Greek Economic Outlook

Gikas A. Hardouvelis

Professor of Finance & Economics

University of Piraeus

Former Minister of Finance

www.hardouvelis.gr

Economic Chamber of Greece

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The Greek Economy after the closing of the 3rd adjustment programme

STAVROS NIARCHOS FOUNDATION CULTURAL CENTER

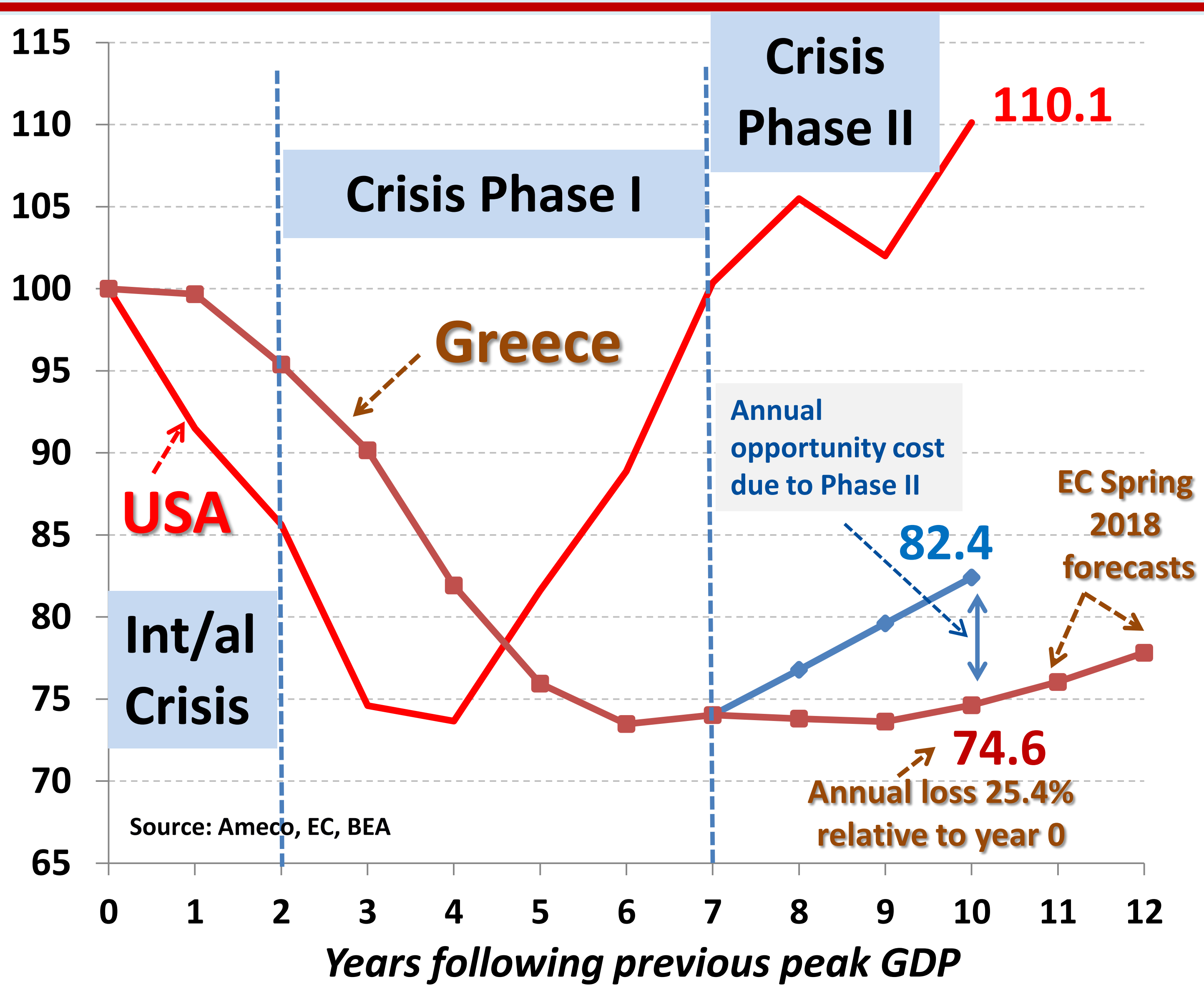
Greek Economic Outlook

I. **Long Greek stagnation: Why?**
(because of an unnecessary Phase II)

II. **What is the way out of stagnation?**

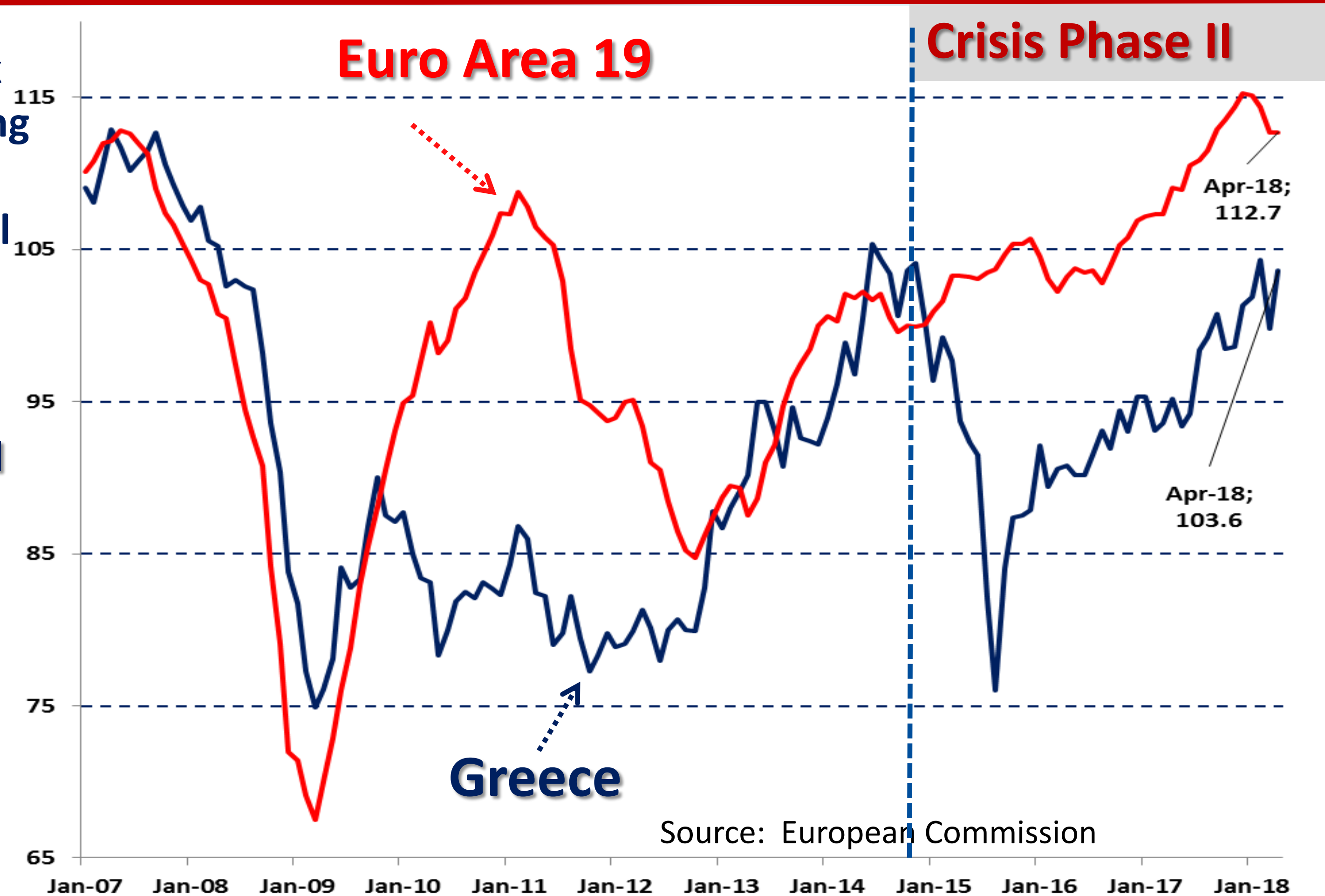
I. Unusual length of Greek crisis due to its Phase II plus the earlier international crisis

- Date 0 is 1929 for the US and 2007 for Greece: Real GDP is set at 100
- The Greek recovery of year 10, 2017, is a forecast
- After 10 years, the US was at 110.1 in 1939 but Greece at 74.6 in 2017
