



NATIONAL BANK OF GREECE
Economic Analysis Department

Survey of Greek SMEs H2:2016

Special Issue: Capital Controls

Paul Mylonas
Deputy CEO

Nelly Tzakou-Lambropoulou
General Manager Retail Banking

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- ❑ 2016 presented a gradual recovery of the business climate, as reflected in the 8 point improvement in the business confidence index for SMEs during the year (to -2 in H2.2016, from -10 in H2.2015) – though remaining in negative territory. The main driving force behind the improvement was the tourism sector, whose confidence index rose by 27 points in 2016 (to +13 in H2.2016, from -14 in H2.2015).
- ❑ Specifically, the two main components of the confidence index (current and future demand) appear to converge at a level well above 2015, but significantly lower than 2014 (with the confidence index showing about 15 points change between H2.2016 the respective period of 2014). In seeking the factors limiting the recovery dynamic, we focused on the impacts of capital controls on Greek SMEs.
- ❑ A year-and-a-half after the imposition of capital controls, SMEs show clear signs of adapting to the new state of play – with 39 per cent of the sector stating that they no longer face any problems in their operations (compared with just 5 per cent in the first six months after the imposition of capital controls).
 - ✓ Relatively significant problems – although with apparent improvements – still seem to exist regarding the collection of receivables (53 per cent of the sector), the completion of customer orders (45 per cent) and the supply of raw materials (41 per cent).
 - ✓ On the other hand, wage payments and product transportation processes seem to have normalized to a large extent.
- ❑ Accordingly, operational adjustment to the capital control regime seems for the most part to have been effected, though the process was not easy, as SMEs deployed significant policy changes that put a sharp brake on their medium-term growth dynamics. Indicatively, we note that 34 per cent of the sector has cancelled investments (compared with 24 per cent in H2.2015).
- ❑ In addition, the extension of the capital controls over many months absorbed the “short-term liquidity cushion” (outside Greek bank accounts) held by a significant segment of SMEs (about 36 per cent), thereby exacerbating the depth and breadth of the consequences of the capital controls.

- ❑ The fact that the continued implementation of capital controls is leading to structural changes in the business sector is confirmed by the view of SMEs that the return to normality will not be swift. Specifically, 17 per cent of SMEs state that when capital controls are removed they will require more than a year to return to normal business operations. It is notable that this figure has tripled in the last 12 months, as only 6 per cent made this statement in the first six months after the imposition of capital controls.
- ❑ These findings point to the conclusion that a rapid removal of capital controls is:
 - ✓ crucial to prevent structural problems in SMEs (especially as a result of the cancellation of investment projects), while
 - ✓ of relatively low risk, as entrepreneurs in all sectors say they will not rush to withdraw all their deposits, suggesting that the level of cash amounts held by SMEs with Greek banks will remain at roughly similar to the current levels (90 per cent).
- ❑ In addition, it is worth noting that the removal of capital controls will likely prompt about 1/3 of SMEs to reboot “frozen” investments over the ensuing six-month period. Assuming behaviour similar to that of the past 15 years (with investments in the range of 3-4 per cent of sales), new investments would likely reach a total of about €1 billion.

❑ Business conditions in H2.2016

- SME business confidence index
- Breakdown by size
- Breakdown by business sector

❑ Capital Controls

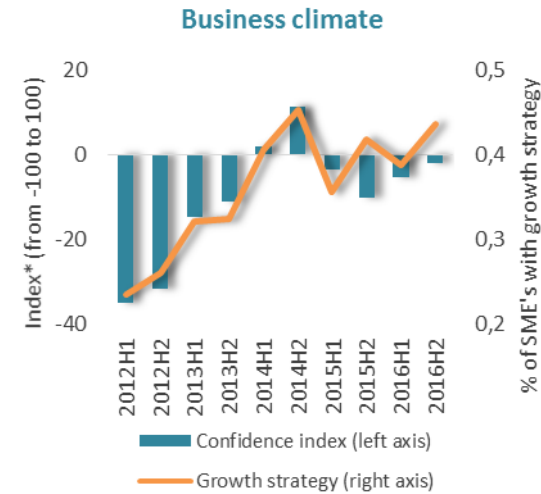
- Short-term impacts
- Medium-term changes in strategy
- Estimated time to return to normal operation
- Strategy for cash reserves

❑ Annex

- Mapping the SME segment in Greece
- Sample description
- Constructing the business confidence index for SMEs
- Survey ID

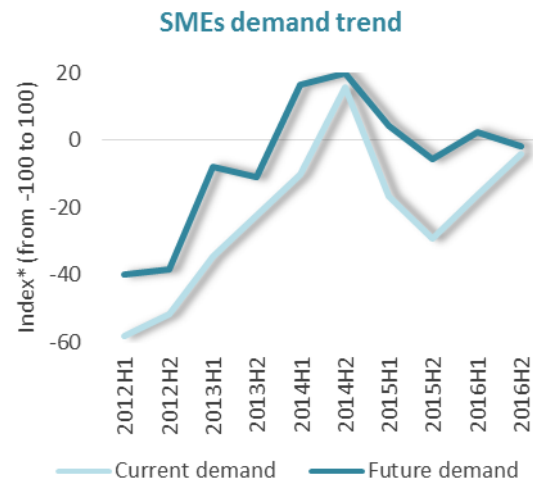
Gradual recovery in business confidence during 2016 – micro enterprises, however, have difficulty in keeping up

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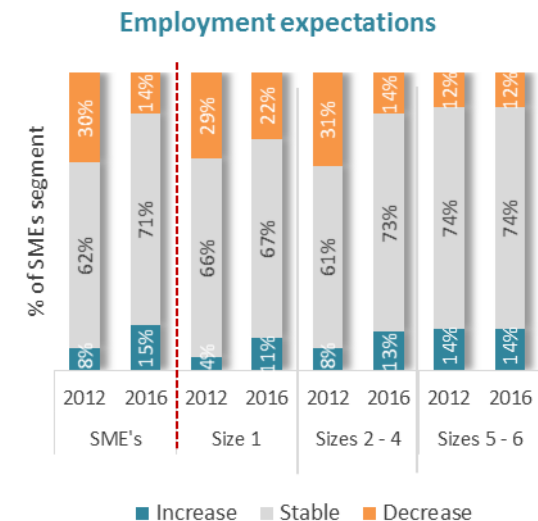
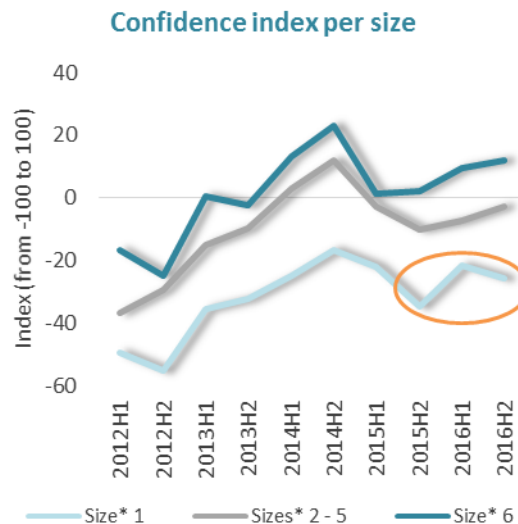


* The confidence index corresponds to the net balance of answers for decrease (-100), stability (0) and increase (+100).

