Restarting the Process of Privatisation in Greece

Explaining Inertia

Privatisations have been hindered by political managerial planning institutional and economic impediments. Outsiders are perplexed by the slow progress on privatisations but there are several factors acting as sand in the wheels.

First, the ideological baggage carried by the government from the time in opposition and the historically close links with public sector unions have complicated the situation continuously postponing crucial decisions on priorities. The unions are resisting privatisation mainly because privileges and opaque power sharing "understandings" are under threat. The implementation of even the mildest of privatisations has been delayed in an effort to avoid political cost and the associated risks. Furthermore, divisions among ministers are exacerbating the situation as the Ministry of Finance looks increasingly isolated and other departments negotiate with unions on their own terms. According to market sources the first act of the Privatization Secretariat, when this government took office in October 2009, was to make a list of all the declarations made when in opposition of what should not be privatized. As a result very few public corporations could be sold to the private sector and the initial privatization list was really very short indeed!

Second, the management process has been weak with the ministers preoccupied with negotiations of the stabilisation program the implementation of the fiscal measures and the quarterly review by troika. The privatisation secretariat was lacking the necessary authority and expertise to plan and carry out privatisations. They have been acting up to now as if privatisation is an academic exercise and not a deeply complex political and business process.

Third, the re-design of certain markets was delayed and as a result assets in these markets could not be privatised as persisting uncertainty was undermining market confidence.

Fourth, the country risk perceptions are undermining the effort and although valuations have been adjusted to incorporate the worse off scenario, investors were still questioning[1] the ability of the country to avoid some variation of default and are worried about the ensuing chaotic situation.

The situation calls for stronger political leadership at the highest level and improved management at the operational level. The government must raise the issue with the central trade union council (GSEE) and must send clear (with one voice) and unequivocal messages to sectoral unions that this time they will persevere in the implementation of the privatisation program.

In the public at large there is now widespread support for privatisations but some entrenched perceptions need to be addressed. The main issues are:

- The current low valuation of companies is translated in the public debate as sell out.
- The likely (?) interest of foreign investors reinforces this perception and raises issues of loss of national control over policies.

Therefore, communication is an important part of any privatisation campaign.

A Fresh Start is Required

Troika, fed up with inaction, has insisted that privatisations should be implemented through a new independent entity. The "Fund for the Exploitation of State Assets" (Fund) has been established and immediate action should be taken to strengthen its operational capabilities. The Law

[1] The European Council's decision regarding the Greek debt on the 21.07.2011 may give Greece the required breathing space to implement the medium term stabilisation program and create the right environment for privatisations.

establishing the new entity envisages that the governing board of five (already appointed) members will be assisted by an advisory board of seven (3 proposed by the troika observers). It is expected that some or all of existing experienced staff employed by the privatisation secretariat will be transferred to the new entity. There is an internal deadline for the new body to start working by the 15th of August.

I believe that further private sector involvement at the central level of implementation is also required. A Project Management Office (PMO) with adequate staff (5 long term experts and 5-7 short term experts) should be established with strong assistance from the private sector. The PMO can be assigned to a foreign investment bank or to an international consultancy or to a consortium of foreign and domestic institutions with established track record on privatisations and structural reforms through a tender. It will be responsible for coordinating privatisations and assisting the chief executive by:

- Planning the whole process with milestones and target dates.
- Assessing alternative ways of privatising public corporations especially in complex cases as in energy.
- Monitoring the work done by consultants and financial advisors.
- Coordinating the efforts of advisors and companies' management.
- Preparing briefings for political leadership.
- Proposing a communications strategy for each case.

According to the new law:

- All state assets (securities and real estate) will be transferred irrevocably to the new entity with the sole purpose of privatising them as soon as possible.
- All revenues will be credited to the budget line "Privatisation Revenues" within 10 days.
- Existing financial and other advisors for specific privatisations will continue working with the new entity.
- Real estate assets situated outside planning zones will be developed according to new improved planning terms (building ratios will range from 20% to 40%) existing spatial and planning regulations

may be amended in order to improve their development potential and building permits will be issued within 60 days of application.

- For state land surface rights and long-term leaseholds have been legally established.
- All contracts before signing will be ratified by the Audit Court and the Board will be cleared from any responsibility.

The government is now better prepared to restart the privatisation process. The legal framework is more flexible and market friendly. But the target set by the government and troika is still very ambitious. With 50 privatisations over the next 2 and half years and twice that number in land sales the new Fund will be under extreme pressure to cope with procedures.