- Fall 2014: Greece was forecasted to be around 82.4
- At minimum, Phase II costs annually 7.8 ppts or ca. €18bn



I. Crisis Phase II shows up clearly in Economic Sentiment

- The sentiment index in Greece was moving together with sentiment in EA until late 2009, both declining
- **Decoupling during the Greek crisis until November 2012**
- From late 2012 until late 2014, **re-coupling**: Greek sentiment moved upward and in line with EA sentiment



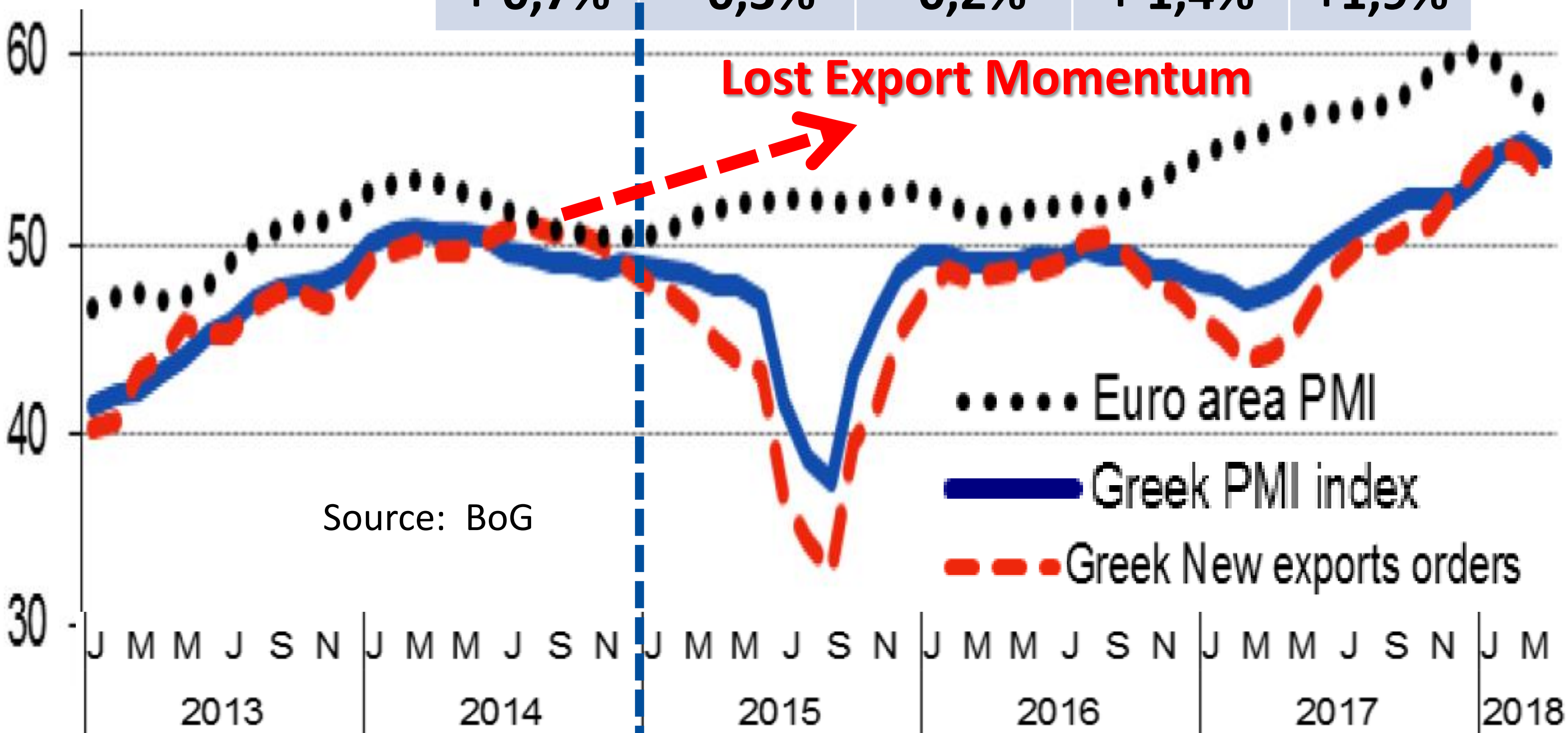
- Greek sentiment peaked in the period June 2014 - November 2014, but subsequently began a fast downward slide as the political landscape deteriorated and generated new uncertainty, thus decoupling a second time from the rest of EA. **Phase II of the crisis was creating anxiety in sentiment.**