- During 2016, the SMEs confidence index improved by 8 points – counterbalancing in part the decline of 2015, though still remaining below the 2014 level (by almost 15 points). Reflecting the climate of gradual recovery is the fact that (i) the two components of the confidence index (current and future demand) seem to converge at a significantly higher level than in 2015, and (ii) dynamic SMEs (i.e. with growth targets) now account for 44 per cent of SMEs compared with 36 per cent in 2015.
- At the same time, the gap between micro enterprises (turnover below €0.1 million) and medium enterprises (turnover between €5 million and €10 million) is widening, with the latter presenting a steady dynamic while micro enterprises struggle to maintain stable growth. As regards small enterprises (turnover between €0.1 million and €5 million), in the beginning of the crisis they reduced employment with the same aggression as micro enterprises (31 per cent of SMEs went ahead with layoffs in 2012), whereas now they have adopted a more conservative strategy, which resembles that of medium enterprises (with 14 per cent of SMEs carrying out layoffs in 2016).



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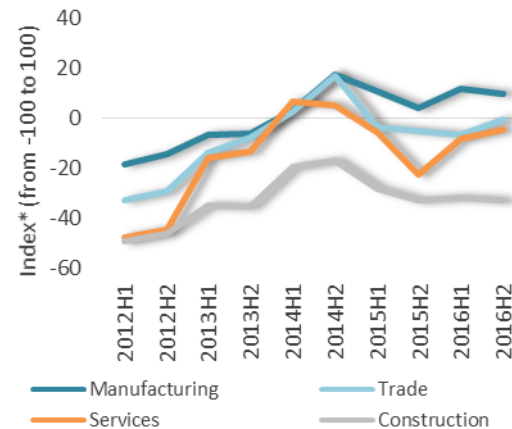


*The 1-6 scale in the above diagram refers to scales of turnover. Specifically (in € millions): 1=(0-0.1), 2=(0.1-0.5), 3=(0.5-1), 4=(1-2.5), 5=(2.5-5) and 6=(5-10).

Manufacturing remains in general the most dynamic sector, while tourism SMEs post a strong recovery

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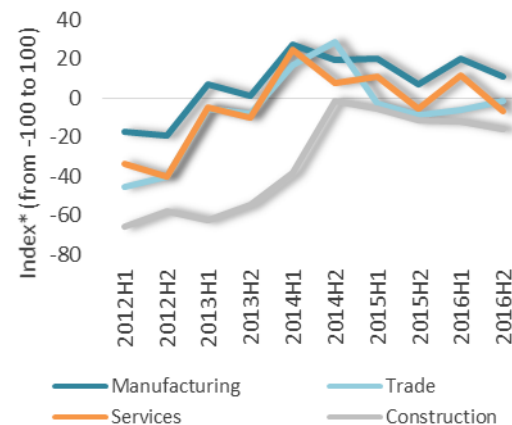
Confidence index per sector



* The confidence index corresponds to the net balance of answers for decrease (-100), stability (0) and increase (+100).

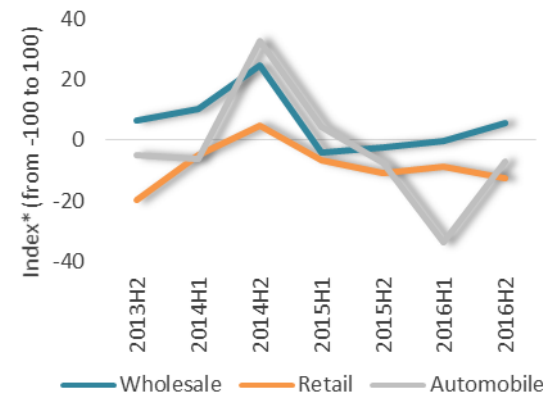
- Manufacturing SMEs still present the greatest dynamism and resilience, while the confidence index for services posted a notable increase during 2016 by 18 points (compared with 3 points for the other sectors). Specifically, the driving force behind this growth in services were tourism SMEs, as their confidence index improved by 27 points in 2016.
- Excluding retail trade, all other trade sectors also present signs of recovery, with auto trade reversing the sharp decline it posted in H1.2016 and returning to the 2015 level, while wholesale trade continued its slow but steady growth of the last decade (by 10 points, cumulatively).
- However, the fragile nature of the improvement in the business climate is reflected by the fact that the recovery in expectations for future demand observed in H1.2016 has now reversed in all sectors (excluding trade).

Future demand per sector



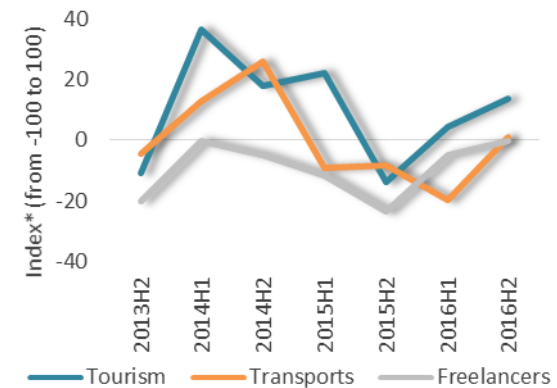
* The confidence index corresponds to the net balance of answers for decrease (-100), stability (0) and increase (+100).

Confidence index: Trade



* The trade confidence index corresponds to the net balance of positive and negative answers concerning the level of stock and the trend of past and future demand.

Confidence index: Services



* The services confidence index corresponds to the net balance of answers concerning the business situation and the past and future demand.

❑ Business conditions

- SME business confidence index
- Breakdown by size
- Breakdown by business sector

❑ Capital Controls

- Short-term impacts
- Medium-term changes in strategy
- Estimated time to return to normal operation
- Strategy for cash reserves

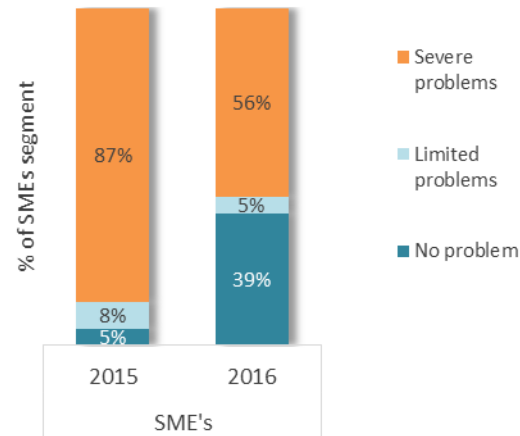
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The short-term impact of the capital controls has been limited, thus evidencing adaptation to the new state of play

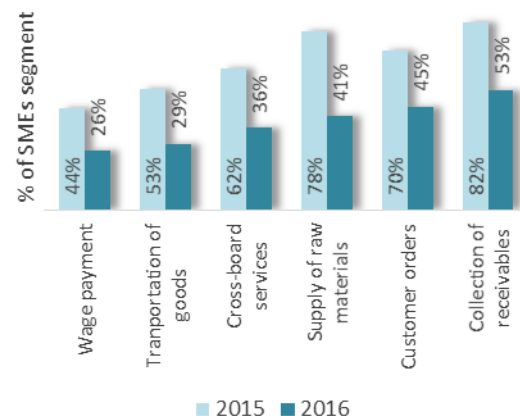
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Short-term problems due to capital controls

