1. Historical background

After the restoration of democracy in 1974, Greece experienced a swift political transformation and, under the leadership of Prime Minister Konstantinos Karamanlis, it achieved accession to the European Community in 1981. A period of harmonisation to the European acquis and of deepening European integration followed, especially after an initial phase of special exemptions negotiated by the socialist government of the Panhellenic Socialist Movement (PASOK) under Andreas Papandreou, which came to power in 1981. As an EC member, Greece participated in all stages of European integration, including the Single European Act and the signing of the Maastricht Treaty. Greece also played a pivotal role in the development of the Integrated Mediterranean Programmes and their successor, the Cohesion Funds under the Community Support Framework. Nevertheless, and despite some redistribution and political reconciliation policies that it pursued, PASOK largely failed to take advantage of the opportunities offered by EC membership or to resolve long-lasting structural economic problems. PASOK lost power in 1989 under allegations of corruption, leaving the country in significant political turmoil and dismal economic performance with huge budget deficits and public

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debt, inflation averaging over 20% and rising unemployment rates. By 1990 Greece seemed to be facing a ‘transition challenge’, in the face of an urgent need for modernisation, stabilisation, restructuring and general improvement of economic performance.

The PASOK government was followed by successive short-lived transitory and coalition governments and then by a centre-right government by New Democracy, which ruled with a marginal majority and eventually lost power in 1993. The New Democracy government tried to implement a number of aggressive ‘shock-therapy’ reforms to cut established privileges in the public sector, rationalise public expenditure, increase tax revenues, control inflation and reduce unemployment and the public debt. New Democracy’s approach generated public unrest and strong opposition but eventually the Government lost power due to internal opposition, related to the issue of the constitutional name of the former Yugoslav Republic of Macedonia. The 1993 elections were won by the socialist party (PASOK), which was still under the leadership of A. Papandreou. Papandreou led a reformed PASOK, which engaged with economic and structural reforms (including the ‘taboo’ issue of privatisation), albeit under a more gradualist approach, and implemented fiscal consolidation and wage moderation measures. However, new PASOK’s modernisation and reform programme (and a more consensus-building approach) really took off after 1996 when Costas Simitis became Prime Minister having taken control of the party after A. Papandreou was removed from office due to ill health (Papandreou’s death one year later was marked by most as ‘the end of an era’, a perception that helped strengthen Simitis’ modernisation programme).

Under the premiership of Simitis (until 2004) the Greek economy registered strong rates of growth (consistently above the EU15 average), positive employment growth, declining inflation (which fell to single-digits in 1995 for the first time since the early 1970s) and rising private and public investment. At the same period a number of modernisation policies were successfully applied, including the full privatisation of the Athens Sock Exchange, implementation of central bank independence, the privatisation of a number of public utilities
companies and the liberalisation of markets especially with regards to the energy and telecommunications sectors. The newly independent Bank of Greece implemented a tight but successful monetary policy programme, keeping interest rates high (around 12%) to control demand-driven inflation and restricting liquidity and money growth through a number of regulatory measures imposed on the banking system. Tight monetary policy, coupled with the government’s fiscal consolidation and market liberalisation policies, helped reduce inflation to its lowest level for more than three decades (at 2% in spring 2000). As a result, and despite the bleak predictions about the country’s prospects in the beginning of the 1990s, Greece managed to meet all Maastricht criteria for accession to the EMU by 2000 (apart from the debt criterion, which was waived given the strong reduction in the budget deficit) and became a member of EMU in January 2001.

