Euler Hermes Economic Research

Country Report

Greece

Back to economic recovery despite significant challenges

General Information

GDP	USD194.851bn (World ranking 46, World Bank 2015)
Population	10.82mn (World ranking 81, World Bank 2015)
Form of state	Parliamentary Republic
Head of government	Alexis Tsipras (Prime Minister)
Next elections	2019, Legislative

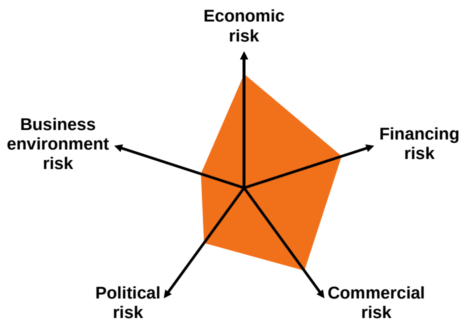
Strengths

- Major economic hub of Southeast Europe
- Strong tourism sector
- Labour market reforms boost competitiveness
- Current account surplus
- Primary fiscal surplus

Weaknesses

- Capital controls in place since July 2015
- Rigid business environment
- Weak industrial base
- Fragile banking sector
- High fiscal pressure on corporates
- Low R&D expenditure

Country Rating C3



Source: Euler Hermes

Trade Structure

By destination/origin (% of total)

Exports		Rank		Imports
Italy	11%	1	11%	Germany
Turkey	8%	2	8%	Italy
Germany	7%	3	8%	Russia
Cyprus	6%	4	6%	Netherlands
Bulgaria	5%	5	5%	China

By product (% of total)

Exports		Rank		Imports
Refined Petroleum Products	29%	1	17%	Crude Oil
Non Ferrous Metals	7%	2	7%	Pharmaceuticals
Fats	5%	3	7%	Refined Petroleum Products
Other Edible Agricultural Prod	5%	4	4%	Ships
Preserved Fruits	4%	5	3%	Plastic Articles

Source: Chelem (2015)

Economic Overview

Return to recovery in sight, challenges still significant

The Greek economy stagnated in 2016, following a mild contraction in the previous year, with a relatively strong growth contribution from private consumption offset by negative contributions from public consumption and net exports. Meanwhile gross fixed investment had no significant impact on GDP growth. Elevated economic uncertainty in H2 2016 due to delays in the completion of the second review of the EUR86 billion ESM bailout program weighed on economic activity.

In 2017 the Greek economy is likely to return to positive growth. Yet the downside risks are still significant. In Q1 2017 GDP expanded by 0.4% q/q and short-term economic prospects should benefit from the successful conclusion of the second review in mid-June which ensures that Greece can meet upcoming debt repayments removing the risk of an imminent sovereign debt default and clear some arrears.

Domestic demand will be the key driver of economic growth supported by the recovery in business and consumer confidence and a favorable labor market trend. The return of inflation (Forecast: 1.0% in 2017 and 1.2% in 2018) and the limited ability of Greek banks to supply credit given persistently high NPLs will, however, keep a lid on growth dynamics.

Meanwhile exports are expected to benefit from the favorable global growth momentum, a still relatively weak EUR and strong demand in the tourism sector – the Greek National Tourism Organization expects a record-breaking 30 million international visitors to Greece for 2017 (+7% y/y). We expect Greek GDP to expand by 1.0% in 2017 with the pace of the recovery accelerating notably in 2018 to 2.5%. The pick-up in economic growth will be supported by the removal of the capital controls with first steps expected to be taken as early as H2 2017 contingent on the return of confidence in the Greek banking sector.

Labor market on the mend

Greece's labor market outlook continues to gradually improve, however the road ahead is still long. In March the unemployment rate fell to 22.5% – the lowest level since 2012 – and prospects remain positive given the expected pick-up in GDP growth. Employment growth meanwhile rose by 1.7% in 2016 despite the weak economic momentum providing evidence for a relatively job-rich recovery. The pace of job growth is expected to accelerate further over the course of 2017-18 in line with the strengthening recovery.

Fiscal outlook: End of austerity is near

In 2016 Greece achieved a primary surplus of 4.2% of GDP – eight times over the target of 0.5% for the year. Meanwhile the overall public deficit come in at 0.7% of GDP, the fourth highest among all eurozone countries. The result was driven by rising tax revenue as well as a significant reduction in public spending, however one-off, non-recurring measures were partially responsible for the stellar performance. Greece looks set to reach the budget targets for 2017-18 without the need for additional austerity.