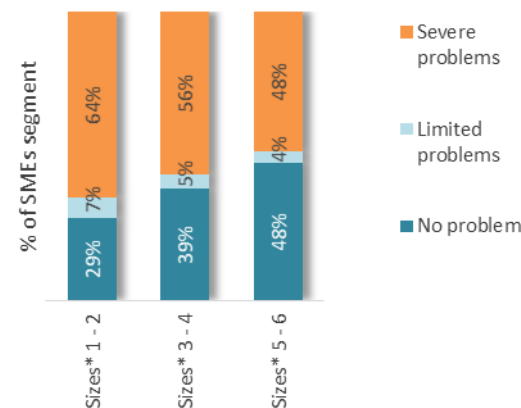


- One and a half years after the imposition of capital controls, SMEs show clear signs of adapting to the new conditions. Specifically, whereas in H1 only 5 per cent of SMEs stated that they had no operational problems following the imposition of capital controls, this rate now stands at 39 per cent.
- Relatively significant - though clearly improved - problems still seem to exist regarding the collection of receivables (53 per cent of SMEs), completion of orders (45 per cent) and supply of raw materials (41 per cent). On the other hand, wage payments and product transportation processes seem to have returned to normality to a large extent.
- Differentiation is also evident across the various business sizes and sectors:
 - ✓ Medium enterprises have managed to adapt better than smaller enterprises, with 48 per cent facing no problems at all compared with just 29 per cent of micro enterprises.
 - ✓ Manufacturing and services SMEs are in a better position compared with trade and construction SMEs, which face overall fewer problems in their operations.

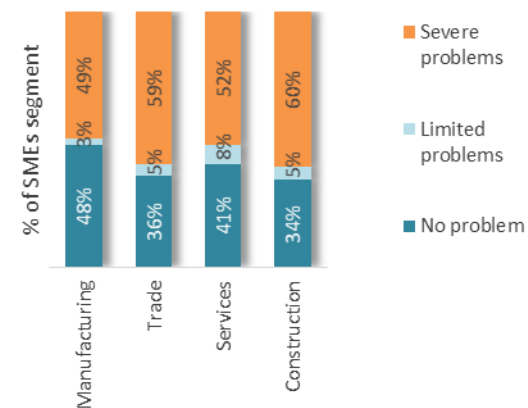
SMEs facing problems due to capital controls



Short-term problems due to capital controls (per size)



Short-term problems due to capital controls (per sector)



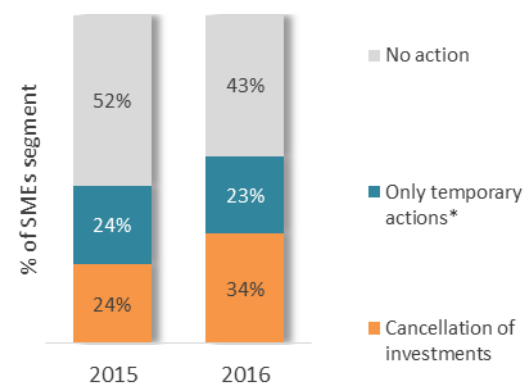
*The 1-6 scale in the above diagram refers to scales of turnover. Specifically (in € millions): 1=(0-0.1], 2=(0.1-0.5], 3=(0.5-1], 4=(1-2.5], 5=(2.5-5] and 6=(5-10].

However, this adaptation was achieved with significant cancelations of investment plans, resulting in a tendency for medium-term contraction of SMEs

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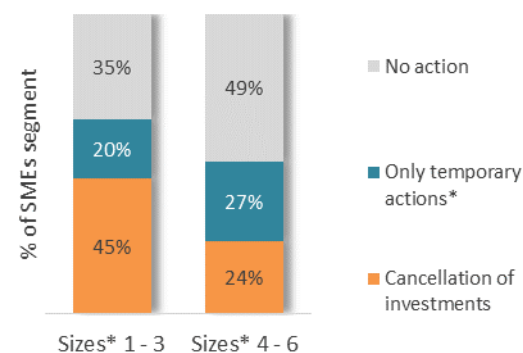
- The observed adaptation to the current conditions following the imposition of capital controls was achieved by taking a series of actions that in the medium term serve to bring about contraction in the SME sector.
- While the share of SMEs that have taken only temporary measures (temporary reduction in production and/or employment, search for new suppliers) remains close to 1/4, the share of SMEs that have embarked on a medium-term change in their strategy has increased significantly. Specifically, one and a half years after the imposition of capital controls, 34 per cent of SMEs state that they have cancelled their investment plans as a result of the capital controls. Given that this percentage was significantly lower during the first 6 months after capital controls were imposed (24 per cent at the end of 2015), its strongly rising trend gives cause for concern and reflects the structural impacts that capital controls will have if they are maintained for much longer.
- The most significant changes in strategy can be seen in small enterprises (with turnover below €1 million), with 45 per cent having cancelled their investment plans due to capital controls (compared with 24 per cent of medium enterprises). There do not appear to be significant variations across sectors – excepting the high rate of temporary measures in construction (33 per cent compared with 21-25 per cent in other sectors).

Measures against capital controls



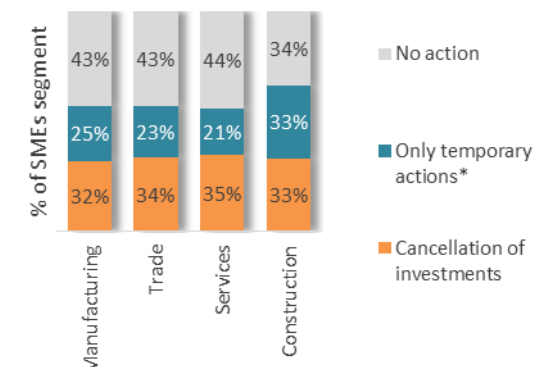
*Temporary downsizing of production or/and employment, search for new suppliers

Measures against capital controls
(per size)



*Temporary downsizing of production or/and employment, search for new suppliers

Measures against capital controls
(per sector)



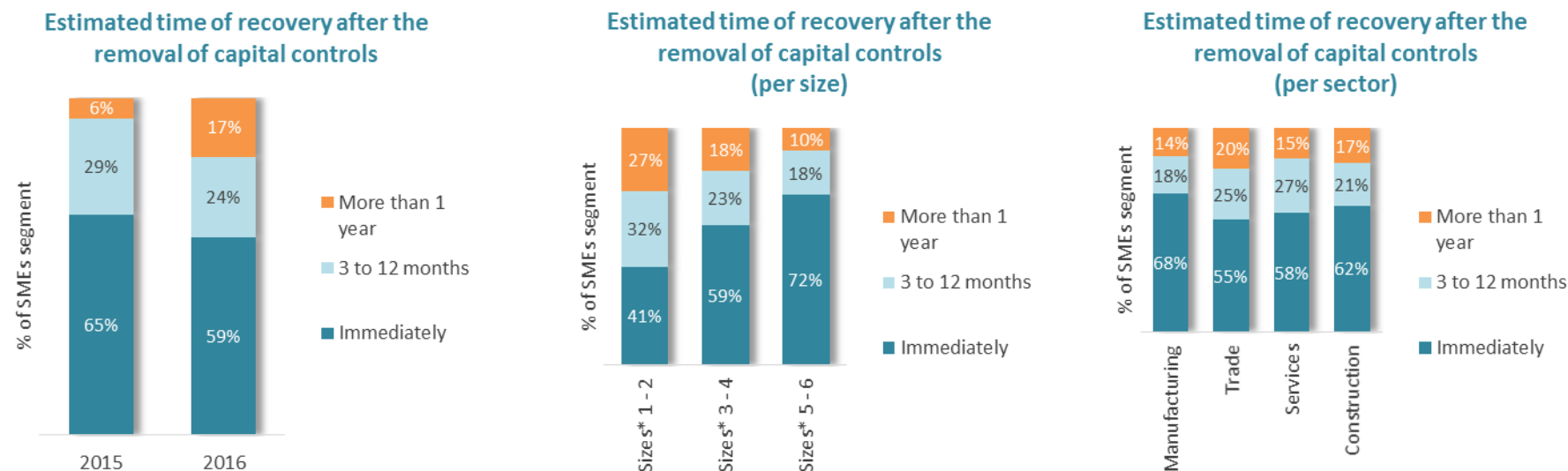
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Structural changes in the operation of SMEs will delay their return to normality after the removal of capital controls