Greece’s change of fortune since 1996 is, not unreasonably, associated with Simitis’ premiership but a number of other factors also contribute in accounting for it. Since the early 1990s Greece experienced a significant immigration flow from the Balkan transition countries which, despite naturally causing some initial instability, helped with economic development by providing cheap labour, boosting consumer demand and partly counter-balancing the earlier patterns of rural depopulation. Further, Greece benefited notably by a significant allocation of EU funds under the 3rd Community Support Framework that, combined with an expansion of public investment in the build-up to the 2004 Athens Olympics, helped boost the economy. More importantly, deeper economic integration and policy harmonisation under the EU Single Market and the external pressures from the process of European monetary unification impacted significantly on (i) consensus-building regarding costly reforms, (ii) modernisation of public administration and policy implementation, and (iii) the expansion of competition (and thus also lower prices) in many sectors of the economy. Finally, the opening-up of the Balkan markets boosted Greek investment and demand for Greek products (thus also profitability) and removed Greece from its geographical isolation, thus providing a further impetus to economic development in the country.
Despite fears about Greece’s ability to continue its strong growth and convergence performance after the adoption of the Euro, the economy continued to grow at above-average rates (around 4%), while registering continuing employment expansion and net reductions in unemployment. Nevertheless, a controversial fiscal audit conducted by the newly elected New Democracy government in 2004 –and confirmed by Eurostat– revealed an exceptionally high budget deficit and eventually led to the initiation of the Excessive Deficit Procedure by the European Commission, which put the country under close monitoring with regards to its structural and fiscal policies.

Owing to strong growth and a tight fiscal policy (and tax rises), by 2006 Greece managed to bring down its deficit within the 3% limit (as share of GDP – estimated at 2.6% in 2006), while an equally controversial revision of its GDP estimates (by 9.6%, as agreed with Eurostat, against an original claim of 25% made by the Greek National Statistical Service) is now placing Greece on par with the EU25 average in terms of GDP per capita. The recent global economic turbulence (with the collapse of the US sub-prime market and the record increases in oil prices), coupled with the inability to control government expenditures and to expand sufficiently the revenue base, has led to a relative slowing down of GDP growth, rising inflation rates and a general deterioration of public finances, with the 2007 budget deficit estimated once again above the 3% SGP ceiling (estimated at 3.1% by OECD). Thus, despite the impressive improvements in the space of only about ten years, Greece still faces significant structural economic problems. The main problem appears to be the very high levels of unemployment (still close to 10% the second highest in EU15, with worrying structural characteristics including youth, female, long-term and graduate unemployment; and low labour mobility). But fiscal problems, related to inelastic public expenditures, the sustainability of the pension system (combined with an aging population) and the narrow tax base (owing to the huge size of the unregistered economy), as well as more structural problems relating to the low technological base, low foreign direct investment, weak agglomerations and exceptionally low levels of spending on research and development, and are also rather urgent.
2. Economic structure and policy

2.1. Structure of the economy

The Greek economy has a rather traditional structure, with disproportionately high levels of agricultural employment, low levels of heavy industry and business services and an estimated unregistered employment of around 25%. The economy is dominated by small and family-owned businesses, which represent over 90% of all registered firms and about 60% of total employment, while the average firm size in Greece is 5.8 employees (Eurostat data for 2005). Self employment (including employers and family members) is around 36% (having declined by up to 5pp in the last decade) while labour force participation is one of the lowest in Europe (62% in 2006). Employment in the primary sector is as high as 12% (producing 3.7% of national GVA), only a fraction smaller than the employment share of manufacturing, and employment in total industry, including construction, is 22.5% (producing 23.5% of national GVA) – while service sector employment is nearer to the European average at around 66% (producing 72.8% of national GVA, of which 19% is in financial intermediation). Part-time employment is particularly low (5.7% in 2007) as is female labour force participation (48% in 2007), while temporary employment stands at 11%. The wider public sector covers around 35% of total employment.

Around half of national GDP is produced in the Attica region (48.8% in 2005), while another 9.5% is produced in the region of the second largest city (Thessaloniki) – with the two regions hosting around 36% and 10% of total population, respectively. The strong presence of the agricultural sector in the Greek economy is also reflected in the sectoral specialisations of its regions, with the regions in the west (Western Greece and Epirus), the centre (Thessaly and Central Greece) and the south (Peloponnese and Crete) specialising in agriculture. Outside these specialisations, agglomeration in the country is particularly weak, with only a few industrial clusters in Central and Western Macedonia and in Attica, while the service sector is mainly but weakly
concentrated in Attica (business services) and the South Aegean (tourism). At the national level the country specialises in labour intensive products (mainly Food, Beverages & Tobacco and Textiles & Wearing Apparel), while its share of capital-intensive industries (mainly Fuel Products and Chemicals) is three times lower compared to the EU15 average (15% and 34%, respectively).

