



ΟΙΤΕΚ

ΟΜΙΑΟΣ
ΠΡΟΒΛΗΜΑΤΙΣΜΟΥ
ΓΙΑ ΤΟΝ
ΕΚΣΥΓΧΡΟΝΙΣΜΟ ΤΗΣ
ΚΟΙΝΩΝΙΑΣ ΜΑΣ

GREECE AFTER THE CRISIS

Gikas A. Hardouvelis *

Athens, February 17, 2010
Chrysa Pagona **19:00**

***Ημερίδα ΟΠΕΚ,
«Οικονομική Κρίση: Μπορούμε να την υπερβούμε;»
Ακαδημίας 20, ΕΣΗΕΑ, ΑΘΗΝΑ***

**** Professor, Department of Banking and Financial Management, Un. of Piraeus
Chief Economist, Eurobank EFG Group***

GREECE AFTER THE CRISIS

MAIN THEMES

- I. IS THE INTERNATIONAL FINANCIAL CRISIS OVER?**
- II. THE SPECIAL GREEK PROBLEMS**
- III. CONCLUSION**

I.

IS THE INTERNATIONAL FINANCIAL CRISIS OVER?

❖ **Yes, but risks remain**

I.1 Consensus Output Forecasts for 2010

Real GDP

	2008	2009f	2010f
USA	0.4	-2.4	2.7
Euro area	0.6	-4.0	1.2
Japan	-1.2	-5.0	1.4
China	9.6	8.7	9.5
Brazil	5.1	0.2	4.8
Russia	5.6	-7.9	3.2
India	7.5	6.6	7.7
Greece	2.0	-2.0	- ?
Bulgaria	6.0	-5.9	-1.1
Poland	5.0	1.3	2.0
Romania	6.2	-7.5	0.5
Serbia	5.5	-3.5	1.5
Turkey	0.9	-5.5	3.0

- ✓ Recovery almost everywhere
- ✓ Stronger recovery in the US
- ✓ Sluggish recovery in our region, with Turkey showing the best prospects
- ✓ We avoided a repetition of the 1930's by transferring the associated costs in the future

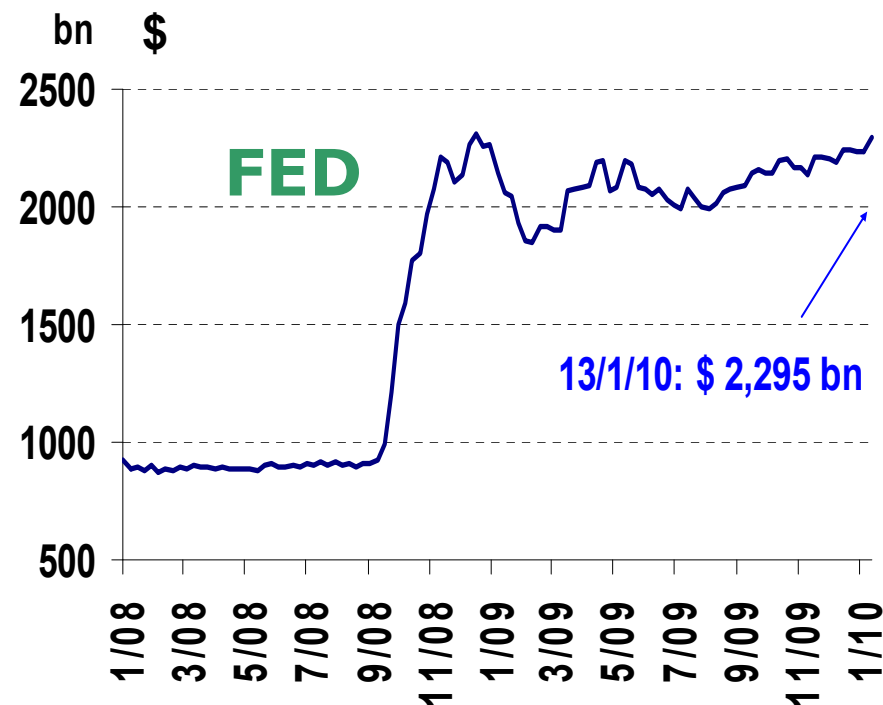
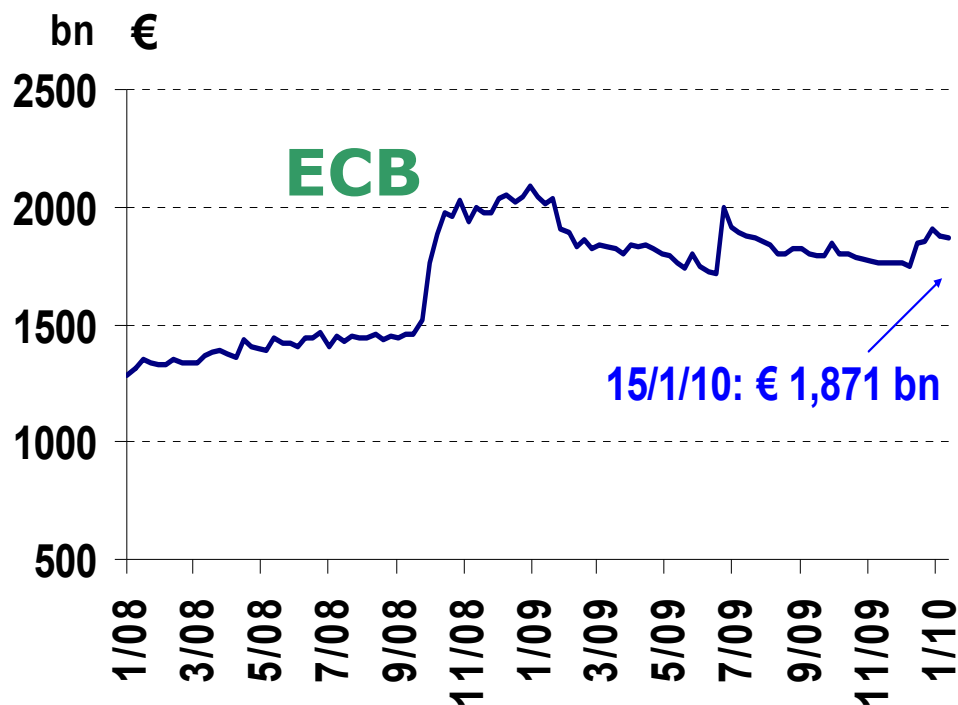
I.1 Consensus forecasts: Policy rates

Policy Rates	2009	Current	Q1 10f	Q2 10f	Q3 10f	Q4 10f
US	0.00-0.25	0.00-0.25	0.00-0.25	0.00-0.25	0.50	0.75
Euro Area	1.00	1.00	1.00	1.00	1.00	1.50
Japan	0.10	0.10	0.10	0.10	0.10	0.10
China	5.30	5.30	5.30	5.60	5.85	5.85
India	4.75	4.75	4.75	5.00	5.50	6.25
Russia	8.75	8.75	8.50	8.50	8.50	8.50
Brazil	8.75	8.75	8.75	9.25	10.5	11.25