A Lot of Open Issues Remain

There are a lot of unresolved problems and risks associated with the process. The Fund and the government have to address those concerns before they can start selling assets.

Some markets, in which public companies operate, are poorly designed and there is a lot of uncertainty regarding regulation and the government's intentions (electricity, lottery and rail markets). With lack of clarity in the regulatory environment conflicts of interest are likely to arise in certain key policy areas.

Several important assets have to be transformed in a corporate mode in order to be privatized and this transformation will determine the final commercial value of these assets. The corporatization process is going to take some time. With lack of clarity in the regulatory environment conflicts of interest are likely to arise in certain policy areas such as port and airport pricing policies.

Some privatizations involve more than one operation. For instance regional ports and airports will be sold in packages. This process may create further complications as investors will be reluctant to commit themselves in running assets that may not be on a standalone basis profitable.

In several cases the European Commission has opened inquiries for state aid purposes and this process is likely to lead to further delays of up to a year or more (TRAINOSE and ELVO)[2].

Privatization of banks is likely to be delayed by the implementation of the decisions on Greek bonds swap agreed by the European Council as new recapitalization will be required to a certain extent. (Postal Bank, Agricultural Bank).

Other assets have to be vested with permits or additional rights so that their value is augmented and that process may take more time than originally envisaged. One of these cases is OPAP with the extension of an exclusive license and the addition of electronic and fruit games put on the agenda in order to enhance its value.

Greece is a high tax economy. Taxes on property have been increased over the last two years (taxes for transfer of property, tax on large property holdings, extraordinary taxes etc) and they act as a counterincentive for undertaking investment in real estate. As the privatization program is relying heavily on real estate development a reversal on tax policies is required before starting the sale.

Large scale land development has always been a notoriously contentious and slow process. Legal challenges on environmental grounds or ownership rights have derailed the most ambitious projects even if they were protected by a tailored made law (Athens double regeneration project).

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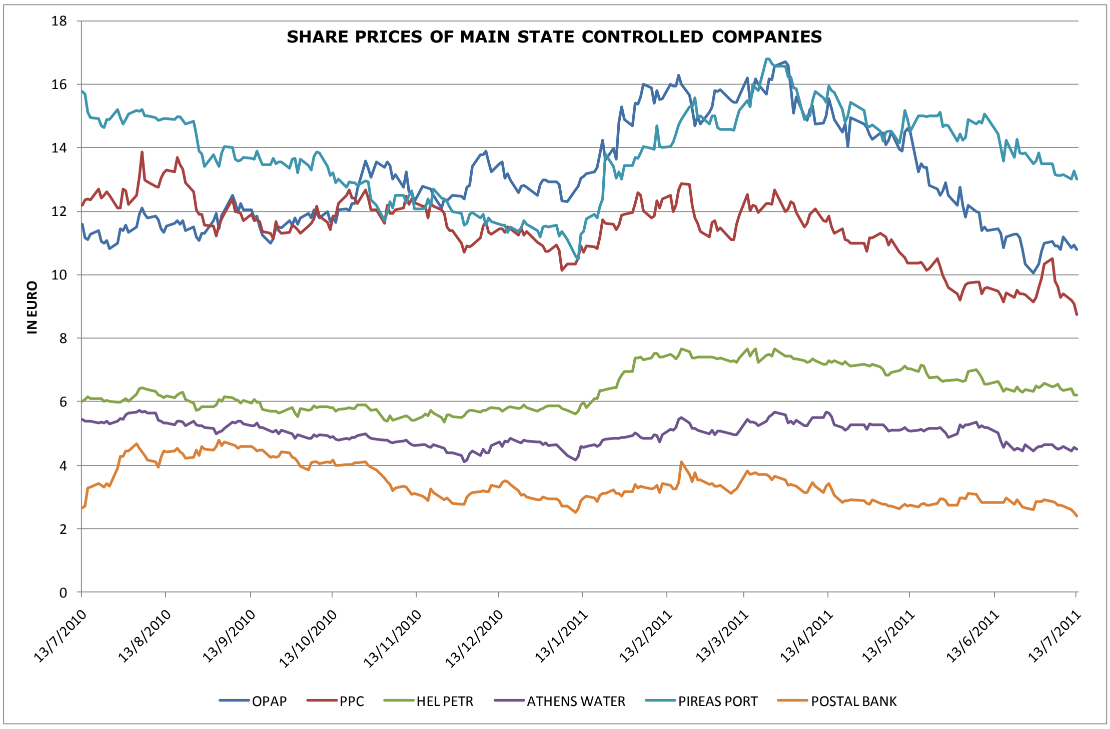
[2] The European Commission has announced on the 13th July that is opening an in-depth inquiry into the restructuring aid for the railway company TRAINOSE for state aid, questioning measures of a total value of 1.2 billion euro.