Overall, the Greek economy is characterised by low levels of competitiveness and significant rigidities, especially in the product market where it ranks 25th out of 30 countries in the OECD rankings for competition-friendly product market regulation. Besides the dominant position of the state-owned enterprises in a number of sectors of the economy (energy, telecommunications, transport, etc), market rigidities are also due to the existence of oligopolistic structures in various markets, as is for example the case of the industries for dairy products (where the two largest firms control over 90% of the fresh milk market), non-alcoholic beverages, beer, coffee and others. Concentration shares are particularly high also in the supermarkets sector and in the banking sector, where the top five banks control 70% of the market share. The high concentration rates and profitability in some basic sectors of the economy lead to above-average inflation rates which in turn reduce the competitiveness of the Greek economy at large. Low competitiveness is also due to very low R&D expenditures (0.5% of GDP), the generally weak technological base of the Greek economy and the very weak export market penetration (with exports accounting for less than 8% of GDP and a trade deficit around 16% of GDP).

Significant are also the rigidities in the labour market, especially in the public sector where strong unions, centralised collective bargaining and strict employment protection legislation (and established ‘insider’ privileges) produce, on the one hand, strong wage-inflation pressures (low wage flexibility) and, on the other, a significant pattern of labour market duality – at the expense of the less protected private sector employees. The pattern of duality is further reinforced by the significant proportion of unregistered employment and large shadow economy (estimated at around 30% of GDP), which is contributing to
the casualisation of the employment relationship, weakens labour incomes (and thus also consumer demand), squeezes government revenues (with estimates concerning tax evasion suggesting a magnitude of foregone revenues as high as 15% of GDP), and creates disincentives for investment in technology and human capital.

### 2.2. Government finances and fiscal stance

Owing to the deterioration of economic performance during the 1970s and throughout the 1980s, Greece entered the 1990s with very high budget deficits and government debt. High inflation kept interest rates also particularly high, thus putting an additional burden to government finances through the high cost of debt repayments. The consolidated debt of general government rocketed from around 30% of GDP in 1981 to 80% in 1990, peaking at 110% in 1993. Since then, despite the attempts for fiscal consolidation, the Maastricht convergence programme (which included wage restraint and nominal convergence and thus a reduction in interest and inflation rates), the remarkable growth of the economy, and the strong reduction in net debt interest payments (from 12.1% in 1994 to 4.6% in 2004), government debt has fluctuated around this value, with a sharp deterioration in the period 1999-2002 and a slow but steady improvement since 2003. According to the latest OECD data, which include the adjustments made after the revision of deficit figures, government debt has fallen from 114% in 2004 to 104% in 2007 while it is projected to fall below the GDP volume by 2009 (at 98%). According to Eurostat data, which further include adjustments for the revised GDP figures, the debt-to-GDP ratio has been already below 100% since 2003 and in 2007 it stood at 94%.

The exceptionally high public debt, which is the second largest in the EU27 (after Italy), is clearly related to structural problems in the government finances, which are best reflected in the composition and size of the budget deficit.
Entering the 1990s with deficits of around 15% of GDP, Greece struggled to reduce its net borrowing to below 10% and it was only after 1995 that the deficit started declining steadily, reportedly reaching 2% of GDP in 2000, thus allowing Greece to enter the EMU in 2001. Fiscal deficit reportedly declined further in 2001 reaching 1.4% of GDP and stabilising there (1.7% in 2003). However, the 2004 fiscal audit revealed that the deficit figures had been significantly under-reported. The revision of the deficit figures generated a huge political controversy in Greece, with New Democracy arguing that PASOK had manipulated the figures (by mis-calculating military expenditures and transferring surpluses created in the wider public sector to the central government) to achieve EMU entry. The new revised figures approved by Eurostat showed Greek budget deficit to have been consistently above 3% since 1997, climbing to 4.8% in 2002 and 7.2% in 2004. In June 2004 Greece was placed under the Excessive Deficit Procedure and given a two-year deadline for bringing its deficit below 3% of GDP. Greece exited the EDP in May 2007, on the basis of a strong decline in the deficit from 5.5% in 2005 to 2.6% in 2006 (revised figures available at the time). More recently the deficit situation has deteriorated and the OECD estimates that for 2007 the Greek budget deficit stood at 3.1% of GDP (compared to an earlier estimate of 2.9% and projections around 2.4% at the start of the year). OECD’s forecast for 2008 and 2009 is 2.1% of GDP for both years (against estimates by the Greek authorities of 1.6% and 0.8%, respectively).