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- The growing number of SMEs that need to deploy measures of a strategic nature in order to address the impact of capital controls makes enterprises less optimistic about their quick recovery to pre-capital controls levels. For example, the share of SMEs that anticipate a recovery period greater than one year has almost tripled, reaching 17 per cent compared with 6 per cent in 2015.
- These estimations improve significantly when we move from smaller to larger SMEs, with 72 per cent of medium enterprises estimating that the return to normality will be achieved immediately after the removal of capital controls and just 10 per cent considering that the required period will exceed one year, whereas the corresponding figures for micro firms are 41 per cent and 27 per cent, respectively. These estimates indicate to some extent the greater resilience and adaptability larger SMEs when addressing the challenges of capital controls (as reflected in the limited adoption of emergency strategies, see slide 9).
- As far as individual sectors are concerned, manufacturing SMEs are more optimistic (68 per cent anticipate immediate recovery), while the operations of trade SMEs were affected the most, as 20 per cent estimate that more than one year is required to restore their business operations to normality.

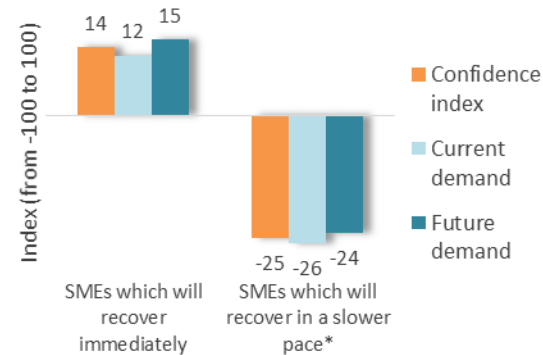


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The imposition of capital controls may widen the gap between strong and weaker enterprises

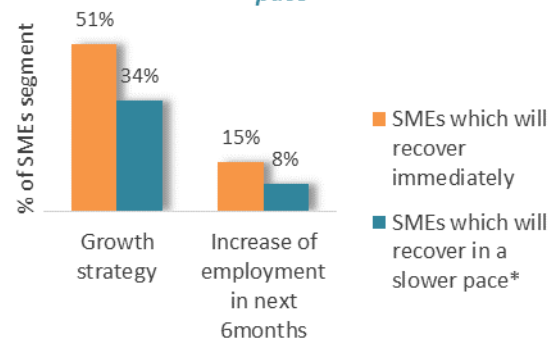
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Confidence Index:
SMEs which will recover immediately after the removal of capital controls vs those which will recover in a slower pace



*more than 3 months

Dynamism indexes:
SMEs which will recover immediately after the removal of capital controls vs those which will recover in a slower pace



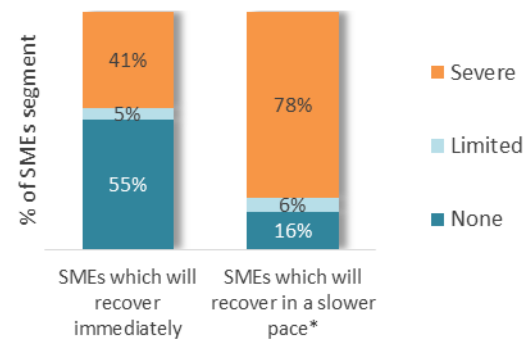
*more than 3 months

□ The estimations of SMEs regarding the required time for their recovery doesn't seem to be just a matter of perception of each entrepreneur but a reflection of the profile of each enterprise. Specifically, the 41 per cent of SMEs stating they will need more than 3 months after the removal of capital controls in order to return to normal operation coincide with the weakest SMEs, as:

- ✓ they present a lower confidence index (-25 points compared with +14 points for other SMEs) and are less oriented to growth strategies (34 per cent compared with 51 per cent for other SMEs), and
- ✓ just 16 per cent of these SMEs state that they do not face any operational problems due to capital controls (compared with 55 per cent of other SMEs), while more than ¾ of those have taken strategic measures to face capital controls (compared with 45 per cent of the other SMEs).

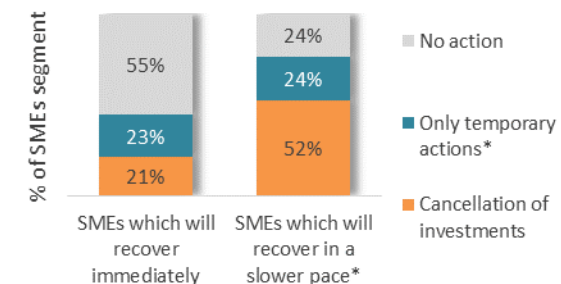
□ As a result, in the period after the removal of capital controls, the remaining segment of SMEs (i.e. 59 per cent) – which is already the strongest – will return immediately to normal operation, thus further widening the gap over the weaker enterprises.

Problems due to capital controls:
SMEs which will recover immediately after the removal of capital controls vs those which will recover in a slower pace



*more than 3 months

Actions against capital controls:
SMEs which will recover immediately after the removal of capital controls vs those which will recover in a slower pace



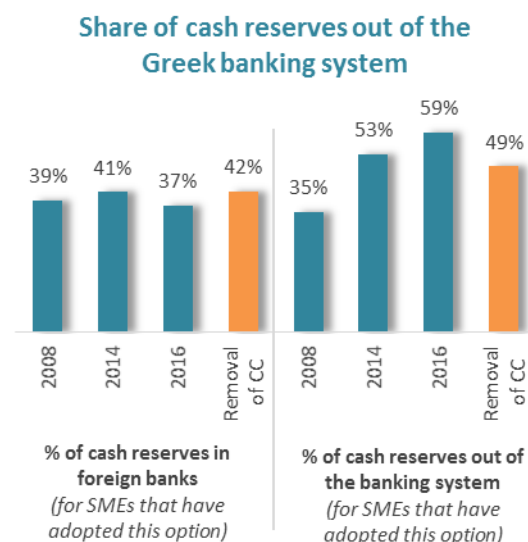
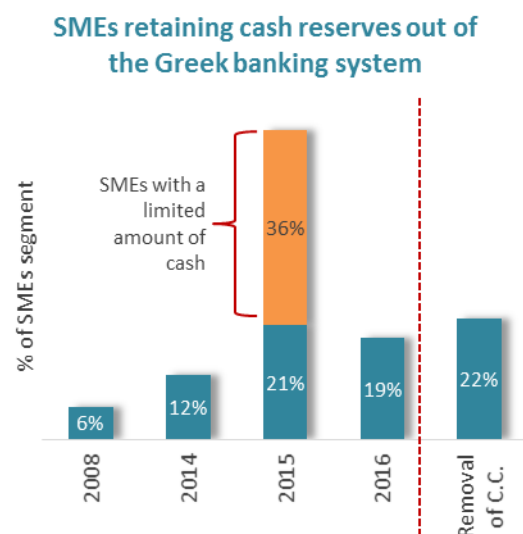
*Temporary downsize of production or/and employment, search for new suppliers