I. Phase II aborted the recovery of 2014

Crisis Phase II

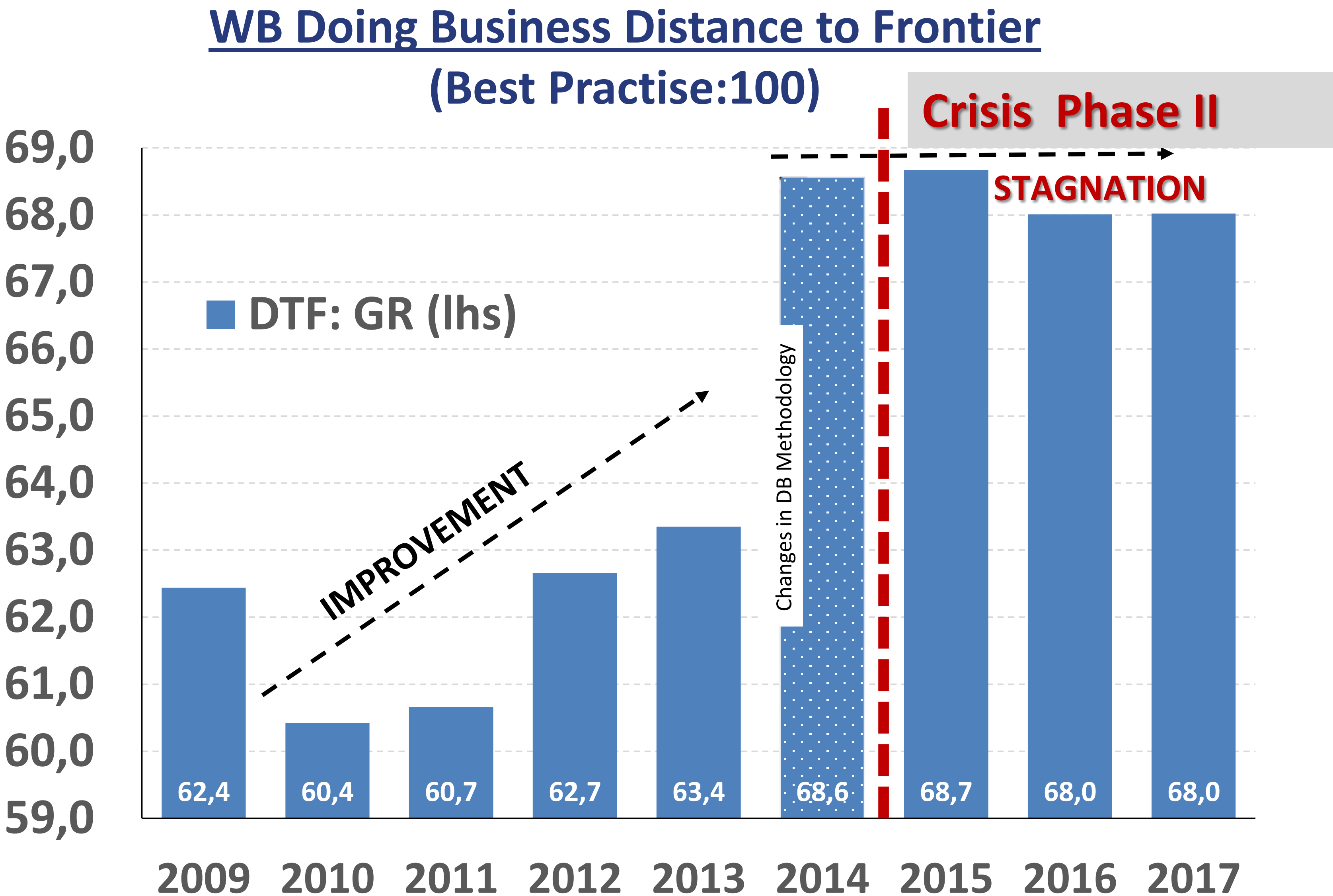
Greek GDP growth

2014	2015	2016	2017	2018
+ 0,7%	- 0,3%	-0,2%	+ 1,4%	+1,9%



Source: BoG

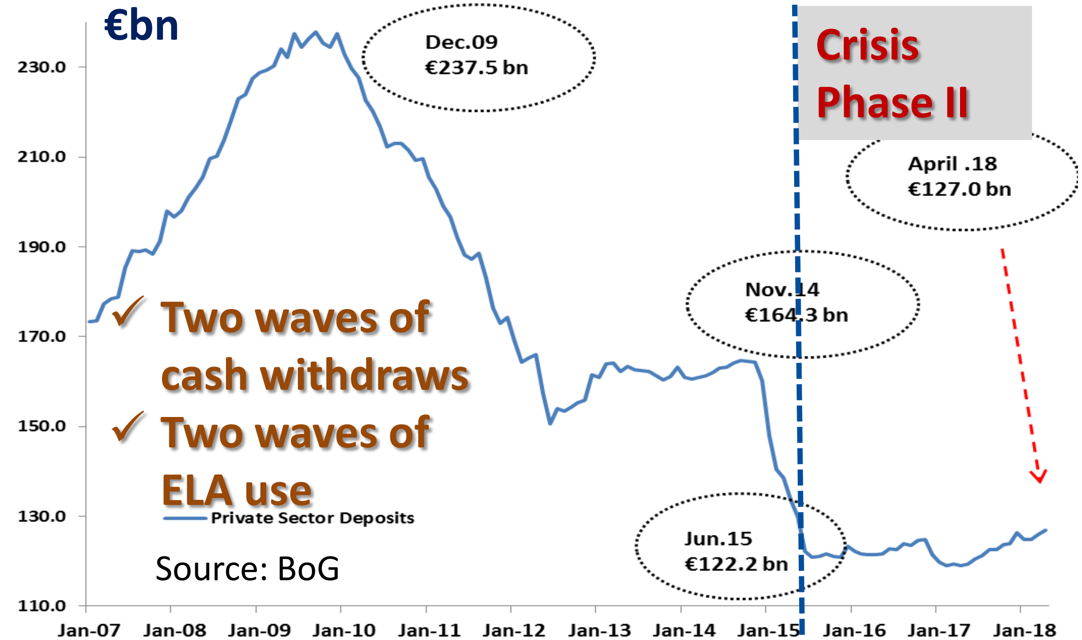
Quality Competitiveness: Stagnation from 2015 onwards