The poor performance in terms of public debt and budget deficits is linked to some key structural problems, such as a rather low tax base and widespread tax evasion (with the shadow economy estimated at 30% of GDP), weak general government primary balances (never exceeding 2% of GDP since 2000 and negative in 2003-2005), and inelastic expenditures (the main components that are responsible for the decline in total expenditures as a share to GDP between 1995 and 2007 are, besides the strong growth, a net reduction in capital expenditure and interest repayments; whereas current expenditures have actually been increasing). More recently, some signs of improvement in the collection of tax and non-tax revenues have been
registered, although the expected slowdown of economic growth and the acceleration of inflation, which is also expected to suppress real incomes and demand, may neutralise in the near future the recent progress.

2.3. Structural reforms

Besides the attempts for fiscal consolidation, successive governments since 1990 have tried to implement a number of structural reforms to address key structural problems of the economy, mainly related to the labour market, the pension system, privatisation and the education sector. As was mentioned earlier, the early attempts for privatisation and market liberalisation by the New Democracy government of 1991-1993 were of limited success. Under the Simitis premiership a number of reforms, especially with regards to privatisation and market liberalisation, were implemented, including the partial privatisation of large state-owned enterprises in the energy sector (Public Power Corporation), the telecommunications sector (Hellenic Telecosms Organisation), the banking sector (General Bank, National Bank, etc; and mainly the Athens Stock Exchange and the Bank of Greece), the ship-building industry (Hellenic and Elefsina Shipyards) and other heavy industries (cement production, oil refineries, etc).

Generally, however, these were ‘halfway house’ privatisations, with the state retaining the majority ownership and the participation of strategic investors limited to minority holdings. Further, the government was less successful in implementing pension reform which, given the projections about Greece’s ageing population, appears urgently needed. Two attempts, in 1997 (by the Spraos Committee) and 2000 (the Giannitsis proposals) faced strong opposition by the public and the trade unions and had to be effectively withdrawn, with a mini-reform introduced in 2002 (the Reppas reform). In the labour market the main reforms were related to flexible working (teleworking, flexible hours, etc), temporary agency workers and part-time employment (Law
2639/1998), to collective dismissals, overtime pay and annualisation of working hours (Law 2874/2000), and to temporary employment and unemployment insurance (Law 2956/2001).

Since 2004, the New Democracy government under Costas Karamanlis has made further attempts to implement structural reforms and, despite the strong opposition, has been successful in passing a number of reforms in the labour market (Law 3385/2005, deregulating working hours and overtime pay) and the education (Law 3255/2004 and Law 3549/2007) and pension systems (Law 3655/2008), as well as introducing measures to expand the use of Public-Private Partnerships (Law 3389/2005) and shrink the size of the wider public sector (further privatisation in the banking system, the postal services, telecoms, etc and Law 3429/2005 on the management of enterprises in the wider public sector).

Nevertheless, many of these have been partial half-house reforms facing significant problems at the implementation level (as with the example of the recent legislation for tertiary education and pension reform, which is still not fully enforced and has triggered a strong wave of public opposition and industrial action) and are generally considered to be less deep than originally intended and than necessary. Finally, a number of issues that link to Greece’s significant structural problems, e.g., low rates of foreign and domestic investment, large red-tape bureaucracy and weak central and local administrations, low absorption of EU cohesion funds, and low levels of R&D and technology, have not been sufficiently addressed.
3. Economic performance since the 1990s

3.1. Sectoral developments

Robust growth for the national economy since the early 1990s has led to a significant expansion of most sectors of the economy. Growth was particularly due to the significant expansion of the banking sector (following liberalisation and market consolidation in the 1990s), construction activity (with the boost provided by the inflow of cheap migrant labour, the preparation for the 2004 Athens Olympics and the funds under the 3rd CSF, as well as the liberalisation of the mortgage market), and consumer demand (following strong credit expansion and the decline in inflation).