* Bloomberg Survey, end-of quarter forecasts

I.1 Is the crisis over? The main risk of early liquidity withdrawal

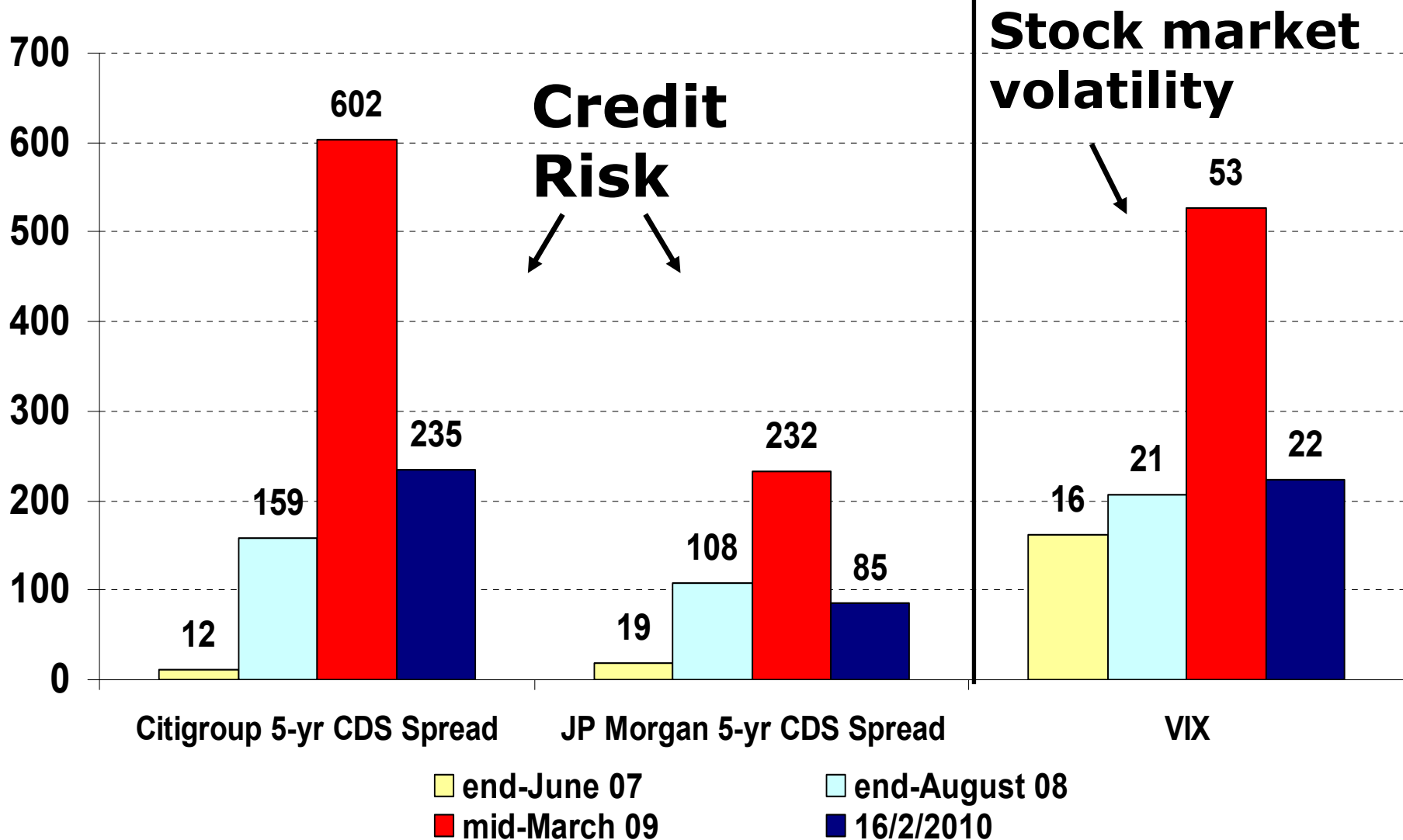
Central bank balance sheets



Source: ECB, Federal Reserve

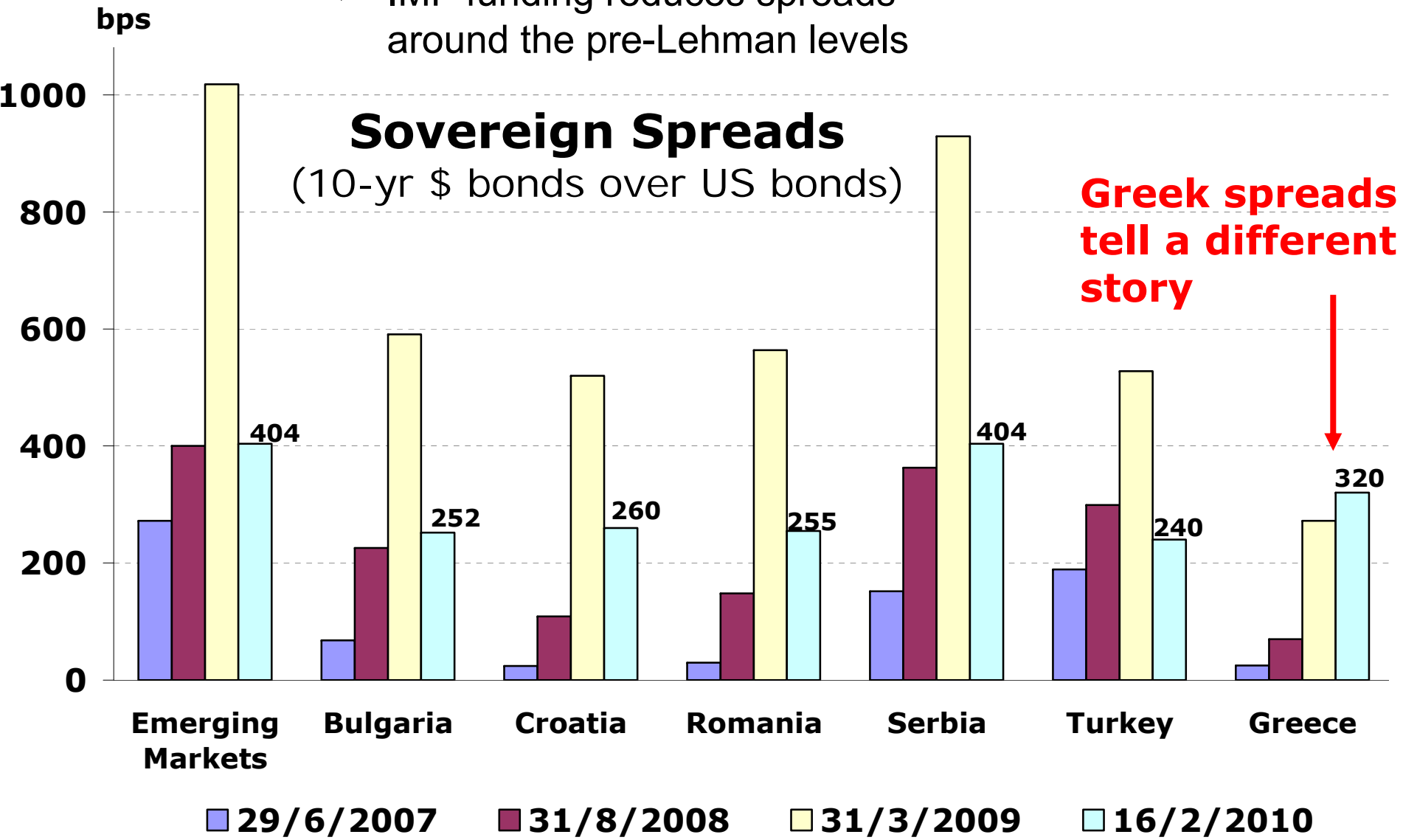
- ✓ Central banks decreased their intervention rates and pioneered new ways to provide liquidity, especially post-Lehman (quantitative & qualitative easing).
- ✓ Recovery depends on the continuing support by central banks and governments
- ✓ ECB is more conservative than the Fed, will likely withdraw liquidity sooner

I.2 Is the crisis over? Spreads down but not at pre-crisis levels

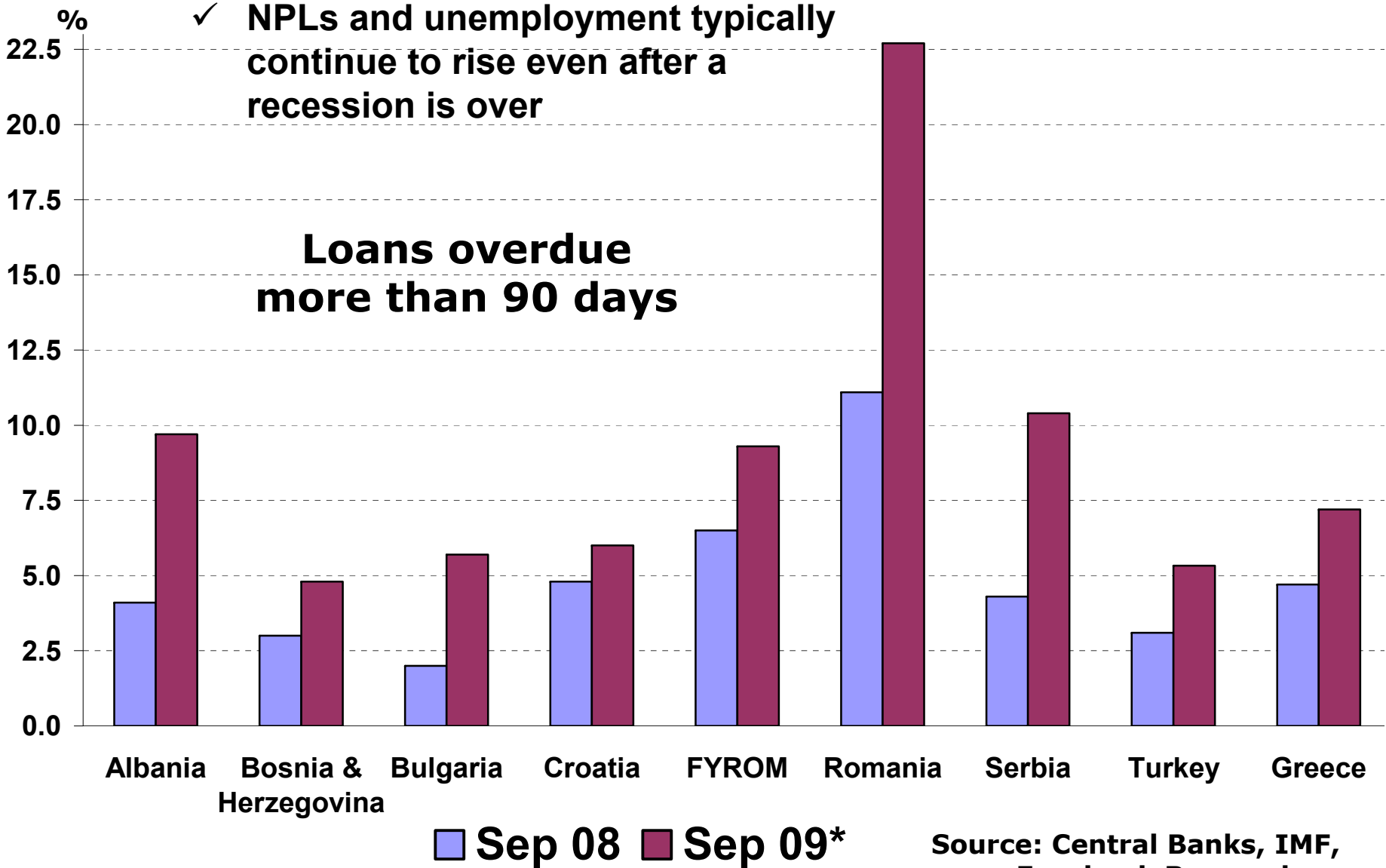


I.2 Is the crisis over in our region?