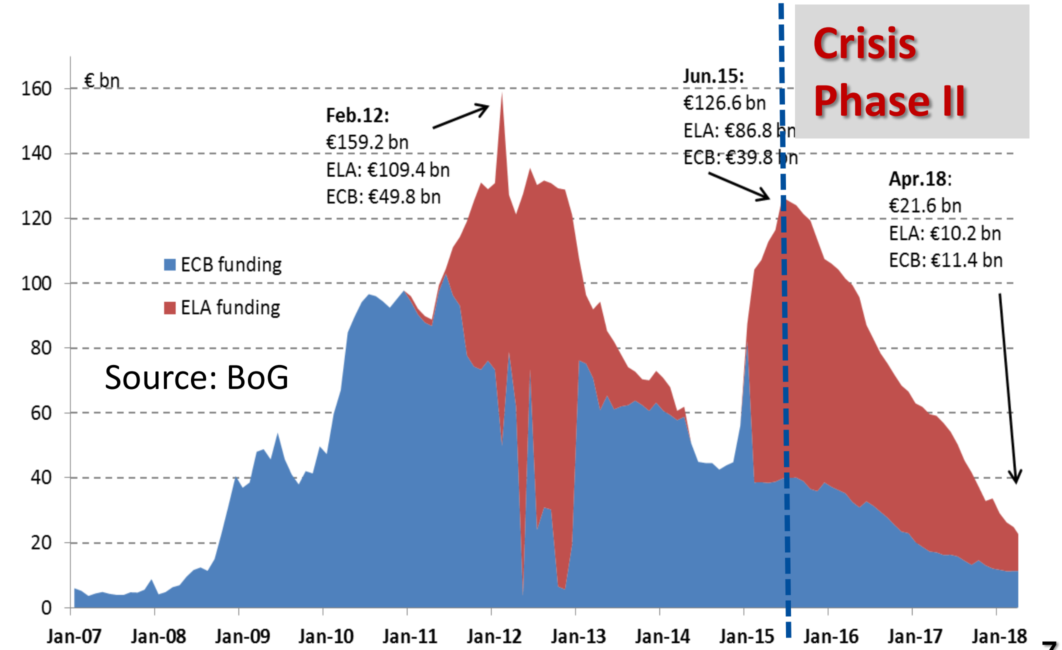


Source: World Bank

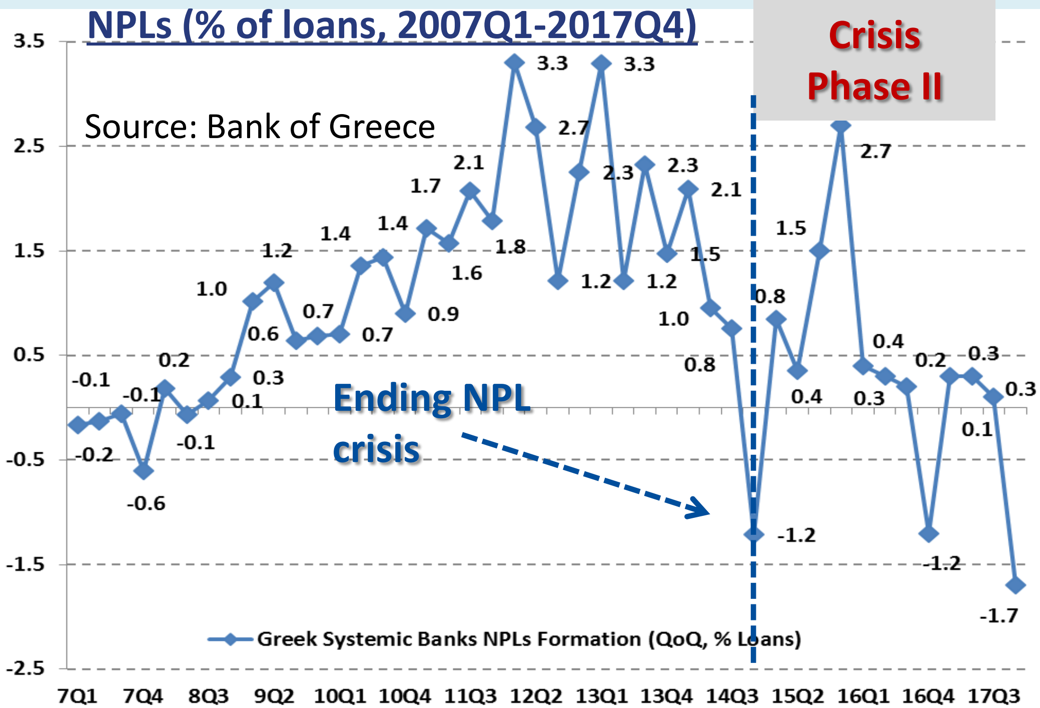
I. Crisis Phase II shows up in the Financial Sector

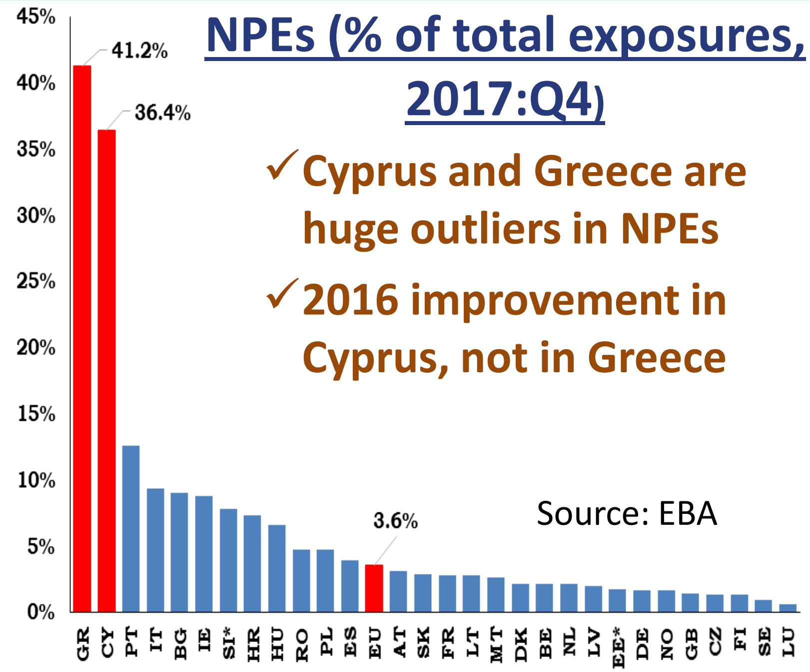
- ❑ A <u>second wave of cash withdrawals</u> in 2015 plus a disappearing inter-bank market <u>leads banks to ELA</u>:
  - ELA was zero at the end of 2014, yet it peaked again in 2015
  - After re-introduction of ECB waiver in July 2016, gradual improvement in ELA dependence
  - It remains at €21bn today
  - Capital controls still imposed
- ❑ <u>Bank stock prices collapsed</u> in 2015H1, State lost over €25bn in value, and a necessary 3rd recapitalization in Nov 2015
- ❑ State owner-ship of systemic banks shrank: NBG (40.4%), Piraeus (26.4%), Alpha (11.0%), Eurobank (2.4%)
- ❑ Capital strong, yet depends on DTC, about 2/3 of CET1