More recently the construction sector has shown large volatility, having grown by 40% in the period 2000-03, declined dramatically immediately after the Athens Olympics (by 48%, cumulatively, in 2004 and 2005), and grown fast again in 2007 (by almost 20%). In 2008 a remarkable drop is again reported, with the number of building permits issued in the first quarter of 2008 dropping by 26%. On the other hand, the banking sector continued its robust growth, registering very high profitability and continuous expansion domestically and abroad (though FDI and various M&As especially in the Balkans). According to Deloitte, by 2007 the five largest Greek banks controlled between 14% and 24% of the national market shares in terms of loans in five Balkan countries (Romania, Serbia, Bulgaria, Albania and FYROM). Domestically, credit expansion to the private sector in 2006-07 was 20%, while consumer lending grew by almost 24%. Total lending as a percentage of GDP remains low for European standards (86% compared to EU25 average of 131%), suggesting large scope for further expansion.

The tourism industry has also experienced significant growth recently, with international tourist arrivals growing by 8.4% between 2005 and 2006 and total turnover increasing by over 4% between 2006 and 2007. Equally favourable was the situation with the international shipping industry, with the total receipts
from international transportation growing by 14% in 2007 and accelerating even faster in 2008. Similar dynamism has been exhibited by the transport sector more generally, with a turnover growth of above 20% in 2006 and 2007.

In the domestic services, the telecommunications sector grew modestly by 1.1% in 2007 while IT sector grew by 9.9% in the same period. Retail trade grew by 5.6% in 2007, although in the past few months some strong signs of decline are evident, related to rising inflation and interest rates and the slowdown of the Greek and world economies. In the first quarter of 2008 private consumption declined in absolute terms for a first time since 1993. If the trend continues, this will halt the buoyant growth that wholesale trade has registered since 2005 (11.5% per year).

The dramatic drop in consumer demand has also led to a halt in the growth of industry. Industrial production in 2007 grew by 2.2% (manufacturing production grew by 1.8%), recovering from the minor decline of 2005; however, data for the first quarter of 2008 suggest a dramatic collapse of over 2.5% (-5.4% in March 2008 compared to March 2007), with the sectors suffering most being textiles (-12.5%), non-metallic minerals (-11.7%), clothing (-7.8%), and basic metals (-5.7%) and the sectors of chemicals, transportation vehicles and food & beverages showing the greatest resilience. Mining has been more strongly affected and continues its strong negative growth since the early 2000s (by over 25% since 2003), whereas the energy sector had, until recently, experienced robust growth (3.7% in 2007). The energy sector is expected to expand significantly in the medium-term, given the process of liberalisation and restructuring and a number of international projects that are underway (the Burgas-Aleksandroupolis oil pipeline, the Turkey-Greece-Italy gas pipeline and the South-Stream gas pipeline).
3.2. Macroeconomic performance

As already mentioned, Greece exhibited high and remarkably resilient rates of growth throughout the last 15 years. Since 1998 real GDP growth ranged from 3.4% in 1998/99 to 4.5% in 2000/01 and 5% in 2003, deflating somewhat more recently (4.0% in 2007). Growth in the country has been consistently above the EU15 average throughout the period (by an average of 2 percentage points). Labour productivity also increased significantly, albeit somewhat slower than GDP, growing at rates close to or above 4% pa in 1997-2003 but subsiding to rates closer to 2% since 2004 and thus moving from 83% of the EU27 average in 2000 to 96% in 2007. While much of the growth during the late 1990s is attributable to factors such as internal migration, the Athens Olympics, monetary convergence and the 3rd CSF, in more recent years the main components of growth have been private investment, exports of goods and services, and private consumption (growing since 2002 at an annual rate of 8.1%, 5.6% and 4.3%, respectively).