✓ IMF funding reduces spreads around the pre-Lehman levels



I.2 Is the crisis over? The rise in NPLs

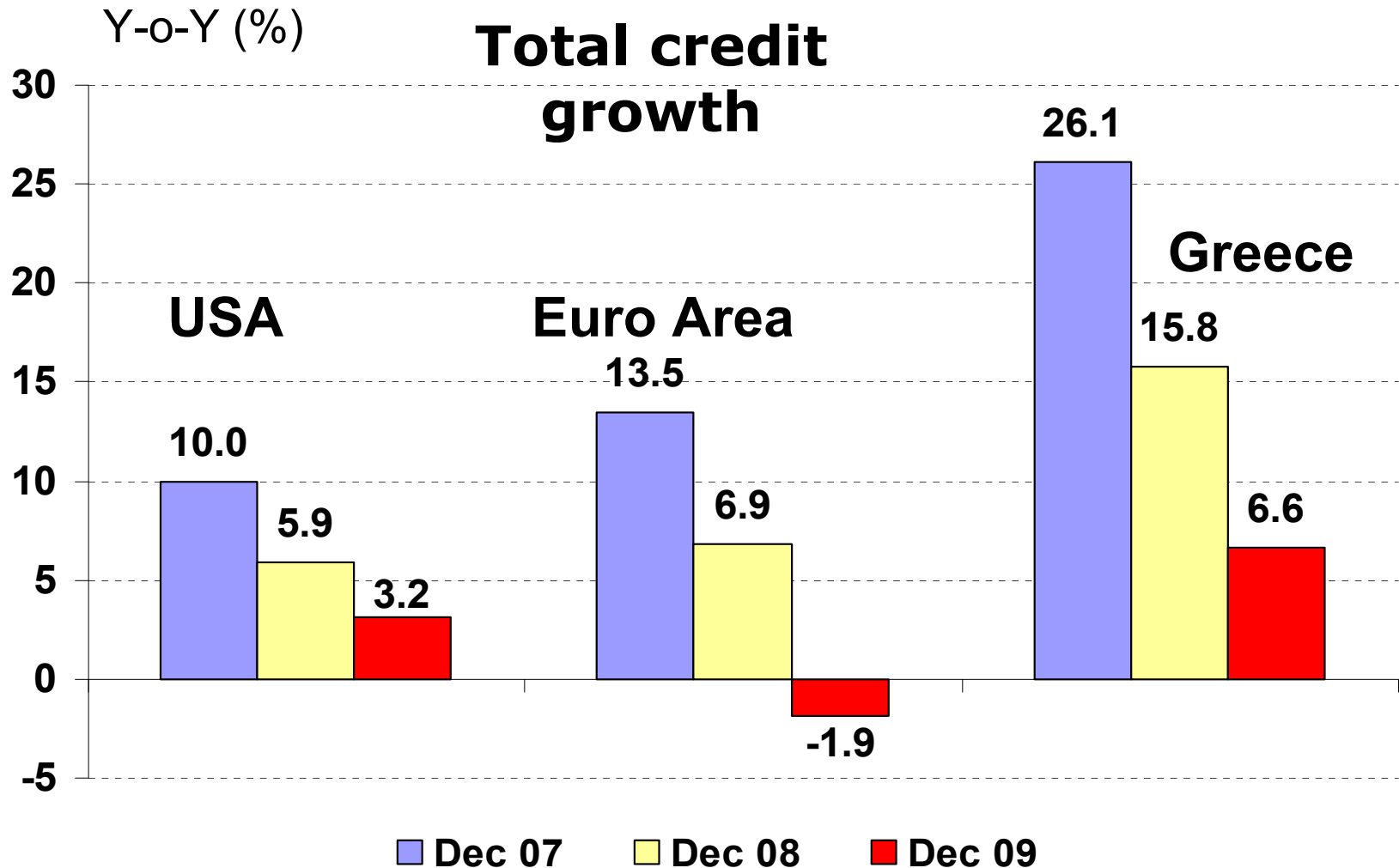


II.

THE SPECIAL GREEK PROBLEMS

- 1) The imported international crisis**
- 2) Greece faces two major idiosyncratic risks**
 - i. Lack of Competitiveness**
 - ii. Fiscal laxity**
- 3) A gloomy view from the outside**
- 4) Greek SGP and the view forward**
- 5) Can the economy recover?**

II.1 Credit growth still positive in Greece ...

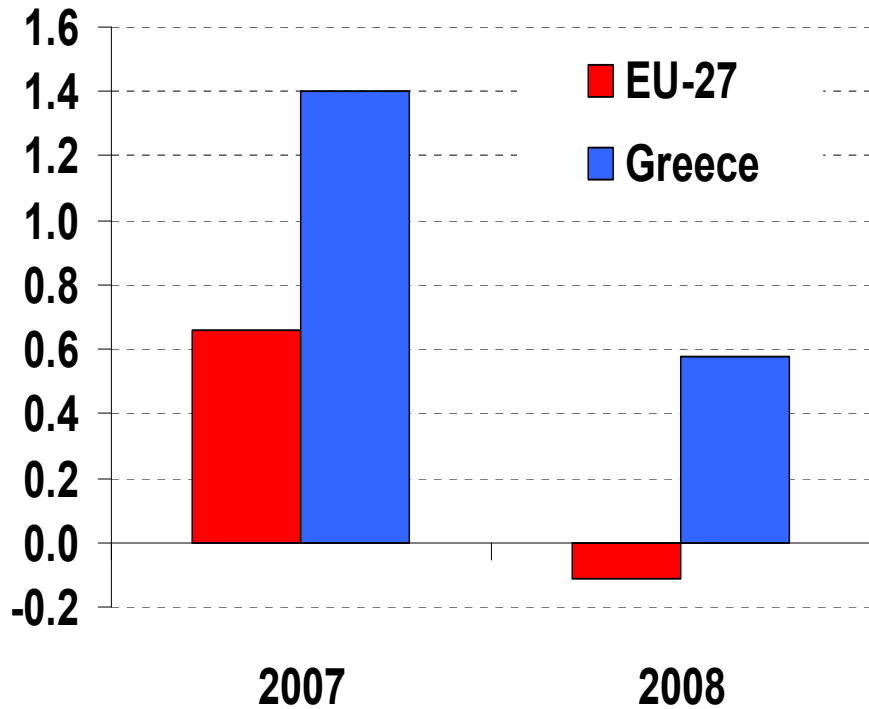


Source: ECB, Fed

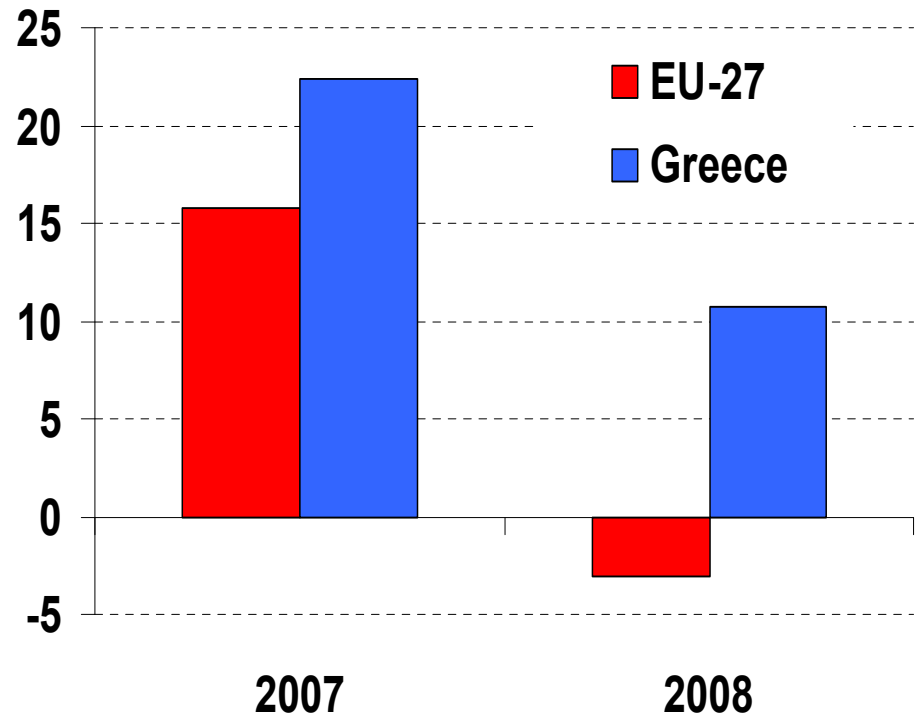
II.1 ... as Greek banks, unlike US & European FIs, remained strong