I. Banks remain vulnerable on the Asset side of their balance sheet as well





✓ Cyprus and Greece are huge outliers in NPEs

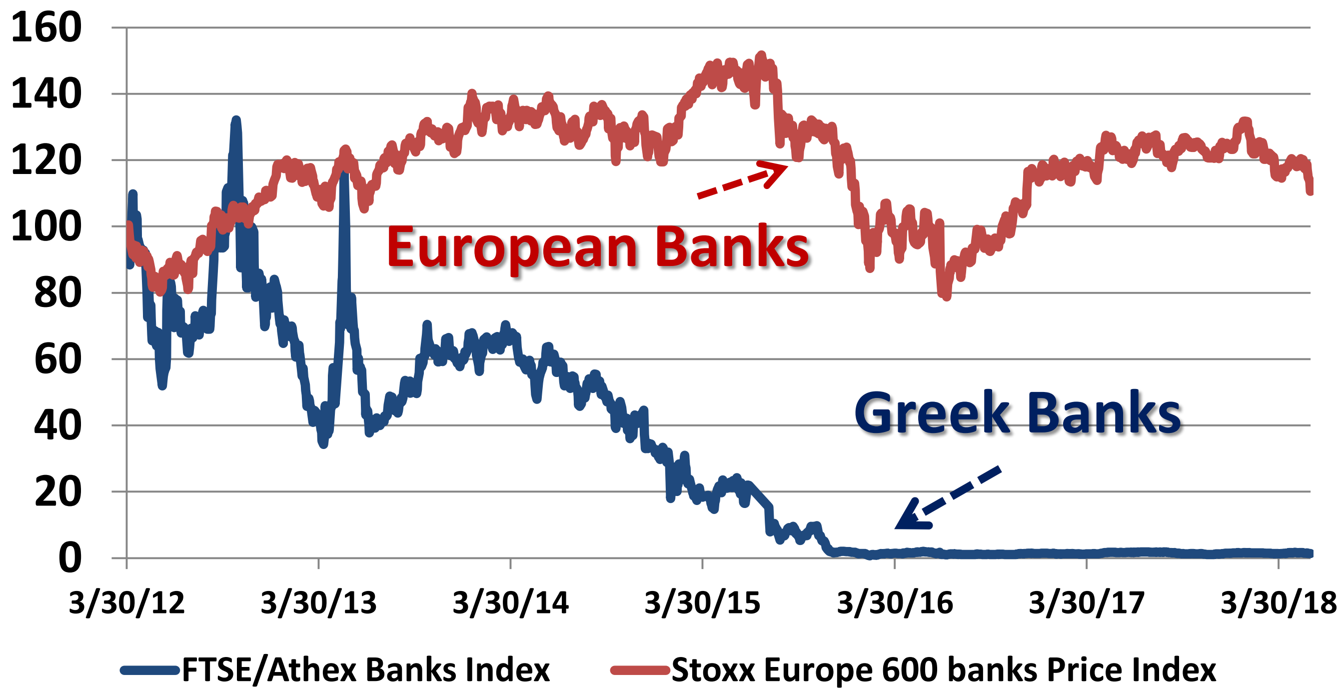
✓ 2016 improvement in Cyprus, not in Greece

- The NPL improvement of late 2014 was reversed due to Phase-II of the crisis
- Improvement in 2017, accompanying a 38% target reduction over 3.5 years, from June 2016 to Dec 2019:
  - NPEs from €106.9bn to €66.7bn or 34% new level