On the other hand, HICP inflation in the country has remained persistently above the EU and Eurozone average (ranging between 0.8 and 1.7 percentage points above the latter), jumping from a low 2.1% in 1999 to a high 3.9% in 2002 and remaining above 3% until 2007. The recent financial turmoil and oil prices rises have led to a sudden hike in inflation, which is estimated to have reached 4.4% in March 2008 and 4.9% in May 2008. Combined with the strong performance of the Euro, high inflation in the country has led to a continuous loss in competitiveness, as signified by the real effective exchange rate, which appreciated by 14% between 2000 and 2007. Owing to such developments, as well as some notable nominal wage increases (around 6% per annum since 2001), real unit labour costs in Greece have diverged by around 6.5 percentage points from the Eurozone average.

In turn, these developments, coupled with Greece’s consumption expansion, have led to a net deterioration of the trade balance, with the trade deficit rocketing from €27.5bn in 2005 to €41.5bn in 2007 and the current account
deficit reaching €32bn (-12% of GDP). This deterioration has masked a significant export performance over the recent years, with growth in real terms of around 6.5% per year since 2003 (9.7% in nominal terms) and a significant shift towards high-tech and resource-intensive products. Imports, however, have grown even faster, especially in recent years (by 12% in 2006 and 10.5% in 2007), although the recent drop in consumer demand is expected to contain significantly the growth of imports in 2008.

As mentioned earlier, private investment in the country has been buoyant recently, growing at an average rate of 8.1% (reaching 25.6% of GDP in 2007). On the other hand, public investment as a share of GDP has been subsiding since the Athens Olympics, stabilising in 2007 at 3% of GDP (7% of total general government expenditure). Finally, Greece’s performance with regards to inward foreign direct investment has been particularly poor, with the country being outside the top-100 FDI recipients in the world (compared to an EU average of 67) and FDI flows ranging below 4% of total gross fixed capital formation in the country since the late 1990s. Inward FDI by year has been rather volatile (€1.7bn in 2004, €0.5bn in 2005, €4.3bn in 2006 and €1.4bn in 2007), while FDI stock in the country is estimated at around €30bn. A number of factors explain the poor performance, including the aforementioned product and labour market rigidities, relatively high taxation and unit labour costs in comparison to neighbouring countries, rather significant red-tape bureaucracy and corruption, as well as deficiencies in terms of marketing (including an unwillingness to open-up the privatisation process to large ‘strategic’ investors from abroad). In contrast, outward FDI flows continue to be very strong, reaching €3.9bn in 2007.

3.3. Employment and the labour market

Having fluctuated at around 7% throughout the 1980s, unemployment in Greece rose sharply in the early 1990s, despite the strong growth of the
economy, from 6.4% in 1990 to 9.2% in 1995, peaking to 12% in 1999, when it exceeded for a first time the EU15 average. Unemployment has remained high (and above the EU average) ever since, declining to 10.5% in 2004 and following a steeper rate of decline more recently (9.8% in 2005 and 8.3% in 2007 – although this sharp decline is partly attributable to the inclusion of part-time and contract workers to the labour force on a headcount rather than full-time equivalent basis). This fall has characterised effectively all components of unemployment, including female unemployment (from 18.1% in 1999 to 12.8% in 2007), youth unemployment (from 31.5% in 1999 to 22.9% in 2007 – still around 60% higher than the EU15 average) and long-term unemployment (from 6.5% in 1999 to 4.1% in 2007). In fact, long-term unemployment for males is particularly low (2.2% in 2007; whereas for females it is over twice the EU15 average at 7.0%) while overall male unemployment is at levels comparable to, or below, the EU average (7.9% versus 7.1% in 1999 and in 5.2% versus 6.4% in 2007). Nevertheless, it appears that further reductions in unemployment will be difficult to achieve, as the rate of economic growth slows down and further gains will need improvements in the structural elements of unemployment, especially graduate unemployment (with the unemployment rate of university degree holders in 2007 at 10.1%, even higher than the 9.6% of those with no formal education), female unemployability (with female long-term unemployment being 55% of total female unemployment), and demand-deficiencies (with unemployment rates being higher in the declining manufacturing and mining sectors – as well as in sectors with high seasonal employment, such as hotels and catering).