✓ Less of a problem in Greece relative to EU-27

Return On Assets



Return On Equity



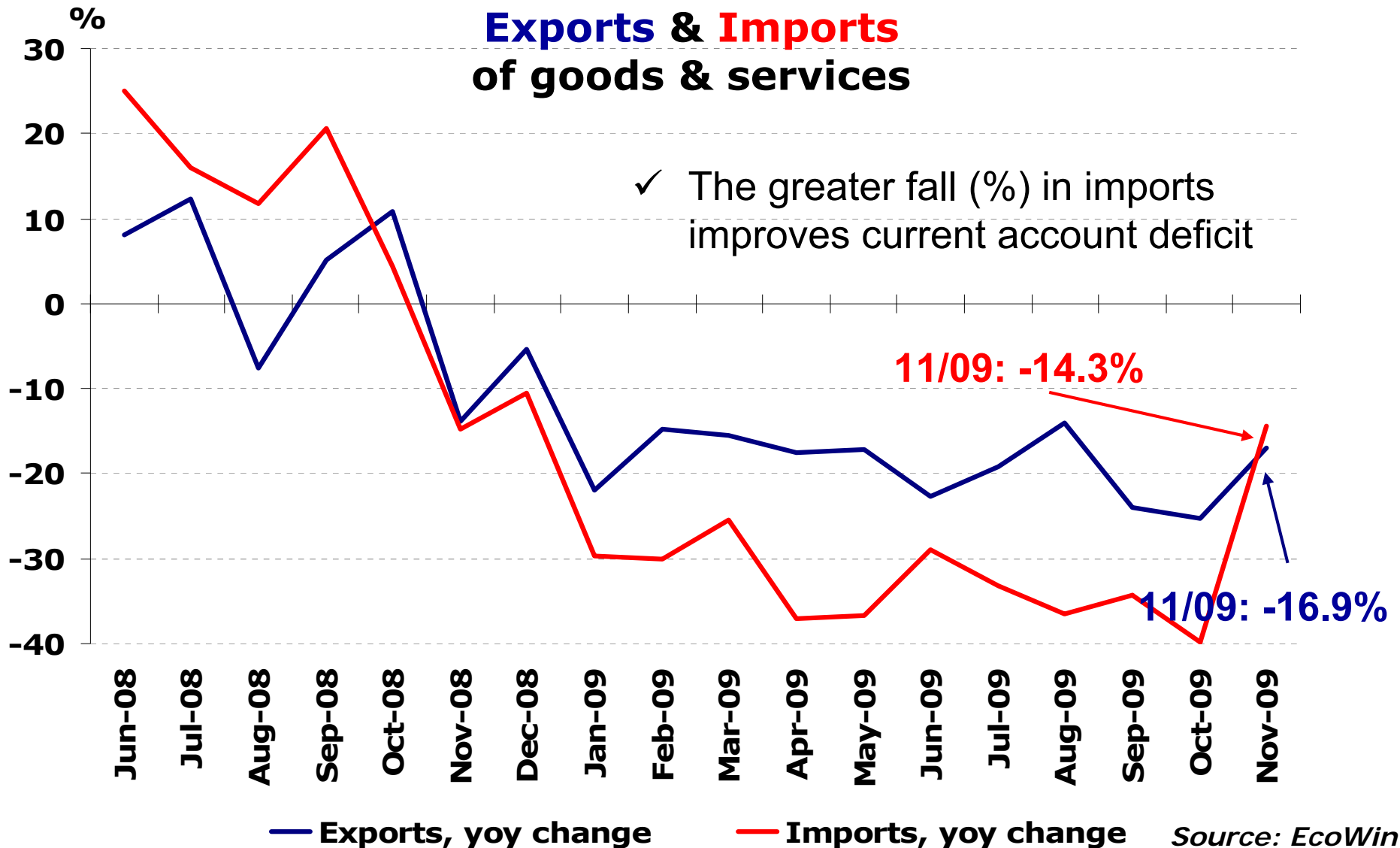
Source: ECB

Bank Groups in Greece

	1H 2008	1H 2009
ROA	1.1	0.5
ROE	15.7	7.7

Source: Bank of Greece

II.1 Greece: Collapse of Trade in Q4-2008



II.2 Ease of Doing Business rankings reveal lack of competitiveness

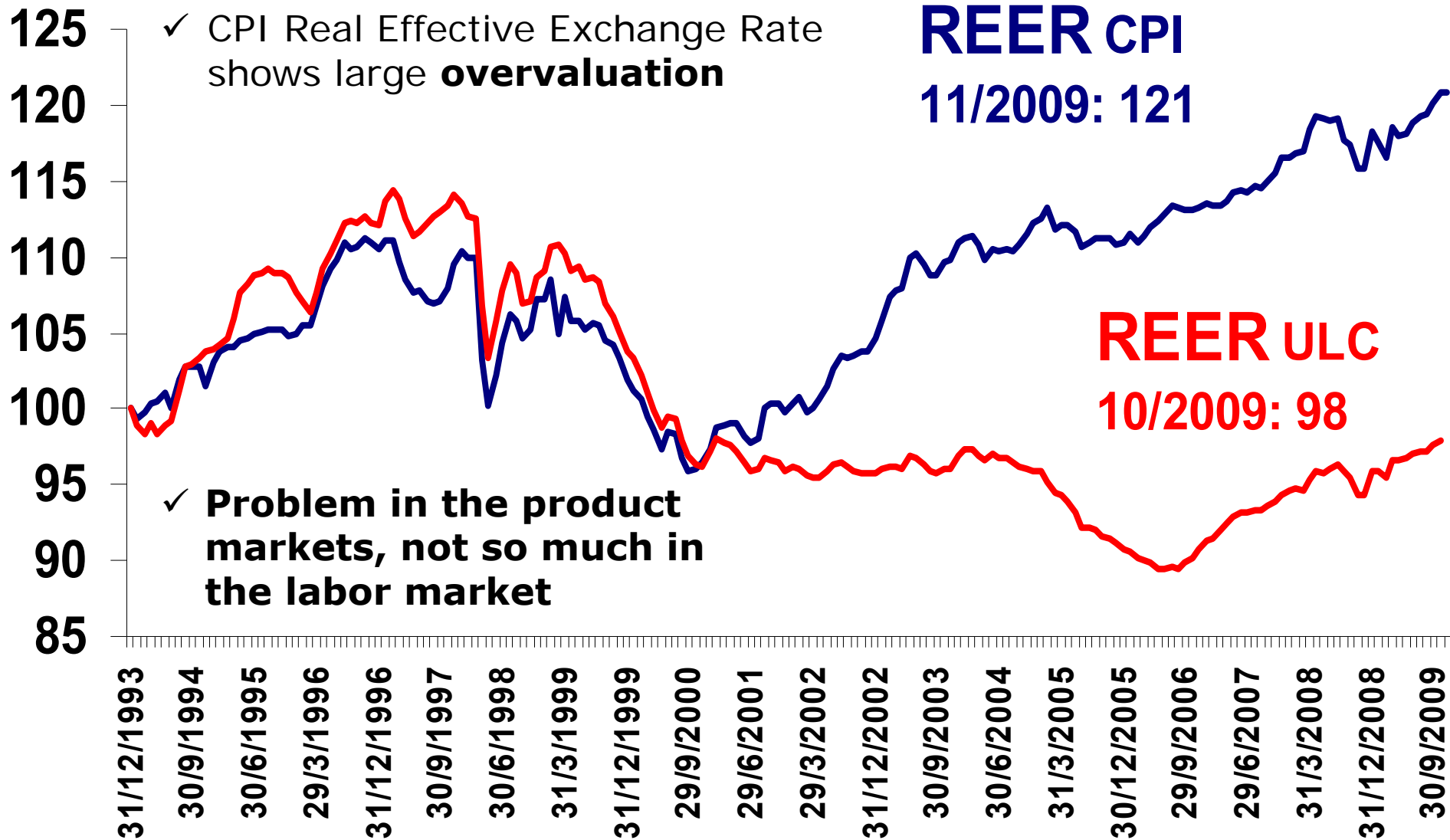
➤ World Bank:

In 2009 Greece ranked 109th out of 183 countries

	Rank	Starting a business (days)	Difficulty of hiring (0-100)	Protecting Investors (0-10)	Exporting Goods (days)	Paying Taxes (hours per year)
Greece	109	19	44	3.3	20	224
OECD		13	26.4	5.8	10.5	194.1
Portugal	48	6	33	6	16	328
Czech Rep.	74	15	33	5	17	613
Turkey	73	6	44	5.7	14	223
Bulgaria	44	18	17	6	23	616
Romania	55	10	67	6	12	202

Source: World Bank *Ease of doing business 2010*

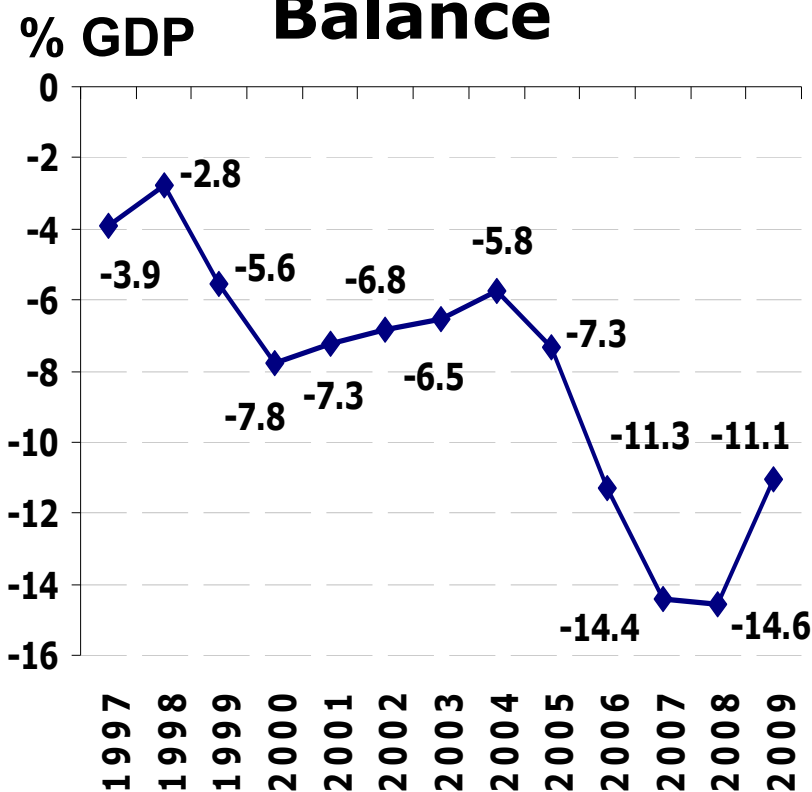
II.2 Price Competitiveness declines post-EMU



Source: IMF, IFS

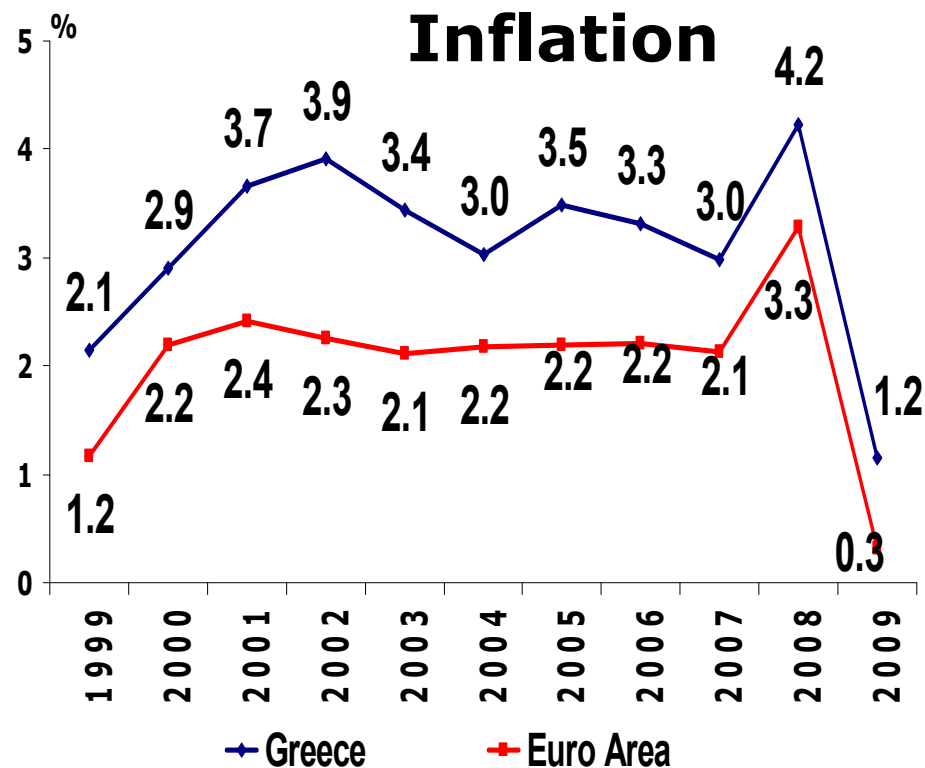
II.2 Lack of competitiveness shows up in current account as well as in inflation differential