  - NPLs from €78.3bn to €40.2bn or 20% new level

I. How does the Stock Market view the Banks?

BANK INDICES = 100 at 30/3/2012

- Bank stocks reached zero value for a second time in November 2015



BANK INDICES = 100 at 30/11/2015

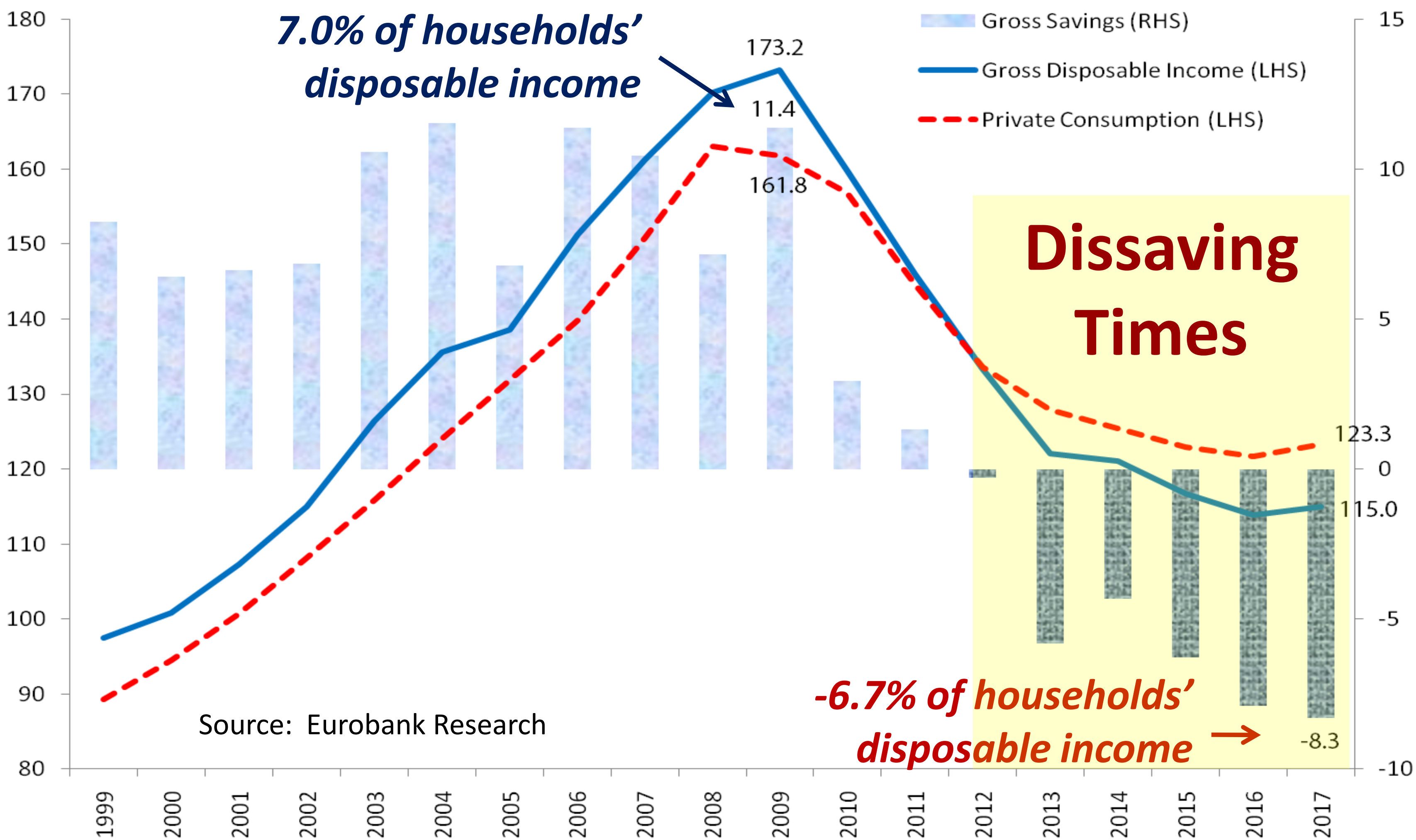
- After the third recapitalization, the Greek bank index fluctuated and now is 30% lower, due to the fears of additional capital needs in 2018