**more than 3 months

The extension of capital controls for many months absorbed the “short-term liquidity cushion” that SMEs held outside Greek banks, thereby exacerbating the extent of their impact

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- Since the beginning of the crisis and the gradual increase of uncertainty, some SMEs started stocking up cash reserves outside Greek banks, with the respective percentage increasing from 6 per cent of SMEs in 2008 to 12 per cent in 2014, then soaring to 57 per cent after the imposition of capital controls. However, most of them (36 per cent) stated that those reserves were limited, as they comprised just a “short-term liquidity cushion” serving as protection against the anticipated imposition of capital controls. Today - 18 months since the imposition of capital controls - this “cushion” has been exhausted and now only 1/5 of SMEs (i.e. those that stated significant cash reserves at the end of 2015) still has cash reserves outside Greek banks.
- When focusing on the first alternative for placement of cash reserves (foreign banks), it can be seen that the percentage of SMEs holding deposits with foreign banks increased to 13 per cent in 2016 compared with 7 per cent in 2014 and 2 per cent in 2008. Note that the share of cash reserves that enterprises adopting this option chose to transfer to foreign banks is on average unchanged at around 40 per cent of their available cash reserves in the period 2008-2016.
- As to the other alternative (outside the banking system in general), the share of SMEs with cash reserves outside the banking system is relatively more stable in the period under review (4 per cent in 2008, 5 per cent in 2014 and 6 per cent in 2016), showing only a modest anticipated increase (to around 8 per cent in the period after capital controls are removed). However, the share of cash reserves held outside banks by enterprises that adopted this alternative presents a rising trend over time (from 35 per cent in 2008 to 53 per cent in 2014 and 59 per cent in 2016).

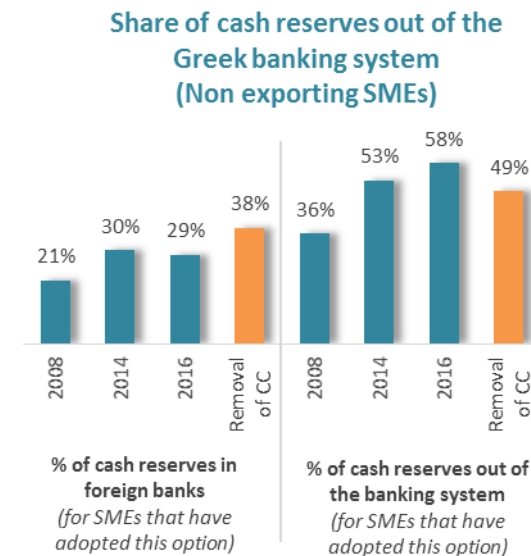
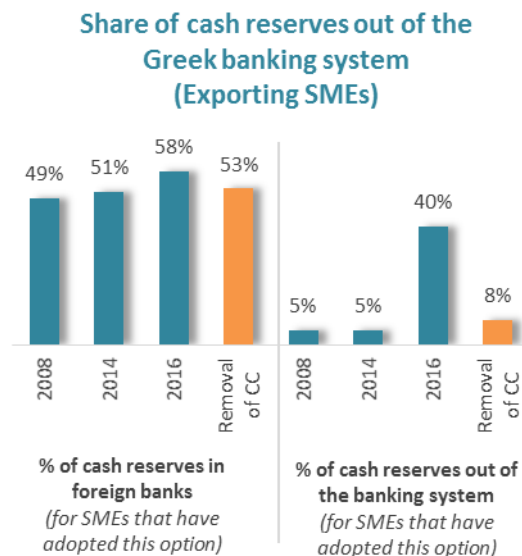


1/3 of export-oriented SMEs have cash reserves in foreign banks

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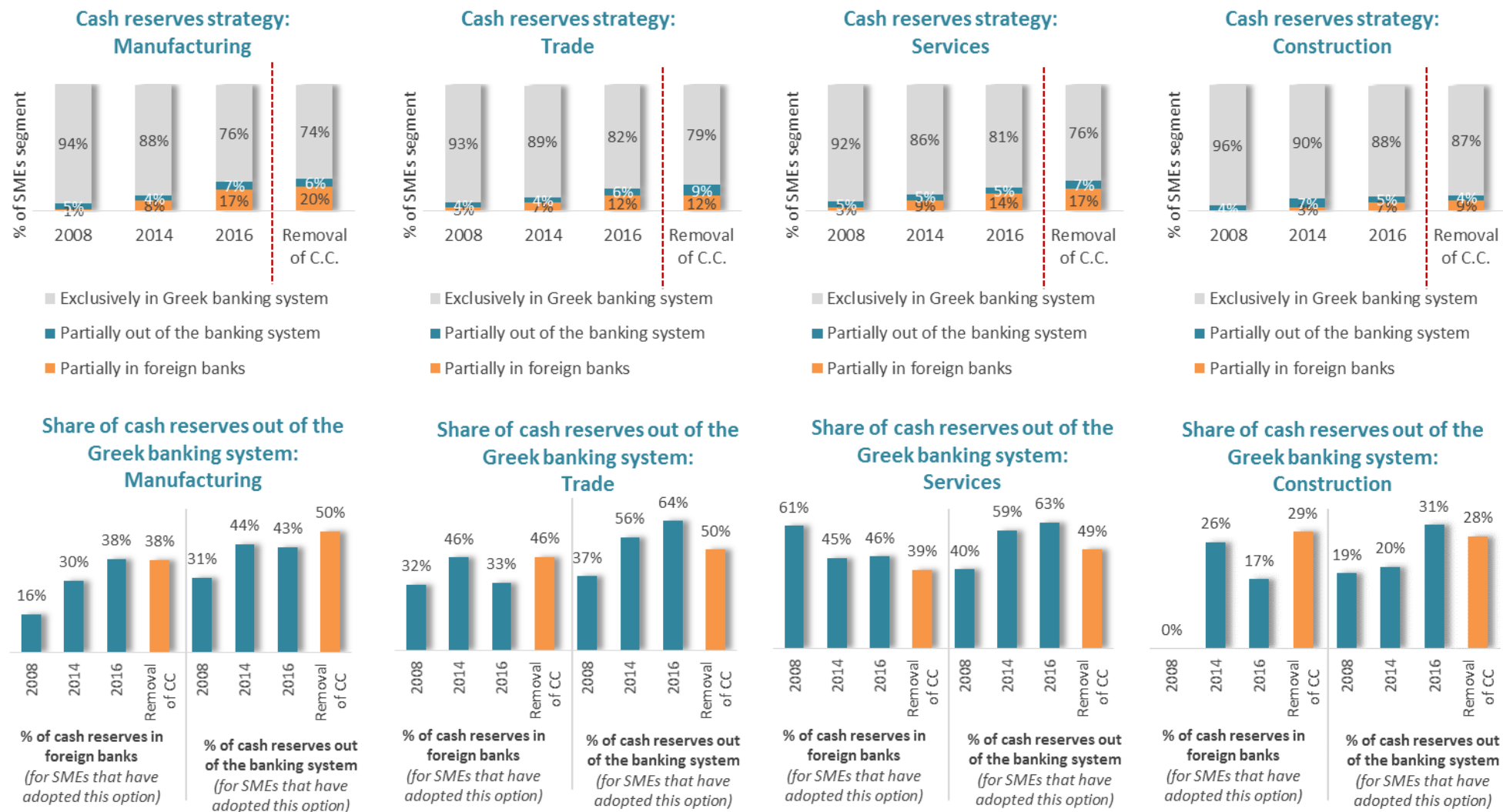