Whether the security of transaction for the foreign investors is adequately covered by the new law is an open issue. However, it can be fully addressed by following a ratification procedure for all major contracts by Parliament.

There are a number of market or company specific problems that have to be addressed before any move on privatization takes place. The financial advisors with the help of the market will identify them and suggest ways to resolve them. On top of that are horizontal problems such as real estate taxation that has to be addressed by the government as soon as possible, otherwise the sale of assets will suffer.

Opportunities do exist

A major issue is whether there is a market for Greek assets at this conjecture. I fully understand why investors may be reluctant to commit themselves in an economy which operates under a cloud of possible default, with a high possibility of social unrest and political upheaval. I believe that even in this uncertain environment there may be some real opportunities for foreign investors. I do not rule out interest from some quarters (sovereign funds, state owned companies or even private companies) for selected assets.



Share prices in listed state owned companies have performed better than the general index over the last year. Utilities lotteries and infrastructure have shown that there are crisis resistant.

Therefore I expect that privatizations in selective infrastructure projects through long term concessions, in energy raw materials and lotteries are likely to attract most interest.

Privatizations in ports and airports will take the form of long term concessions. Investors will upgrade and develop existing facilities and operate them for 20 to 25 years. For the infrastructure hubs connecting Greece with Europe demand will stabilize at a reasonable level as tourist flows will continue and even increase as the country becomes more competitive. As a consequence income will be mainly generated from abroad and not from domestic activities affected by the crisis. Greece has a long tradition in infrastructure concessions. Our main airport and maritime port as well as both main national roads the ring road of Athens and the larger bridge in the country have been built or upgraded through concessions. Private operators from abroad have successfully participated in these projects.

In energy considerable investment is required in order to modernize power generation while the Public Power Corporation will be probably forced to sell lignite power stations for competition reasons before full privatization takes place. The Gas Corporation is also up for sale to a strategic investor. Although the final structure of the energy markets has not been finalized we expect further liberalization to create the right environment for profitable investment.

In those sectors the government will look for investors with a clear business perspective, financial strength and adequate management resources.

Real estate projects will also come into the market with huge potential for commercial and tourist development. Over the next three years most state owned property will be disposed with the assistance of financial advisors and hopefully idle land will become a new source of growth.

A National Sovereign Fund for Public Land with individual specialized portfolios of large properties will be established. Several Greek and international banks will structure the real estate investment portfolios as Special Purpose Vehicles and actively promote their sale in global markets.

I believe that the market for Greek assets is likely to evolve over time. If some investors start to commit funds in major selective privatisations others will follow and reluctance may give way to real and widespread interest. Bear in mind that the international financial advisors involved in this process will play a leading role in packaging and selling these assets.

Is the Privatisation program feasible?