II.

I. **Long Greek stagnation: Why?**
(because of an unnecessary Phase II)

II. **What is the way out of stagnation?**

II. The way out is not consumption - Dissaving will stop



- From positive to negative savings since 2012, which have supported consumption during the last five years.
- But for how long?

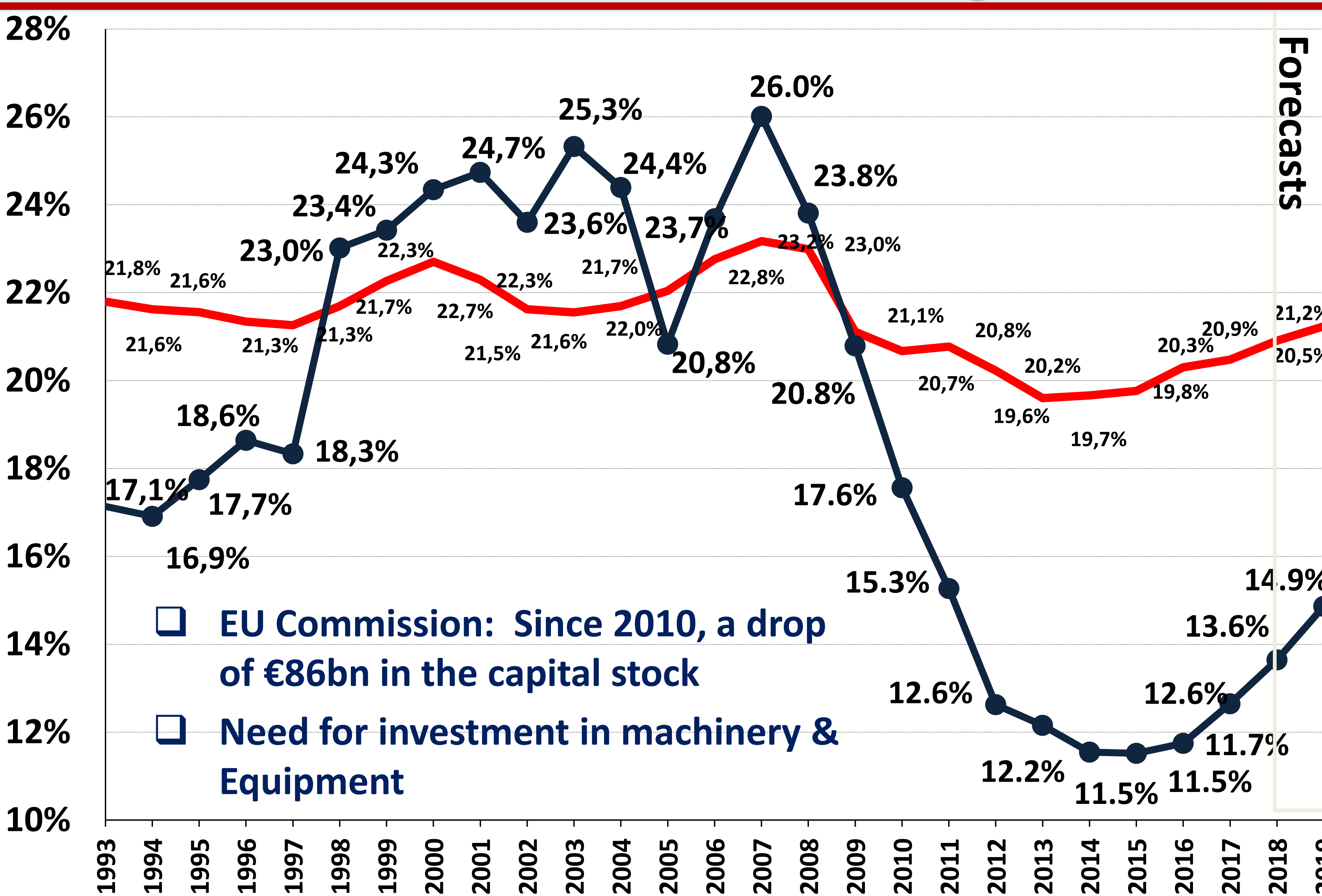
II. Growth has to come from Investment and Exports