- Export-oriented SMEs - due to the nature of their operations - have long term relations with foreign banks to a greater extent, which intensified during the crisis (32 per cent of export-oriented SMEs hold cash reserves with foreign banks in 2016 compared with 12 per cent in 2008). At the same time, export-oriented SMEs that adopted this option seem to have also increased the share of their cash reserves in foreign banks (58 per cent in 2016 compared with about ½ during 2008-2014). Additionally, a limited share of export-oriented SMEs (mainly in wholesale trade) now hold a significant amount of their cash reserves outside banks - a trend which is, however, expected to reverse after the removal of capital controls.
- The behaviour of non-exporting SMEs is also notable, since the share of those keeping cash reserves in foreign banks doubled between 2014 and 2016 (up from 5 per cent to 11 per cent) and has increased by more than ten times since 2008 (1 per cent of non-exporting SMEs). At the same time, non-exporting SMEs that adopted this alternative seem to have also increased the share of cash reserves placed in foreign banks (30 per cent in the last two years compared with 20 per cent in 2008). In addition, a small share of non-exporting SMEs (5-6 per cent) holds a growing share of cash reserves outside banks (58 per cent in 2016 compared with 36 per cent in 2008).



The turn to foreign banks is stronger in manufacturing and weaker in construction

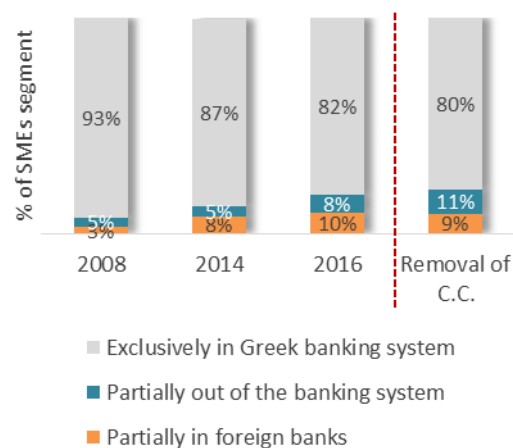
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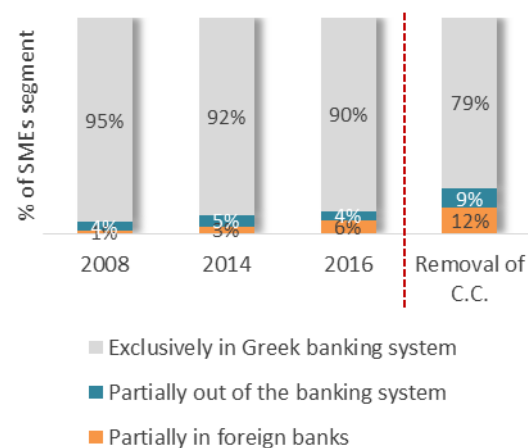
8 per cent of micro enterprises hold on average 3/4 of their cash reserves outside the banking system

15

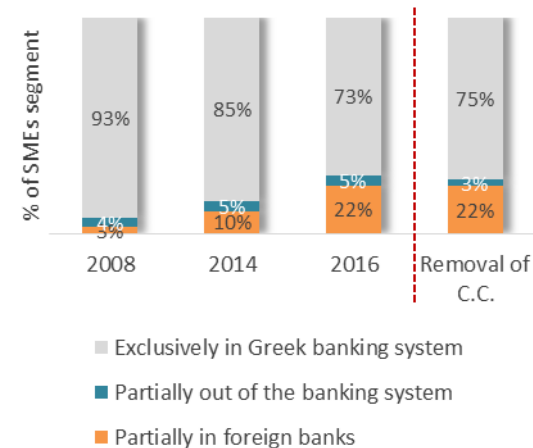
Cash reserves strategy: Sizes* 1 - 2



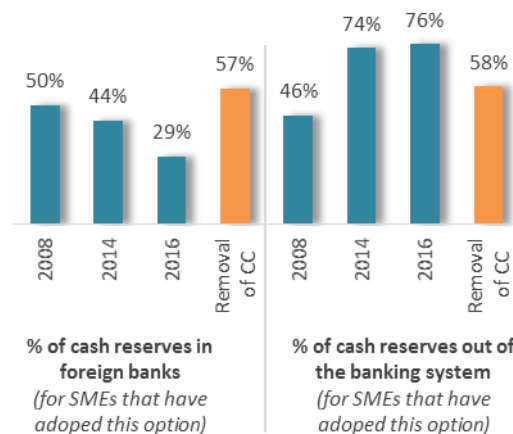
Cash reserves strategy: Sizes* 3 - 4



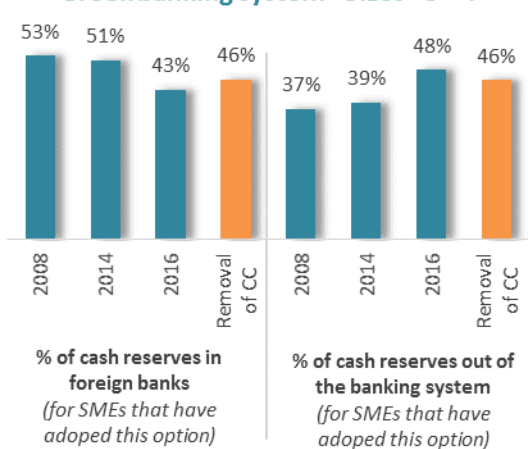
Cash reserves strategy: Sizes* 5 - 6



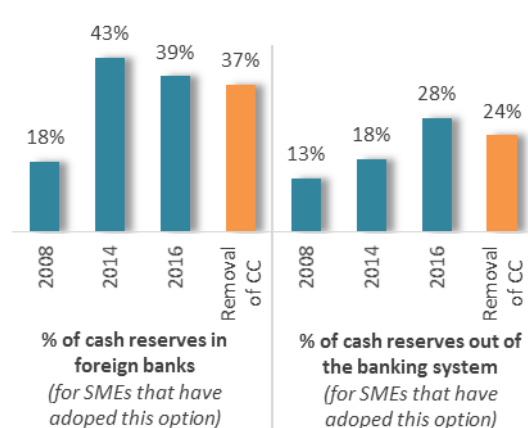
Share of cash reserves out of the Greek banking system - Sizes* 1 - 2