Current Account Balance



Source: Bank of Greece

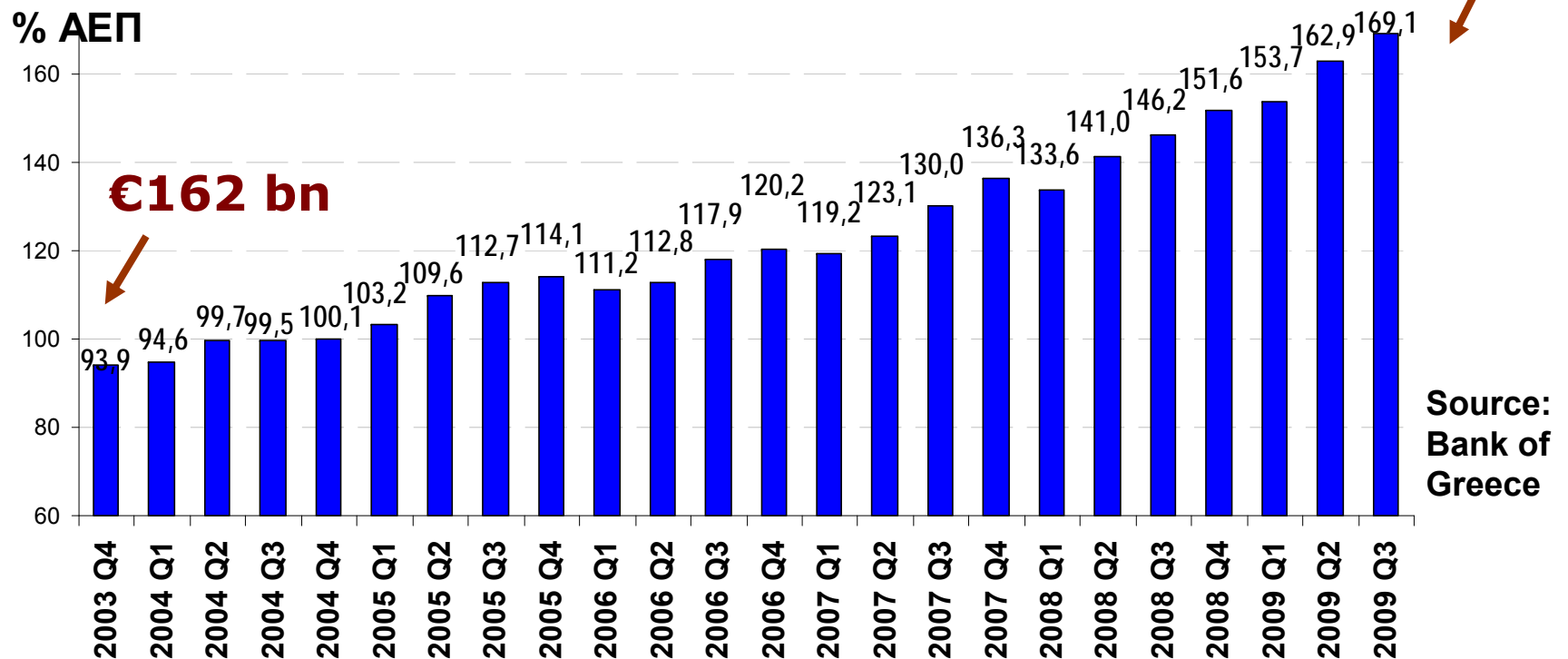
✓ In every single month, inflation in Greece was higher than the Euro Area average



Source: European Commission

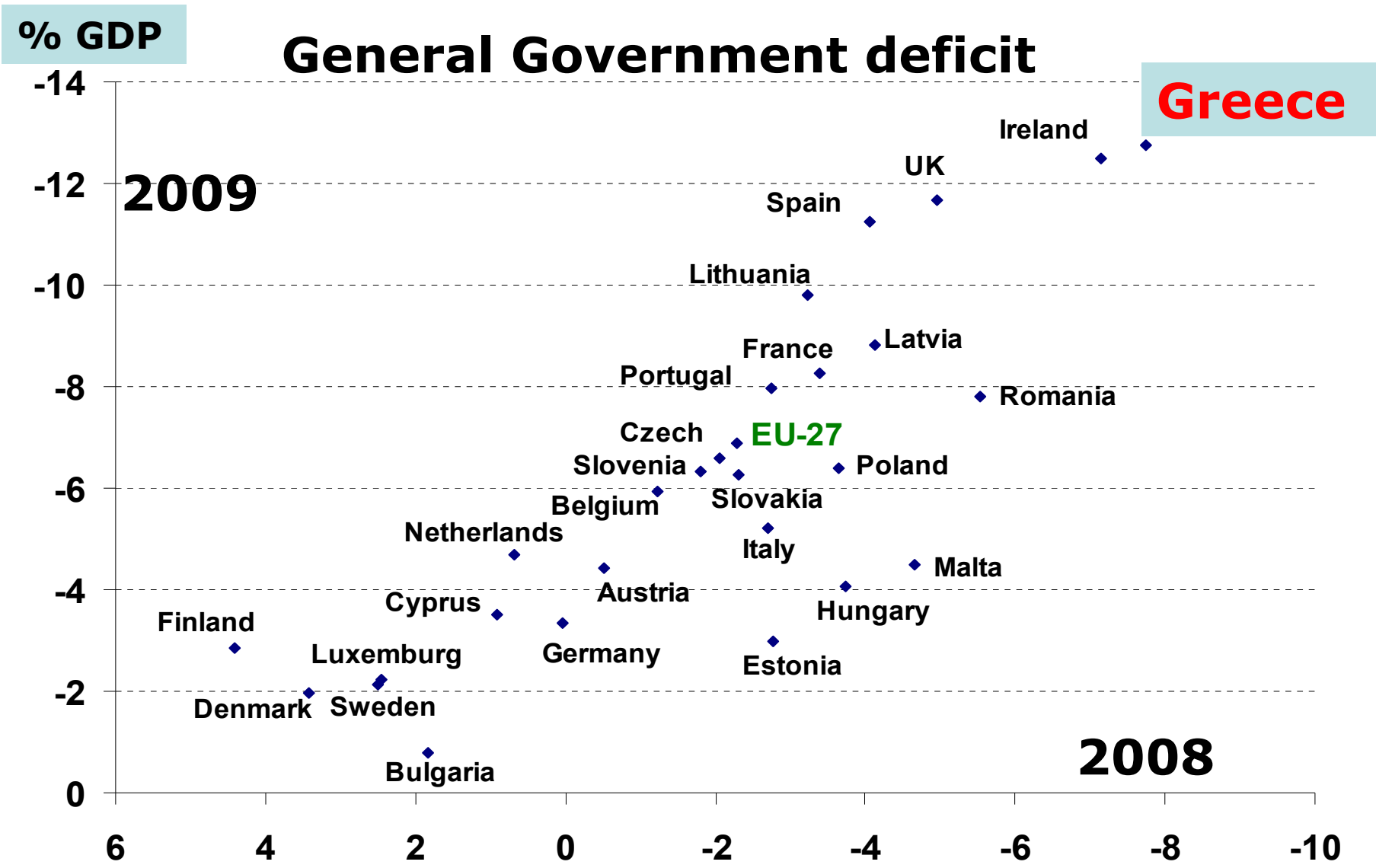
II.2 External debt shoots up

- ✓ The competitiveness deterioration is the deepest problem
- ✓ It also shows up in the post-EMU current account deficits and the subsequent explosion of gross External Debt
- ✓ **The country lives way beyond its means**



- ✓ The 6-year rise in external debt was more than 75 pp of GDP or €244 bn
- ✓ In order to maintain our standards of living we “sold” the equivalent of a city the size of Thessalonica.

II.2 Fiscal laxity is the second problem: Greek government deficits were the worst in EU-27



II.2 Fiscal laxity became evident when growth stopped

✓ I believe the fiscal problem is a lot easier to solve, yet markets focus on this one



II.3 Credit Rating Agencies, 28/1/2010

Greece's sovereign credit rating (foreign currency LT debt)

Moody's	S&P	Fitch
Aaa	AAA	AAA
Aa1	AA+	AA+
Aa2	AA	AA
Aa3	AA-	AA-
A1	A+	A+
A2 (outlook: negative)	A	A
A3	A-	A-
Baa1	BBB+ (outlook: negative)	BBB+ (outlook: negative)
Baa2	BBB	BBB
Baa3	BBB-	BBB-
Ba1	BB+	BB+
Ba2	BB	BB
Ba3	BB-	
B1	B+	
B2	B	
B3	B-	
Caa1	CCC+	
Caa2	CCC	
Caa3	CCC-	
Ca	CC	
C	C	
WR	D	
	NR	

**ECB
line as
of Jan
2011**
↓

↑
**Current
temporary
ECB line**

✓ Downgrades by all three rating agencies in 2009
✓ S&P and Fitch are very harsh, bringing Greece down by two notches, perhaps becoming conservative from earlier failure to foresee the subprime problem

Note: Investment grade above dotted line

Source: Bloomberg

II.3 Better ratings will be slow to come

- ✓ Continuous upgrades
1994-2003:

BBB- → **A+**

- ✓ First downgrade in 2004
- ✓ In 2009, downgrades associated with **negative outlooks** FITCH και S&P (-2 steps), MOODY'S (-1 step)

	S&P	MOODY'S	FITCH
2009	BBB+	A2	BBB+
2008	A	A1	A
2007	A	A1	A
2006	A	A1	A
2005	A	A1	A
2004	A	A1	A
2003	A+	A1	A+
2002	A	A1	A
2001	A	A2	A
2000	A-	A2	A-
1999	A-	A2	BBB+
1998	BBB	Baa1	BBB
1997	BBB-	Baa1	BBB
1996	BBB-	Baa1	BBB-
1995	BBB-	Baa3	BBB-
1994	BBB-	Baa3	
1993	BBB-		
1992	BBB-		