- We do not want consumption to grow fast either – Greeks over-consume
- Investment is the way out of stagnation as it expands both demand and future supply, i.e. potential growth
- Exports have picked up during the crisis but cannot support the economy alone

	2017 €bn (nominal)		2017 Real (YoY%)	2018 Real (YoY%)	2019 Real (YoY%)
GDP	177.7		1.4	1.9	2.1
Private Consumption	123.3	(69%)	0.1	0.5	0.7
Govern. Consumption	35.5	(20%)	-1.1	1.2	0.4
Gross Investment	22.5	(13%)	9.6	8.9	12.1
Exports	59.0	(33%)	6.8	6.3	4.3
Imports	61.0	(34%)	7.2	3.1	3.1
GDP Deflator (YoY%)			0.7	0.9	1.3
HICP (YoY%)			1.1	0.8	1.2
Unemployment (%)			21.5	20.1	18.8

*Note: Real GDP growth rate consensus forecast for 2018 and 2019 at 1.9% and 2.1% respectively (source: **Focus Economics**)*

II. Investment: Can it rebound fast enough?



- EU Commission: Since 2010, a drop of €86bn in the capital stock
- Need for investment in machinery & Equipment

II. The long-run optimistic view

- Energy markets are in the process of liberalization; Investments can close 1/3 of the gap in the capital stock
- The health and tourist sectors are attractive for investment as well
- Macro-stability is here to stay
- Even the hostile left understands the need for privatizations & even tax cuts
- Labor markets are flexible and reforms were not reversed in 2015-2018, despite all the leftist bravado
- The politically hard reforms are behind us
- GREXIT is no longer on the table by the Europeans
- Excluding oil and ships, exports of goods are rising
- A new consensus on a growth recipe seems to have formed
- And …. capital controls will soon be lifted; Some deposits will come back to banks; Banks proved stronger than expected

II. The long-run pessimistic view

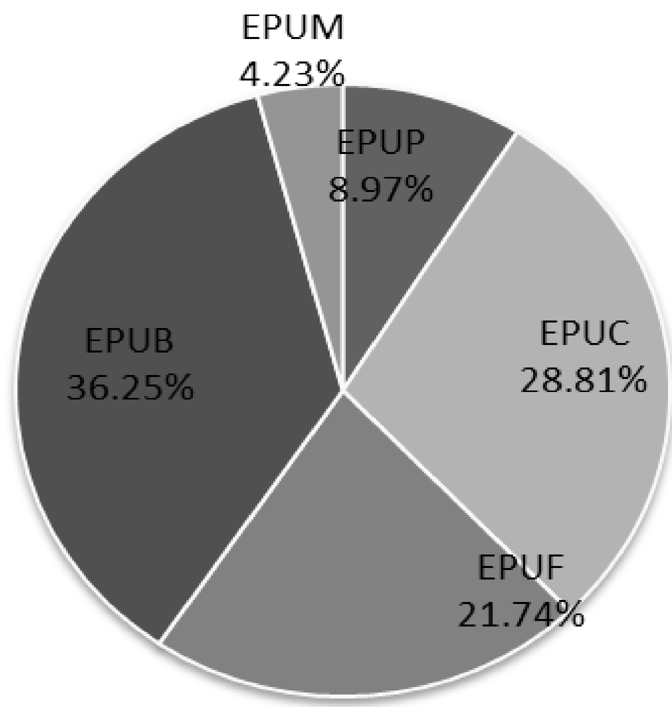
Many, including the IMF, have concluded growth cannot exceed 1% over the long term and they point to:

- ❑ Negative population growth
- ❑ Low factor productivity due to:
  - Low technological content of production
  - Incorrect incentive structure for willingness to work, save and invest
  - Over-taxation of the same group of citizens, leading to low work effort, low innovation, huge tax avoidance plus immigration abroad
  - No 3rd pillar in Pension system yet
- ❑ Fragile financial sector with an overwhelming level of NPLs
- ❑ Debt overhang in both public and private sectors
- ❑ Huge Debt-to-GDP ratio constrains future fiscal policy
- ❑ Little ownership of reforms, hence incomplete and delayed implementation or even a reversal of reforms once the Troika is gone
- ❑ Short-run lack of clarity on post-programme regime
- ❑ Many Greeks have yet to understand the causes of the crisis and come to terms with the globalized world and its demands on competitiveness
- ❑ EMU politics & economic environment may sour due to Italy
- ❑ Geopolitical risks in the neighborhood

II. Which View will prevail?

- Which view has the higher probability of materializing?
- The growth scenario lost its chance in 2015
- Yet Economic Policy Uncertainty (EPU), which was critical in both the depth and length of the Greek depression is down since late 2017 and its major components are perhaps under control:
  - EPUC – Grexit uncertainty is not worrisome
  - EPUD – Debt uncertainty (a subset of fiscal uncertainty) can be tamed, currently under negotiations
  - EPUB – Banking uncertainty, may cause trouble

The composition of EPU (2007:Q3 - 2018:Q1)



Source: Hardouvelis, Karalas, Karanastasis, Samartzis, 2018, SSRN # 3155172 "Political, Economic and Economic Policy Uncertainty in Greece"

Conclusion

- The good scenario can materialize if ...
  - Credibility comes back
  - Incentives for work and innovation reappear
  - The tax and pension contribution structure is cured
  - Reforms continue (privatizations, bureaucracy reduction, rationalization of the public sector, liberalization of energy markets, etc.)
  - Banks manage to survive and provide fresh credit

Thank you for your attention!

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