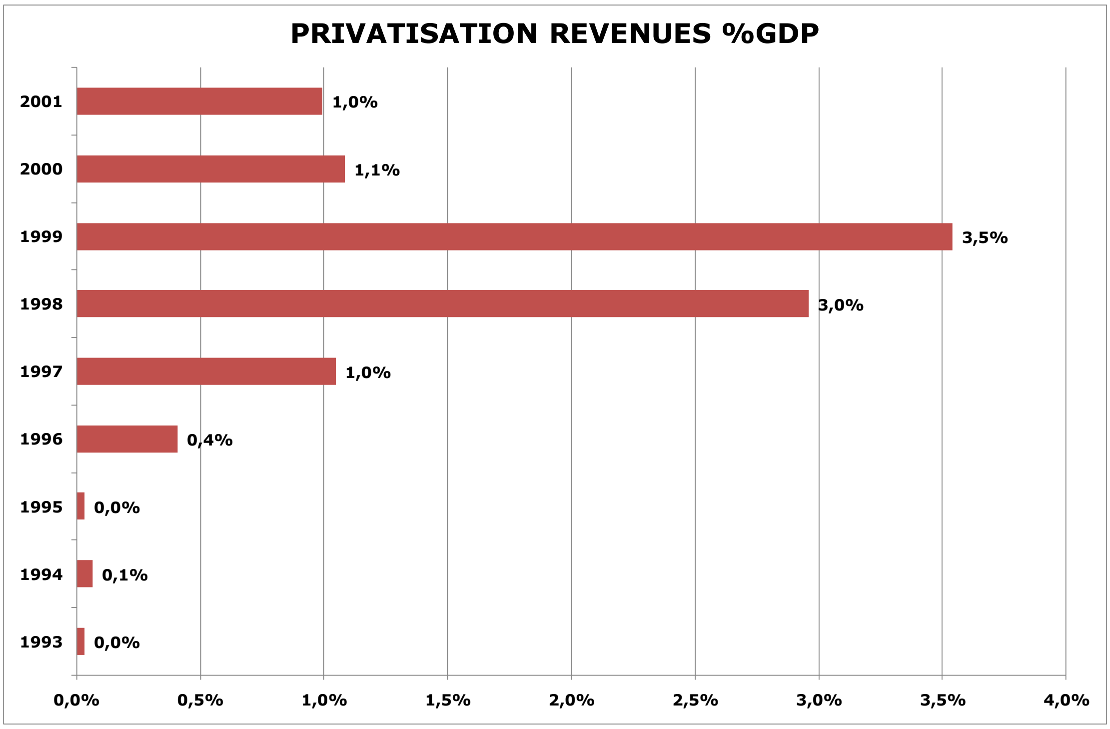
The political initiative on privatisations should be regained through the implementation of some high profile moves such as introducing a strategic investor in Public Power Corporation and the sale of OPAP. Determination in implementation will have a large demonstration effect and open the way to implement the whole program without delays. The announced privatisation timetable remains highly optimistic and with the existing legal framework and attitudes it is highly unlikely that it will be implemented without major revisions at least for 2011 (See ANNEX 1 for a complete list and ANNEX 2 for a list of public land for privatisation).

A last major question is whether this herculean task can be accomplished. I will turn to past experience for arguing that there is a very good chance of partial success. In the years preceding euro zone entry Greece has managed to implement a wide range of privatisations raising revenues of 3.0% in 1998 and 3.5% of the GDP in 1999[3].

[3] Data for privatisations taken from OECD Privatisation Data Base as published in the Financial Market Trends, No. 82, June 2002 and for GDP from IMF World Economic Outlook Database.

PRIVATISATION REVENUES MILLION US$

	1993	1994	1995	1996	1997	1998	1999	2000	2001
PRIVATISATION REVENUES	35	73	44	558	1395	3960	4880	1384	1305



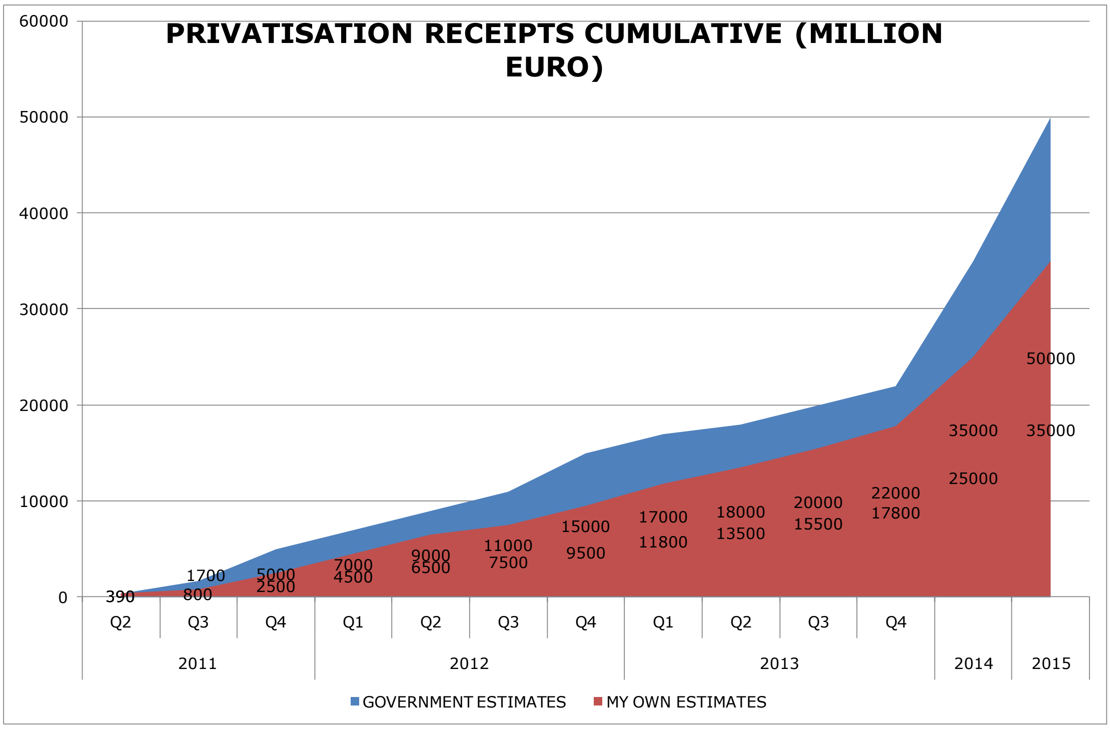
If this achievement is transposed to the current conjecture Greece can raise more than 15 billion euro in the next two years. I consider 2011 almost lost due the delayed start of the process and the late establishment of the new entity. Furthermore, serious investors have finalised their strategic plans for the year and might not be able to raise funds for new investments beyond what they have already decided to commit. *In effect the wishes of the government may not be compatible with the strategy of major international corporations in a number of sectors. The government and troika should not rush from a state of inaction to a state of hyperactivity. They should give international investors ample time to examine their overall strategy for Greece.*

