GDP. Roughly 80 percent of this debt (\$373 billion) was owed to private creditors. The private debt restructuring, completed in Spring 2012, will improve debt dynamics. In addition, as the recovery takes hold, Greece's debt position should continue to improve as revenues are bolstered, banking sector health is restored and GDP growth directly contributes to a lower debt to GDP ratio.

#### **Greece Public Sector Debt**

	2011		2012*	
	\$ bns	% total	\$ bns	% total
Total	470.9	100.0	439.9	100
Private	373.2	79.3	184.5	41.9
Official	97.7	20.7	255.4	58.1
o/w IMF	27.4	5.8	36.0	8.2
o/w EU	70.3	14.9	219.3	49.8

\* IMF Projection

Greece's debt exchange attracted high participation. Bondholders were invited to exchange their bonds for new bonds with a face value equal to 31.5 percent of the original amount and short-term EFSF notes worth 15 percent of the original amount. Interest on the new bonds will be paid annually and principal payments will be made in equal installments over 20 years after a 10-year grace period. Of the \$234 billion in eligible Greek-law bonds, 85.8 percent participated, and the authorities decided to activate collective action procedures, pulling in remaining hold outs. Greece's \$24 billion in bonds issued under foreign law require a separate consultation process and the debt exchange for these holders should settle by end-April. Overall, approximately \$258 billion in debt was subject to the exchange, and debt owed to the private sector was halved according to estimates.



Debt owed to the official sector is projected to increase substantially between 2011 and 2012 with the approval of the EU/IMF program. The bulk of the increase (\$149 billion of the \$158 billion increase) will be owed to other EU member states, which are effectively financing the upfront costs of the debt exchange including by providing the EFSF notes to be used in the exchange and helping to recapitalize Greek banks which suffered losses on their holdings of Greek government debt.

## ***Debt Management Strategy***

Looking forward, the Greek government's primary objective is to place its public debt on a downward trajectory, aimed at achieving a debt-to-GDP ratio of less than 120 percent by 2020. To meet this objective, in addition to the private debt exchange, the government is undertaking fiscal consolidation aimed at achieving and maintaining a primary surplus by 2013 that reduces the need for additional debt and allows for a reduction in outstanding debt. In addition, the Greek government has committed to undertaking significant privatizations that are projected to raise \$60 billion by 2020. The authorities are aiming to regain medium and long-term market access in the period after the program. Initial debt offerings are expected to be at shorter maturities and in low volumes to establish a track record, and then should gradually increase in both volume and maturity.

## ***Vulnerabilities***

The Greek authorities have put together an ambitious package of reforms to regain growth and competitiveness that will take time to implement and bear fruit. There are significant headwinds to improving economic growth in the near term, including fiscal consolidation, the need to regain competitiveness through wage restraint and price reductions, and deleveraging in the financial sector. Protracted economic stagnation could hinder fiscal consolidation efforts and put additional pressure on the banking sector and represents a key vulnerability.

Another challenge is to sustain political and public support for the fiscal austerity adjustment throughout the program. To mitigate this risk, the EU and IMF required significant prior actions, approval of the program by the Greek parliament and written commitments from Greece's major political party leaders that they will implement the agreement regardless of the outcome of future elections. Risks also exist on the structural reform agenda, where the government must demonstrate strong political will in implementing reforms opposed by many interest groups.

Timely program implementation is critical in putting public debt on a downward trajectory. Implementation risks are highest in the area of tax revenue generation, where structural weaknesses in compliance, collection, and overall administration have prevailed. Structural measures and technical assistance under the IMF program aim to mitigate capacity constraints and enhance program implementation.

## ***Overall Assessment***

Greece is heavily indebted and vulnerable. However, its EU/IMF-supported economic reform program, combined with the restructuring of private sector debt, provides the best opportunity for the country to return to a sustainable debt path and lower its vulnerabilities. The IMF program was carefully designed to address the significant vulnerabilities facing Greece, limit the IMF's own exposure and link it clearly to Greece's performance, and to enhance the likelihood of the IMF being repaid.

IMF resources will be safeguarded by the following:

- The government has already demonstrated a commitment to implement critical policy measures that were a precondition of IMF financing under the program, including locking in additional fiscal consolidation measures, and legislating structural reforms.
- The government has already completed a large debt exchange that sharply reduced the net present value (NPV) of its privately held debt. Without this restructuring, the government's debt would have risen to unsustainable levels.
- The IMF program includes strong conditionality and rigorous quarterly reviews. Program conditionality agreed to by the government focuses on the following areas: fiscal consolidation aimed at achieving debt sustainability over the medium-term; strengthening public financial management; reforming the social transfer system and improving its effectiveness, and enhancing the stability of the financial sector.
- The IMF's lending to Greece is set to be repaid over a much shorter time horizon (4.5-10 years) than that of the European contributions (25 years with a 10-year grace period) and the restructured privately-held Greek government bonds (30 years with a 10-year grace).
- The Eurogroup has made financing assurances to provide long-term support to Greece on adequate terms provided Greece continues to adhere to program policies.
- The IMF's preferred creditor status, ensuring that it is repaid ahead of all other creditors.

With these factors in mind, the Treasury Department assesses that the IMF's loan to Greece is likely to be repaid in full.