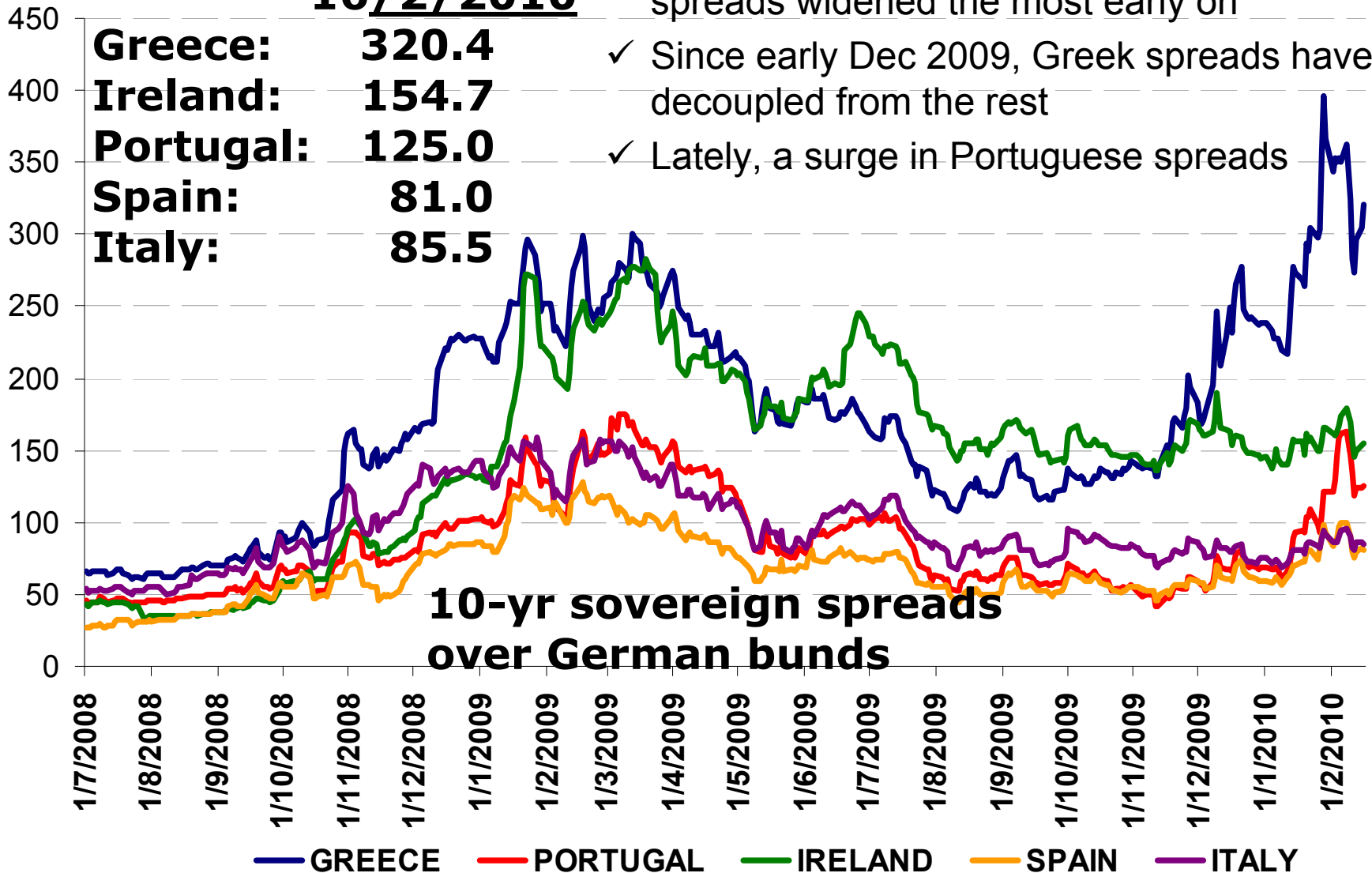
Source: Bloomberg

II.3 Greece: Pressure from bond spreads

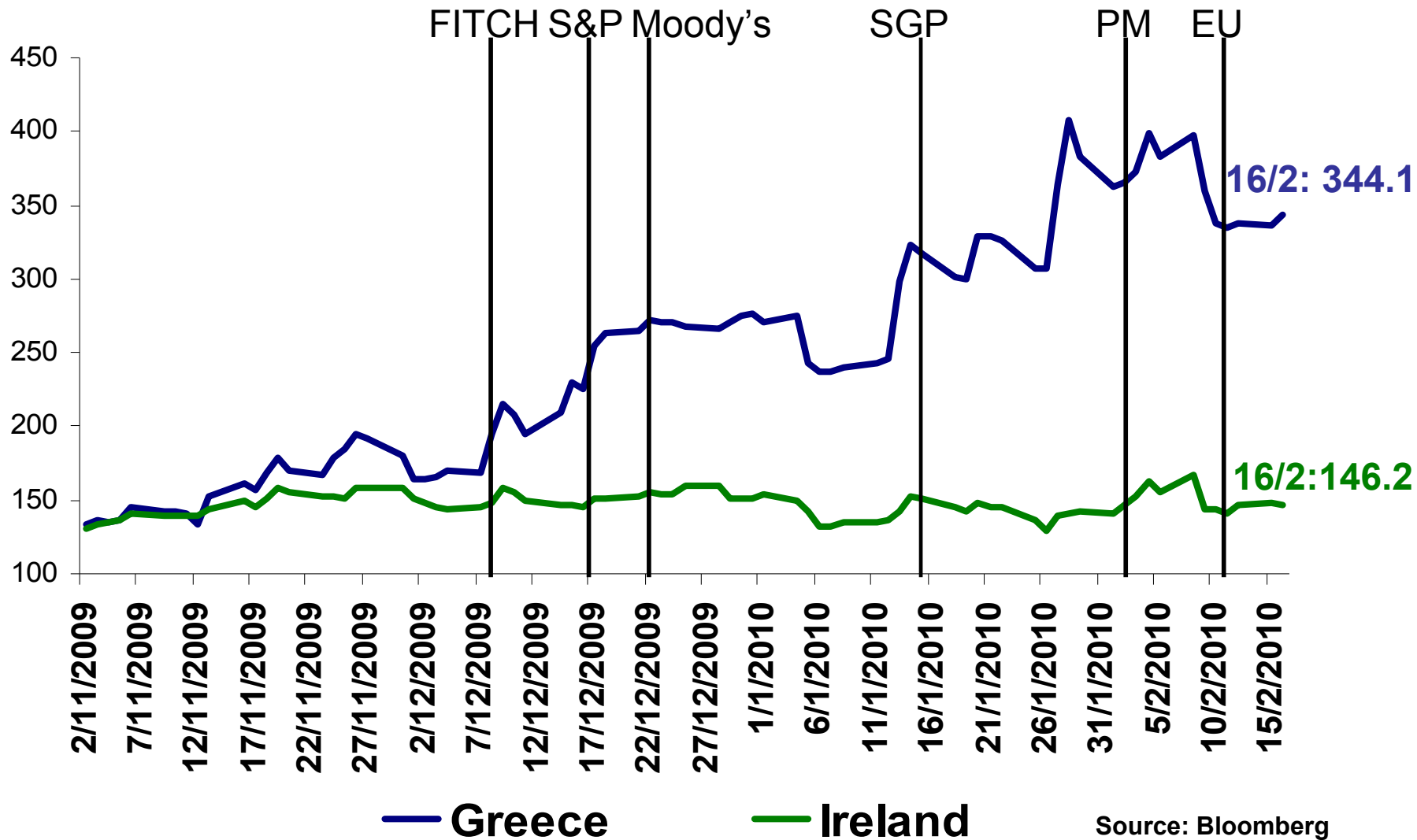
16/2/2010

Greece: 320.4
Ireland: 154.7
Portugal: 125.0
Spain: 81.0
Italy: 85.5

- ✓ Despite a stronger banking system, Greek spreads widened the most early on
- ✓ Since early Dec 2009, Greek spreads have decoupled from the rest
- ✓ Lately, a surge in Portuguese spreads



II.3 Credit default swaps



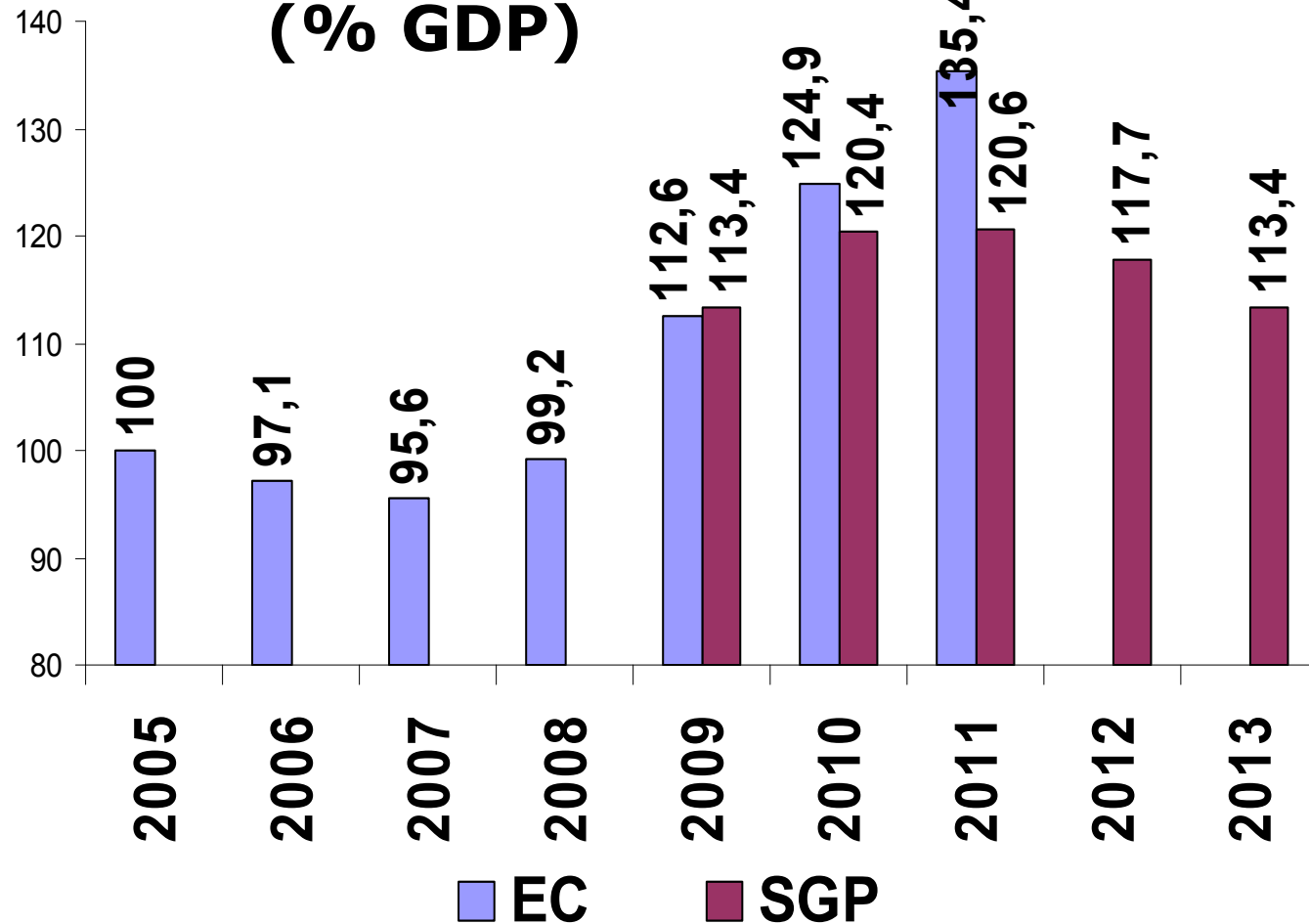
- ✓ The cost of protecting against Greece defaulting on its debt is \$344,100 annually for five years on \$10 mn of government bonds