PRIVATISATION ESTIMATES 2012/13

	2012	2013
REVENUES%GDP	3,0%	3,5%
GDP CURRENT PRICES BILLIONS EURO	228,4	235,5
REVENUES BILLIONS EURO	6,8	8,3

In conclusion, the target for 50 billion euro of privatization revenues until 2015 is rather optimistic. The government might be able to raise 15 billion in 2012/13 and that will lead to an overall figure of between 30 and 35 billion euro for the whole period. But even the latter lower figure, if achieved, is going to have a positive impact on debt reduction and will create a development shockwave throughout the economy. If the overall economic environment is stabilized, we are likely to see a speeding up of the process in the last quarter of 2011 becoming a wave in the second quarter of 2012 and throughout 2013.

If the government manages to raise 50 billion euro our debt to GDP ratio would have gone down to 139.5% by 2015. However, with the recent decision by the European Council the debt to GDP ratio will still be 120% of GDP in 2016 according to JP MORGAN analysts[4]. So any deviation from the target of 50 billion euro will again raise issues about the viability of Greek debt.



If the market's perception for Greek assets improves there is always the possibility of using financial instruments to raise revenues by pledging

[4] Reported in Reuters 22.7.2011

some of the most difficult to dispose assets as collateral (securitization, convertibles, swaps) assuming that these instruments will have the approval of Eurostat.

Privatisation is not a panacea. If done properly it will lead to a reduction of our debt and possibly to renewed growth. As John Kay wrote in his assessment on the twenty years of UK privatisation "privatised businesses have fared better than nationalised ones but most have not thrived in the private sector"[5]. What worries me is that following twenty months of total inaction, the new urgency coupled with tight and inflexible schedules may lead to blunders. And as we all know this time we only have one chance to get it right!

S. Travlos 27/7/2011

[5] Kay John (2002) Twenty Years of Privatisation, at http://www.johnkay.com/2002/06/01/twenty-years-of-privatisation