Share of cash reserves out of the Greek banking system - Sizes* 3 - 4



Share of cash reserves out of the Greek banking system - Sizes* 5 - 6

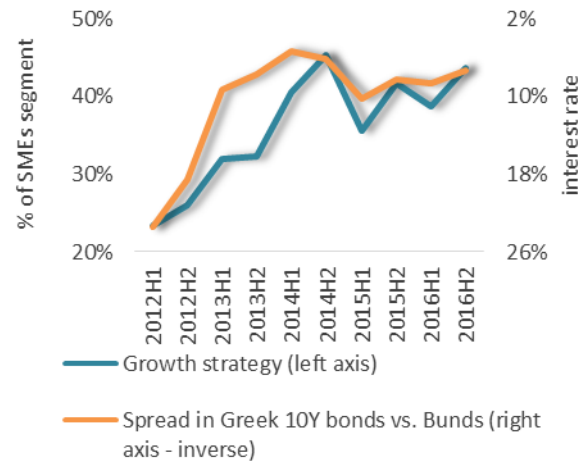


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The quick removal of capital controls (i) is of vital importance so as to avert structural problems in SMEs, (ii) poses a relatively small risk as entrepreneurs state they will not rush to withdraw their deposits, and (iii) will unlock investments of nearly €1 billion

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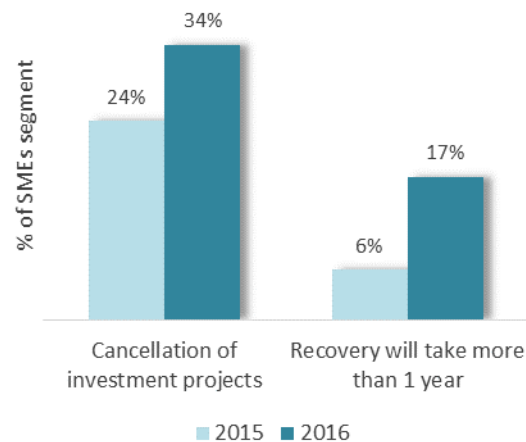
Medium-term SMEs outlook



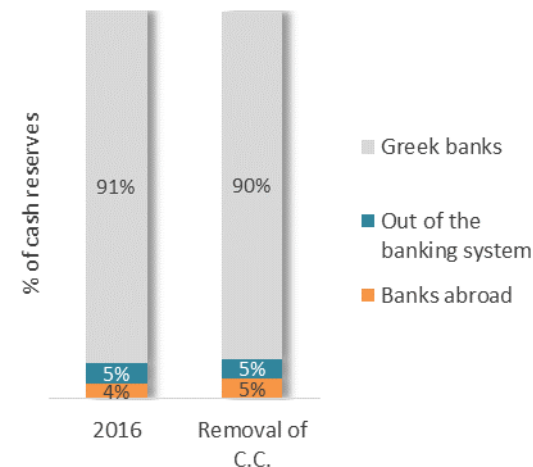
Source: Eurostat, NBG estimates

- The gradual restoration of stability conditions, as reflected in the spreads between Greek and German bond yields (7 per cent by the end of 2016 compared with 23 per cent at the beginning of 2012), is helping to restore confidence and dynamism of SMEs – with 44 per cent of the segment stating growth strategies in 2016, up from 23 per cent in 2012.
- At the same time, however, the need to remove capital controls soon is imperative since they are impacting the medium-term strategy of SMEs, lengthening the process of returning to normality once they are removed (17 per cent of SMEs estimate that they need more than one year, compared with 6 per cent in 2015). By contrast, a strategy to relax capital controls appears to present only a small risk, as entrepreneurs across all sectors state they will not rush to withdraw their deposits, keeping the share of cash reserves held in Greek banks close to their current levels (about 90 per cent).
- The removal of capital controls would likely encourage 1/3 of SMEs to restart “frozen” investment plans over a six-month horizon. Assuming similar behaviour as in the past 15 years (with investments at 3 per cent-4 per cent of sales), new investments are expected to be close to €1 billion.

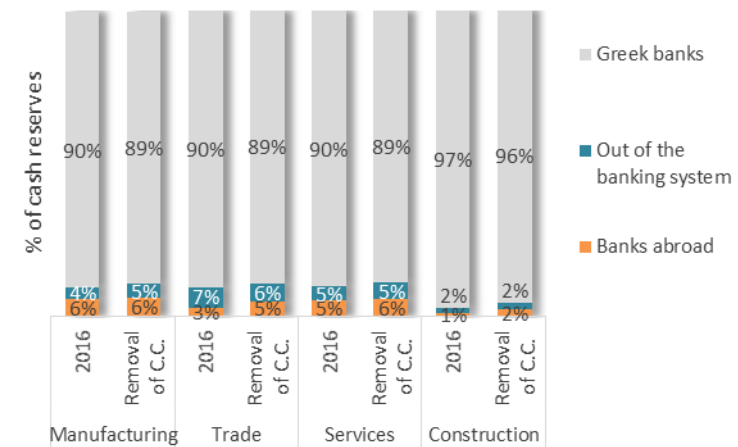
Effects from the capital controls



Cash reserves strategy



Cash reserves strategy per sector



❑ Business conditions

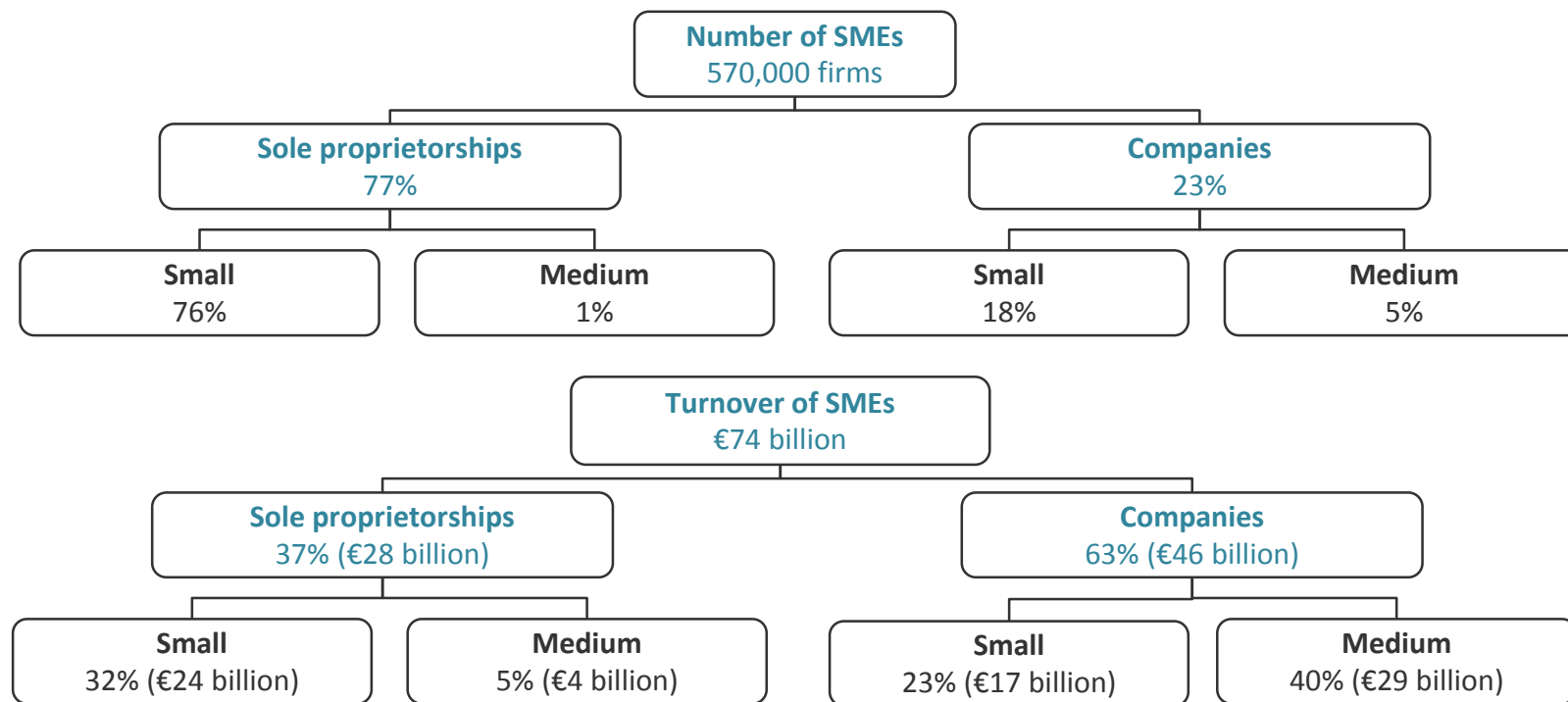
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** For the purposes of the survey, **small** enterprises are those reporting turnover of less than €1 million and **medium-sized** enterprises are those reporting turnover of between €1 million and €10 million.*