II.4 Greek Stability & Growth Programme

	2009	2010	2011	2012	2013
		Baseline Scenario			
Real GDP	-1.2	-0.3	1.5	1.9	2.5
Nominal GDP	0.4	1.7	3.5	3.8	4.4
Unemployment (%)	9.0	9.9	10.5	10.5	10.3
General govnt balance (% GDP)	-12.7	-8.7	-5.6	-2.8	-2.0
Current account (%GDP)	-11.0	-8.1	-7.7	-6.9	-6.0
Private consumption	-1.5	-1.0	0.3	0.8	1.0
Public consumption	11.0	-4.4	-5.9	-5.9	0.7
Investment	-18.8	-1.6	4.5	5.5	8.4
Exports	-16.0	2.5	4.0	6.5	7.2
Imports	-24.7	-3.0	2.0	2.8	3.4
		Alternative Scenario			
Real GDP	-1.2	-0.8	1.0	1.5	2.0
Nominal GDP	0.4	1.1	2.8	3.3	3.6
Unemployment (%)	9.0	10.2	11.2	11.5	11.5
General govnt balance (% GDP)	-12.7	-8.7	-5.6	-2.8	-2.0
Current account (%GDP)	-11.0	-8.1	-7.6	-7.1	-6.4

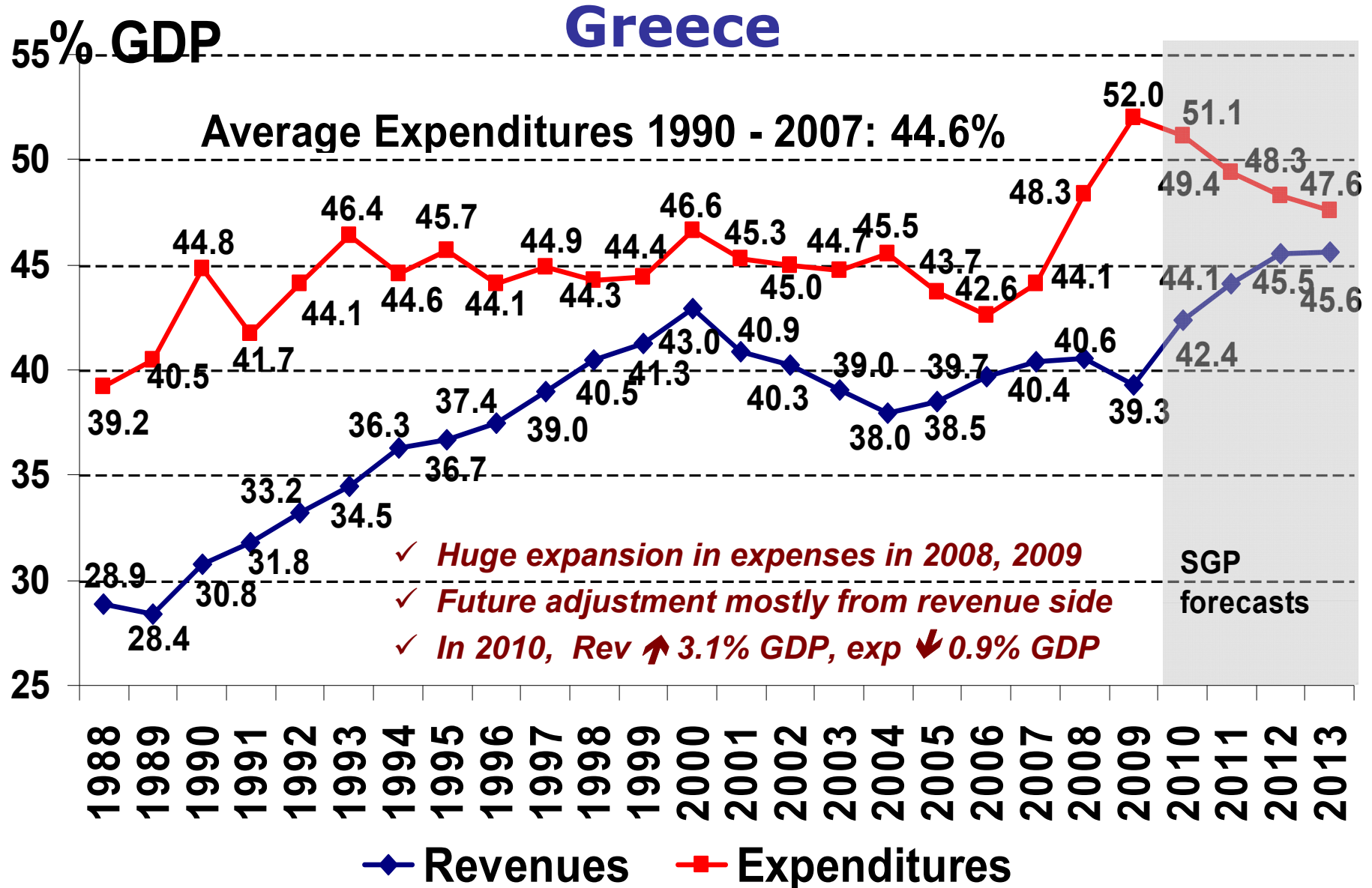
II.4 Greece's SGP tries to put a stop on run-away debt

Gross Public Debt (% GDP)

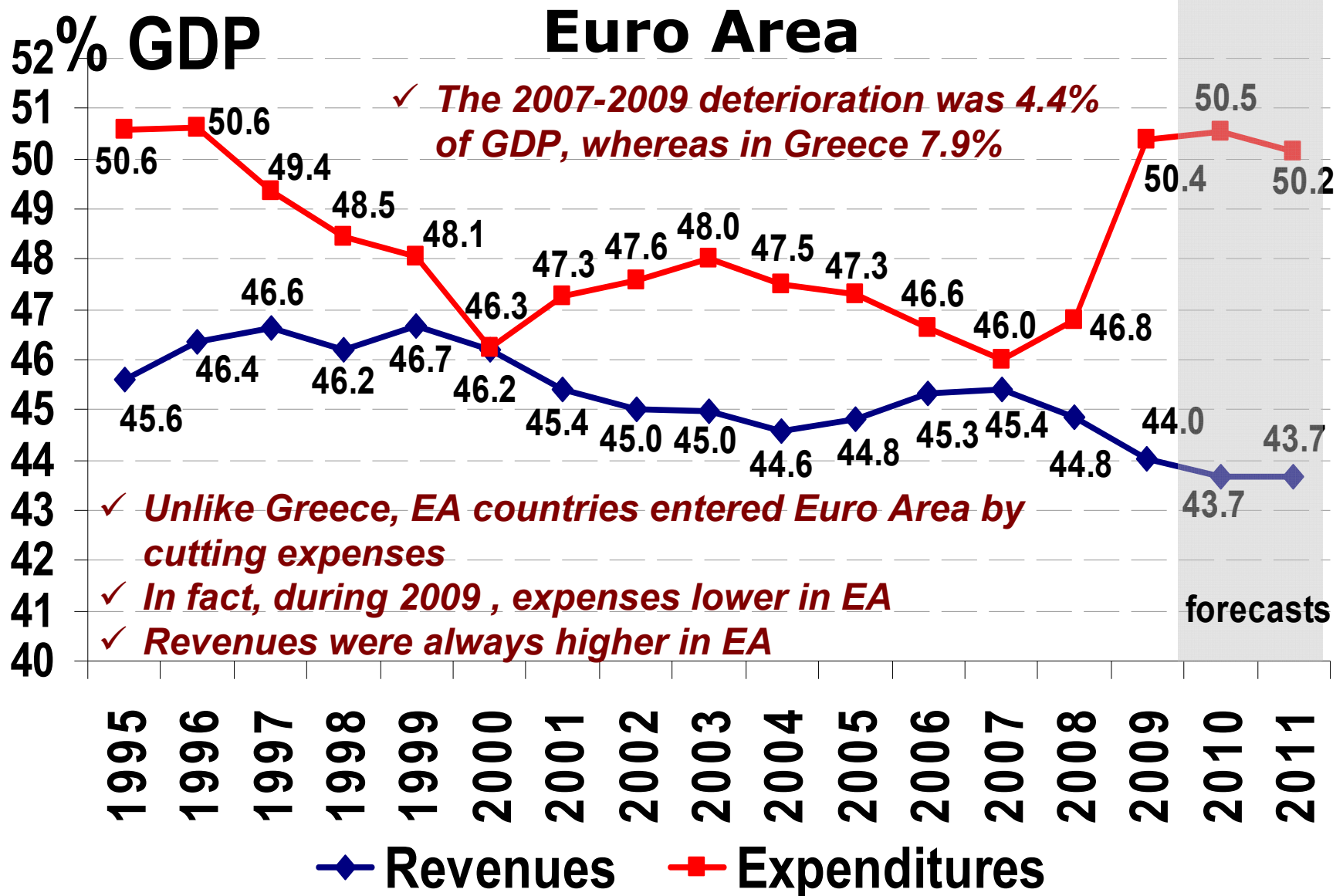


- ✓ EU Commission assumes no change in policy in its earlier forecasts
- ✓ SGP assumes effective new policies
- ✓ A successful SGP would make a big difference in the explosive dynamics of debt

II.4 SGP: General Government Revenues and Expenditures



II.4 Euro Area expenses also show deterioration in 2008, 2009



forecasts

II.5 So, how come everyone points to Greece?