ANNEX 1: LIST OF PRIVATISATIONS 2011-2015

QUARTER	COMPANY	PARTICIPATION TO BE SOLD	TYPE OF SALE
Q2 2011	OTE	10%	SHARE SALE
Q3 2011	THESSALONIKI WATER COMPANY	40%	SHARE SALE
Q3 2011	ATHENS INTERN. AIRPORT	100%	CONCESSION
Q3 2011	OPAP	100%	CONCESSION
Q3 2011	THESSALONIKI PORT	23,30%	SHARE SALE
Q3 2011	STATE LOTTERIES	100%	SHARE SALE
Q4 2011	PIREAS PORT	23,10%	SHARE SALE
Q4 2011	HELLENIC DEFENSE SYSTEMS	99,80%	SHARE/ASSET SALE
Q4 2011	HELLENIC POSTBANK	34%	SHARE SALE
Q4 2011	PUBLIC GAS COMPANY	55%	SHARE SALE
Q4 2011	PUBLIC GAS COMPANY (PIPELINES)	31%	SHARE SALE
Q4 2011	RAILWAY OPERATOR	100%	SHARE SALE
Q4 2011	LARCO	55,20%	SHARE SALE
Q4 2011	ALPHA BANK	0,60%	SHARE SALE
Q4 2011	NATIONAL BANK	1,20%	SHARE SALE
Q4 2011	HORSE RACING ORGANISATION	100%	SHARE SALE
Q4 2011	MOBILE TELEPHONY LICENCES	100%	SALE OF RIGHTS
Q4 2011	CASINO MON PARNES	49%	SHARE SALE
Q4 2011	HELLENIC VEHICLE INDUSTRY	72,60%	SHARE SALE
Q4 2011	OPAP	34%	SHARE SALE
Q4 2011	HELLENIKON 1		SHARE SALE OF SPV
Q4 2011	AIRBUS AIRCRAFT	100%	SALE
Q4 2011	REAL ESTATE ASSETS 1		SHARE SALE OF SPV
Q1 2012	ATHENS INTERN. AIRPORT	21%	SHARE SALE
Q1 2012	HELLENIC PETROLEUM	35,50%	SHARE SALE
Q1 2012	PIREAS BANK	1,30%	SHARE SALE
Q1 2012	HELLENIC AGRICULTURAL BANK	38,60%	SHARE SALE
Q1 2012	EGNATIA ODOS	100%	SHARE SALE OF SPV
Q1 2012	HELLENIC POST	40%	SHARE SALE
Q1 2012	PORTS 1	100%	SHARE SALE OF SPV
Q2 2012	ATHENS WATER	27,30%	SHARE SALE
Q2 2012	LOAN AND CONSIGNMENT FUND	100%	SHARE SALE OF SPV
Q2 2012	REAL ESTATE ASSETS 2		SHARE SALE OF SPV
Q3 2012	PUBLIC POWER CORPORATION	17%	SHARE SALE
Q3 2012	HELLENIC MOTORWAYS 1	100%	SHARE SALE OF SPV
Q3 2012	REGIONAL AIRPORTS 1	100%	SHARE SALE OF SPV
Q4 2012	HELLENIKON 2		SHARE SALE OF SPV
Q4 2012	REAL ESTATE ASSETS 3		SHARE SALE OF SPV
Q4 2012	DIGITAL DIVIDEND 1	100%	SALE OF RIGHTS
Q4 2012	THESSALONIKI WATER COMPANY		SHARE SALE OF SPV
Q4 2012	HELLENIC GOLDMINES 1	100%	SHARE SALE OF SPV
Q1 2013	OFFSHORE GAS STORAGE FACILITY	100%	SHARE SALE OF SPV
Q2 2013	REGIONAL AIRPORTS 2	100%	SHARE SALE OF SPV
Q2 2013	PORTS 2	100%	SHARE SALE OF SPV
Q3 2013	REAL ESTATE ASSETS 4		SHARE SALE OF SPV
Q3 2013	HELLENIC GOLDMINES 2	100%	SHARE SALE OF SPV
Q4 2013	DIGITAL DIVIDEND 2	100%	SHARE SALE OF SPV
Q4 2013	ATHENS WATER		SHARE SALE OF SPV

QUARTER	COMPANY	PARTICIPATION TO BE SOLD	TYPE OF SALE
Q4 2013	HELLENIC MOTORWAYS 2	100%	SHARE SALE OF SPV
2014	REAL ESTATE/LAND		SHARE SALE OF SPV
2014	HELLENIC MOTORWAYS 3	100%	SHARE SALE OF SPV
2015	REAL ESTATE/LAND	100%	SHARE SALE OF SPV
2015	HELLENIC MOTORWAYS 4	100%	SHARE SALE OF SPV

ANNEX 2: LAND FOR PRIVATISATION (*)

	TOTAL AREA IN Ha	**LAND USE ACTIVITY**
HELLINIKON -ATHENS	550	COMMERCIAL/RESIDENTIAL/RECREATION
AFANTOU - RHODES	150	TOURISM
PRASONHSI - RHODES	8000	TOURISM
VEGORITIDA	1800	TOURISM
ANTIRIO	22,3	COMMERCIAL/TOURISM
GOURNES -HERAKLION	75	TOURISM
TOPIROU	800	ECOTOURISM
ERMIONI	15,3	TOURISM
SITHONIA - HALKIDIKI	9,4	TOURISM/RESIDENTIAL
TORONI	7,6	TOURISM/RESIDENTIAL
TOTAL	**11429,6**	

(*) The government has already decided last year to privatise these real estate assets but procedures have not yet started.