The good unemployment performance recently has been of course associated with a net increase in employment, which has been accelerating fast over the past five years, growing by an annual average rate of 1.8% since 2001. Given the slow population growth, this represents a fast increase in employment participation, which has in fact risen by 5pp since 2001 (standing at 61.4% in 2007). Employment growth has been more solid for females (2.5% pa in 2001-2007) and it is mainly attributable to the increase in part-time employment. Indeed, in 2006 part-time jobs represented 70% of total job creation (or
approximately 50,000 jobs), lifting the part-time employment share from 5.0% to 5.7%. Part-time employment is predominantly a female phenomenon (2.7% for men; 10.1% for women), as is temporary employment, which is rather high in the country (10.9%; 9.3% for males and 13.1% for females). Much of the employment growth is also due to substantial increases in the public administration sector (by over 10% in 2006, accounting for over 50% of total employment growth). Nevertheless, employment participation rates in Greece remain dismal, with 2.3 million people being inactive in 2007 (31.8% of working-age population), and with female inactivity still over 50% of working-age population.

This employment growth performance has been achieved despite some fast increases in real wages. Since 1999 total compensation of employees in the private sector has been rising by around 6.2% pa, well above inflation and almost twice as fast as labour productivity, which in the same period grew at 3.2% pa. Wage increases in the public sector were even higher (until 2004), especially in the large state-owned enterprises outside the public administration, which have monopolistic market position and strong unions. Nevertheless, wages in the country remain low relative to European standards (73% of the Eurozone average in 2007, up from 55% in 1998).
4. Future prospects and challenges

Over the last 15 years Greece has exhibited a remarkable record of economic growth and monetary convergence with the Eurozone. Its economy has almost doubled in real terms since the early 1990s (grown by 60% since 1998) while in per capital terms it covered a 15 percentage points distance from the EU27 average in the space of 8 years. Reversing a very long trend, the country has become a net migration recipient and net capital exporter, having placed significant direct investments in the Balkan countries over the last decade. Its financial system has expanded significantly, while many of its sectors of specialisation have developed a competitive international profile.

Nevertheless, as the recent economic turbulence has manifested, the Greek economy is still not based on a solid foundation and rather suffers from a number of structural problems and weak fundamentals. On the one hand, there are significant fiscal problems that have to do with tax evasion, inelastic government expenditures, an ageing population and an unsustainable pension system. On the other, a number of significant structural problems exist, related to export penetration and economic competitiveness, structural unemployment and inactivity, low labour mobility and wage flexibility, low productivity, low technological absorption, low educational performance (as revealed in the OECD PISA studies) and, above all, economic duality (with a large shadow economy and a disproportionately protected public sector). Economic expansion has been largely sustained through the liberalisation of the financial sector (which provided cheap credit to households), the reduction in interest rates due to EMU, the migration inflows, the opening-up of the Southeast European market and the significant growth of public investment and consumption (related to the Athens Olympics and the 3rd CSF). However, progress with labour productivity, employment participation, and the technology content of production has been much more modest.

Given the fact that most of the earlier drivers of growth will be of much less importance in the future (e.g., a much lower allocation of funds under the 4th
CSF and of course no economic boosts anticipated similar to the Athens Olympics and the EMU), the economic outlook for Greece could seem much less secure than what the recent record of robust growth suggests. Significant improvements in the regulation of product and labour markets, rationalisation of the pension and education systems, and more focused interventions to attract domestic and foreign investment in the country are essential ingredients for a strategy to improve employment participation rates, improve the sustainability of public finances, increase the competitiveness of the economy and its export penetration, raise innovation and productivity and upgrade the position of the economy in the value-added chain.

In the short- to medium-run, of course, the most urgent problems have to do with the fast acceleration of inflation, which erodes economic competitiveness and living standards, the decline in private consumption and real household incomes, and the control of the fiscal stance of the country.