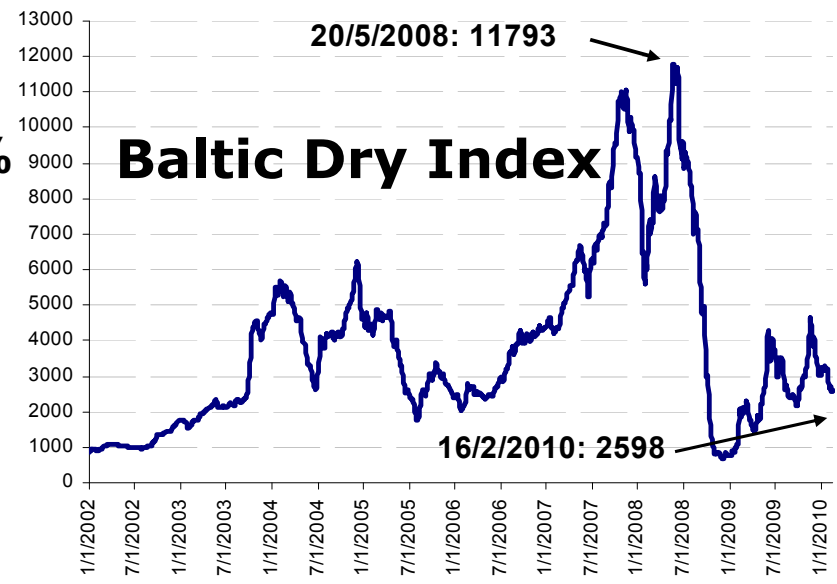
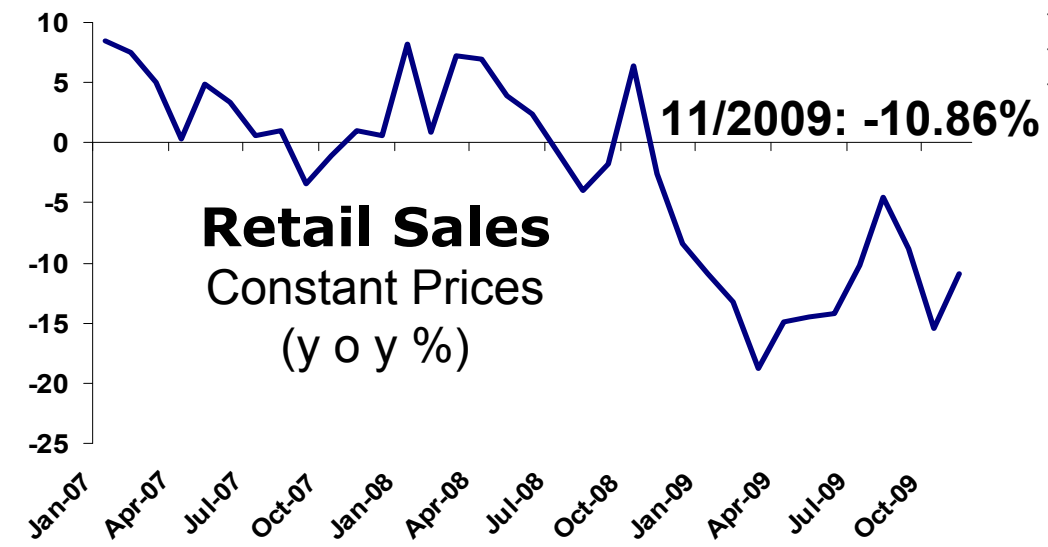
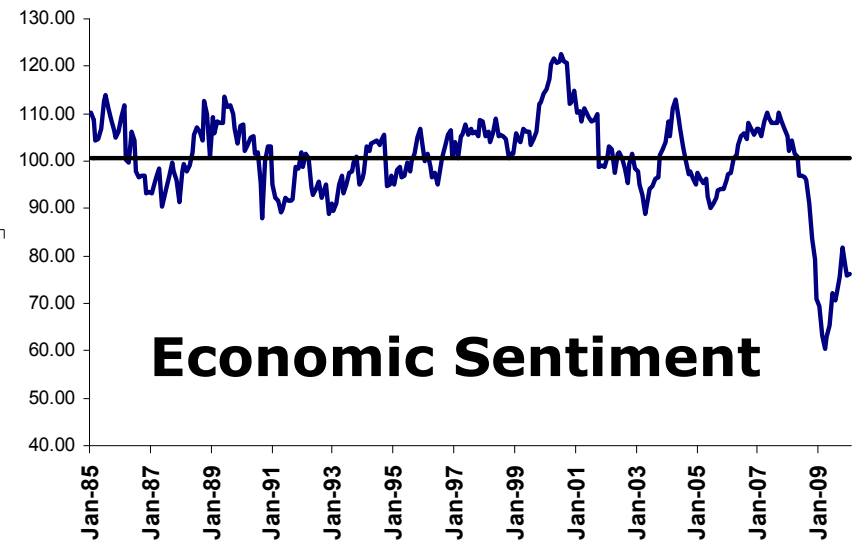
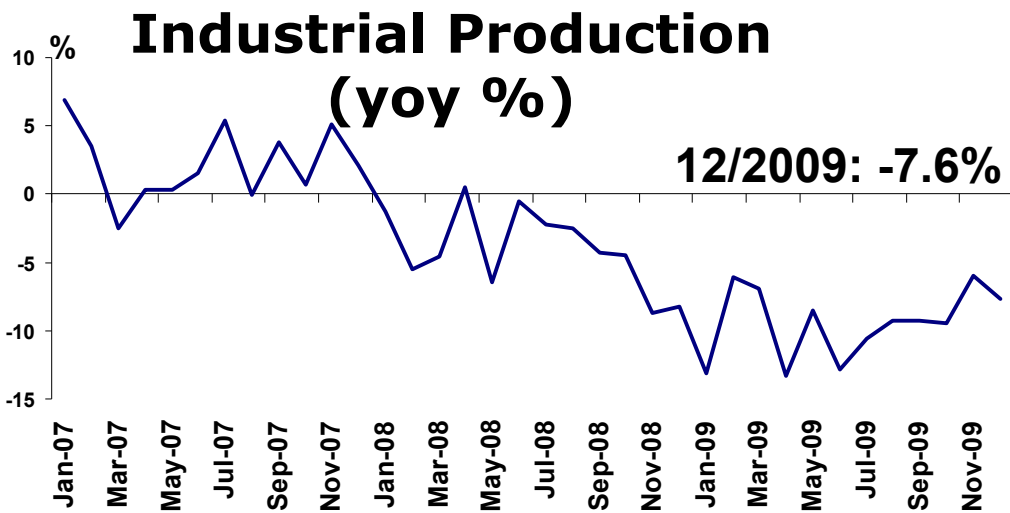
- ✓ *Greek deficits were the largest in 2008 and 2009*
- ✓ *Greek debt is second largest in EU-27 and was explosive*
- ✓ *Pension system future pressures bigger in Greece*
- ✓ *Lack of credibility of Greek fiscal statistics*

	Greece			
	2010	2020	2035	2060
Pension Expenditure (% GDP)	11.6	13.2	19.4	24.1
Pension system dependency ratio (%)*	56	59	78	102
	Euro Area			
	2010	2020	2035	2060
Pension Expenditure (% GDP)	11.2	11.6	13.2	13.9

* number of pensioners relative to the number of contributors in public pension schemes

Source: European Commission 2009

II.5 Will Greece recover?



II.5 Greek GDP Growth and Debt Forecasts

Greece - GDP Growth (%)	2010	2011	2012	2013
Plan A - SGP	-0.3	1.5	1.9	2.5
Plan B - SGP	-0.8	1.0	1.5	2.0
Feasible*	-1.3	0.5	1.0	1.5

* Under the assumption the Greek crisis will not prolong

Greece - Debt (%GDP)	2010	2011	2012	2013
SGP (Plan A & B)	120.4	120.6	117.7	113.4
Feasible*	122.8	127.2	128.3	127.8

* Without new additions from calling to honor past guarantees of €26 bn

✓ **The risks are high and nightmare scenarios abound**

- ❖ What if the 14th salary is cut?
- ❖ What if credit expansion goes down to -10%?

II.5 Greek Stability & Growth Programme: Strong points

- ✓ Re-designing the budget framework
 - ❖ Single Payments Authority will become operational
 - ❖ Establishment of "fiscal rules" to ensure budget execution
 - ❖ Creation of a 10 percent contingency reserve
 - ❖ Ministries required to submit three-year budgets by end-January
 - ❖ "zero-basis" for the re-evaluation of all applications for funding
 - ❖ Monthly reporting requirements for key ministries
 - ❖ Creation of a Parliamentary Budget Office
 - ❖ National Statistical Agency becomes independent
 - ❖ Use of external auditors in public sector entities
- ✓ Tax reform with tax base broadening and a fight against tax evasion
- ✓ A hiring freeze in 2010, and a 5:1 rule from 2011 in the public sector
- ✓ Pension system reform soon
- ✓ Expenditure switch: More investment and less gov. consumption
- ✓ Privatisation revenues of approximately 2.3 % of GDP per year
- ✓ Willingness to proceed with missed structural reforms and a new export-oriented growth model
- ✓ **Greeks do respond when calamity arrives.**

II.5 Greek Stability & Growth Programme: Risks are high - but political will present

- ✓ SGP assumes a relatively benign macroeconomic environment. The balance of **risks** to the growth outlook **skewed to the downside**
- ✓ Risks relate to consumer spending and investment, as consumer and business sentiment remains depressed, wage growth in 2010 will broadly stagnate (or even contract in real terms) and public spending is expected to contract after recording double-digit growth in 2009.

YET

- ✓ EU policy makers realize the attack on Greece is an attack on EMU and recently – following SGP's announcement, began providing strong verbal support
- ✓ The expected close EU inspection of Greek finances implies discipline, which increases the probability of the programme's success
- ✓ It is preposterous to think Greece will ever abandon EMU. The political and economic costs would be way too high, *e.g the post-EMU depreciation would not remain at 30%, probably be 80%, which implies the government debt will increase 5 times!*

II.5 Hard liners prevailed in Europe at the moment

- ✓ The decision to postpone a rescue package is consistent with the objectives of all player :
 - Hard liners who think they protect EMU from moral hazard, and teach a lesson: the more Greece hurts the more disciplined the others will become
 - The ECB, which protects its independence
 - The soft-hearts with debt and deficit problems, who view they can afford a delay as long as markets do not attack beyond Greece
 - Greece, which does not want to pass a signal of fiscal laxity
 - The markets, which love the uncertainty as they can earn more money
- ✓ Greece does not have an option to go to the IMF
- ✓ Greece has to take more stringent fiscal measures to regain credibility

III. Conclusions

- ✓ **A weak global recovery in 2010 and lower world growth in the next 5-7 years with strong pressures on international banking**
- ✓ **Strength of recovery depends on continued provision of central bank liquidity**
- ✓ **The crisis was imported in the region in 2008Q4**
- ✓ **Credit expansion still positive as Greek banks proved stronger than European ones**
- ✓ **Yet, the crisis uncovered the two major imbalances of the Greek economy, the lack of competitiveness and the lack of fiscal discipline**
- ✓ **Greeks do respond to adversity and the expected long stagnation period ahead is likely to trigger the structural reforms the country never dared to undertake before**
- ✓ **The possibility of leaving EMU is out of the question but appears in the media as the scenario heralds the breakdown of EMU**
- ✓ **The Greek SGP puts a credible anchor on economic policies and controls the run-away debt but risks are high**
- ✓ **More attention is required in controlling run-away expenses**
- ✓ **A consensus for mutual sacrifices is required among Greek citizens**