Source: SBA Factsheet 2015, Eurostat, EL.STAT Company Register, NBG Estimates

- ❑ The circa 570,000 SMEs in Greece generate turnover of around €74 billion.
- ❑ 4/5 of SMEs are sole proprietorships, which account for a corresponding share of the total domestic business sector (compared with just ½ of the business sector in Europe).
- ❑ Although sole proprietorships comprise the majority of SMEs, the greater share of turnover (over 60%) is generated by companies of various legal status (SA, limited partnership, limited liability, etc.).

Sample Description

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Sample Structure* (number of companies)						Greek SMEs Segment Structure* (based on turnover)					
Turnover (in millions €)	Manufacturing	Services	Trade	Construction	Total SMEs	Turnover (in millions €)	Manufacturing	Services	Trade	Construction	Total SMEs
1: (0 - 0,1]	45	73	45	30	193	1: (0 - 0,1]	1%	5%	2%	1%	9%
2: (0.1 - 0,5]	45	73	45	30	193	2: (0.1 - 0,5]	3%	6%	12%	1%	22%
3: (0.5 - 1]	45	74	45	30	194	3: (0.5 - 1]	2%	3%	9%	1%	15%
4: (1 - 2,5]	45	74	45	30	194	4: (1 - 2,5]	3%	3%	11%	1%	18%
5: (2,5 - 5]	45	73	45	30	193	5: (2,5 - 5]	4%	4%	8%	1%	17%
6: (5 - 10]	45	73	45	30	193	6: (5 - 10]	4%	4%	9%	2%	19%
Total SMEs	270	440	270	180	1160	Total SMEs	17%	25%	51%	7%	100%

* Depending on data availability, there is possible deviation of 10%

* Weighted average of the past decade

Source: EL.STAT. Company Register (2007), ICAP Data, Eurostat, NBG Estimates

- ❑ Our survey examines a sample of enterprises with a turnover of below €10 million, which, for the purposes of the analysis, we define as small and medium-size enterprises (SMEs).
- ❑ Enterprises were selected using a stratified sampling method, in line with the standards of similar surveys carried out by international organizations. Specifically, a total of 1,164 enterprises were selected in such a way as to enable even distribution of the sample on the basis of two key factors: scale of turnover (6 scales) and sector of activity (Manufacturing, Trade, Services, Construction).
- ❑ In order to draw conclusions that are representative of the SME segment, answers were weighted according to the participation of each sub-set in the total turnover of the segment. Thus, findings were arranged (i) by size, (ii) by sector, and (iii) for the entire SME business sector. In line with the methodology, the segments are weighted on the basis of their shares in total turnover and not the number of enterprises.

- ❑ In order to construct a confidence index for SMEs, we included a number of basic questions regarding the level of business activity in the previous and in the coming half year. The model for the questions is based on the harmonized questionnaire recommended by the OECD and the European Commission, thereby enhancing the comparability of the index.
- ❑ The Index questions offer 3 alternative answers: increase (+), no change (=), decrease (-), or above normal (+), normal (=), below normal (-). To begin with, we convert the number of answers per category (+,=,-) to percentages and then we calculate the net result by subtracting the (-) from the (+) percentage. Last, the confidence index for each sector is the average of the net results for the following questions:
 - ✓ For **manufacturing**: The level of orders, inventories, and future production trend.
 - ✓ For **services**: The business situation of the firm in the previous half year, past and future demand trend.
 - ✓ For **trade**: Level of inventories, past and future demand.
 - ✓ For **construction**: Level of backlog, and future employment trend.
- ❑ For the SME sector, the business confidence index has been estimated as a weighted average of its subsectors (the weights being the shares of the sectors' turnover in the economy).
- ❑ By carrying out the survey on a regular 6-month basis we should be able to form a picture of SMEs' course over time, as reflected in the index. To draw reliable conclusions, comparison will be made between the current index level and its long-term average (so as to correct possible over-optimism or over-pessimism bias).
- ❑ The evolution of the confidence index (and any other reviews over the course of time) does not take into account the closing of companies, just the developments regarding enterprises operating during the period this survey is carried out.

- ❑ Company: TNS
- ❑ Methodology: Quantitative research in the form of Computer Aided Telephone Interviewing - C.A.T.I., using a 20-minute structured questionnaire.
- ❑ Sample: A total of 1160 interviews were conducted (960 within the context of the current assessment plus 200 booster interviews with SME logistic firms):
 - ✓ 480 enterprises with annual turnover up to EUR 1 million (freelancers, sole proprietorships, unlimited partnerships, limited partnerships, limited liability companies, SAs) - 100 of which are vehicle logistics companies
 - ✓ 480 enterprises with annual turnover between EUR 1 million and 10 million (unlimited partnerships, limited partnerships, SAs, limited liability companies) - 100 of which are vehicle logistics companies
- ❑ Geographical coverage:
 - ✓ Athens, Thessaloniki, Heraklion, Ioannina, Kavala, Larissa, Patras
- ❑ Sampling: multi-stage, stratified, non-proportional sampling for sector, turnover size & geographical area in each of the two sets of samples. Quotas relating to turnover and for the booster sample.
- ❑ Statistical error: in each of the two sets of samples of 480 enterprises the maximum statistical error is estimated at +/- 4.15% at a 95% confidence level.
- ❑ Period of survey: 03/10/2016 - 03/11/2016
- ❑ Survey framework: The survey was carried out in line with ESOMAR and SEDEA (Association of Greek Market and Opinion Research Companies) codes of conduct and the quality control requirements set by PESS (Quality Control in Data Collection). A total of 39 researchers and 2 reviewers with experience and know-how in business surveys participated in the field research.



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Economic Analysis Department

Survey of Greek SMEs: H2:2016

Special Issue: Capital Controls

Coordinator:

Jessie Voumvaki

Senior Economist, Head of Entrepreneurship and Business Analysis

(+30210) 334 1549

e-mail: fvoumv@nbg.gr

Analysts:

Athanasia Koutouzou

Economist, Entrepreneurship and Business Analysis

(+30210) 334 1528

e-mail: koutouzou.ath@nbg.gr

Georgios Sakkas

Economist, Entrepreneurship and Business Analysis

(+30210) 334 1547

e-mail: sakkas.georgios@nbg.gr

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