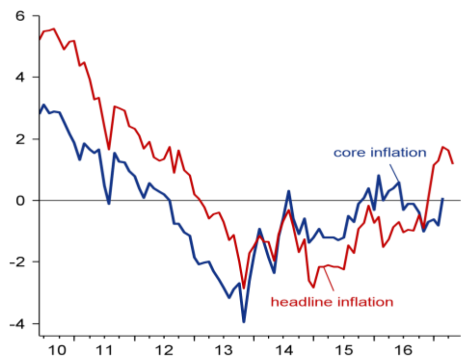
Figure 1 – Key economic forecasts

Greece		weight	2015	2016	2017	2018
GDP		100%	-0.3	0.0	1.0	2.5
Consumer Spending		69%	-0.3	1.4	2.0	2.9
Public Spending		22%	0.0	-2.1	0.7	1.5
Investment		11%	-0.2	0.0	2.6	5.1
Stocks	*	0%	-0.9	0.1	1.6	1.1
Exports		32%	3.1	-1.7	2.7	4.8
Imports		34%	0.3	0.6	9.9	8.7
Net exports	*	-2%	0.8	-0.7	-2.4	-1.6
Current account	**		0	-1	-2	-1
Current account (% of GDP)			*0.1*	*-0.6*	*-1.0*	*-0.8*
Employment			2.1	1.7	2.1	2.1
Unemployment rate			24.9	23.5	21.7	20.6
Inflation			-1.7	-0.8	1.0	1.2
General government balance	**		-10	1	-3	-1
General government balance (% of GDP)			*-5.9*	*0.7*	*-1.5*	*-0.5*
Public debt (% of GDP)			*177.4*	*179.0*	*178.5*	*175.5*
Nominal GDP	**		175	176	177	183

Change over the period, unless otherwise indicated:
*contribution to GDP growth
**EUR bn

Sources: Elstat, Allianz Research

Figure 2 – Inflation (%, y/y)

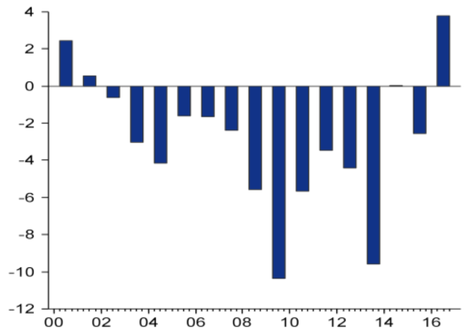


Sources: Eurostat, Allianz Research

Figure 3 – Unemployment rate (%)

Sources: Elstat, Allianz Research

Figure 4 – Primary balance (% GDP)



Source: Thomson Reuters Datastream

Despite the promising fiscal outlook and nominal growth exceeding 2% over the forecast horizon, public debt in relation to GDP will only decline gradually in 2017 – with the government likely to prioritize the reduction of arrears – before embarking on a more pronounced downward trend in the following year.

Competitiveness: Room for improvement

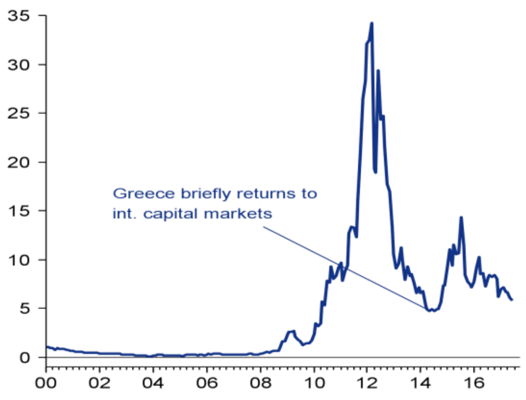
To ensure Greece's economic success beyond the short-term, boosting investment – domestic but especially foreign – is key. Moreover in 2018 with the scheduled completion of the bailout program, Greece will also have to ensure a successful return to international capital markets. This requires not only the full implementation of already agreed growth-boosting reforms but additional measures to strengthen Greece's competitiveness with a view of boosting exports and FDI inflows. Worryingly though after significant increases in structural competitiveness in 2013-14, the process has not only stalled recently but also reversed to some extent. According to the World Bank's 2016 "Ease of doing business" survey, Greece slipped three places to 61 out of 190, at the lower end of advanced economies. The lowest scores were received for registering property, enforcing contracts and getting credit.

Additional measures to strengthen the banking sector – including dealing with the high share of NPLs – will be necessary to ensure there is adequate credit to support the economic recovery. Next to higher tax rates, Greek corporates' key challenge is constrained access to financing, particularly for SMEs. The expected increase in turnover driven by brightening growth prospects, however, should see business insolvencies fall by -3% in 2017 and -5% in 2018.

Debt relief discussion postponed

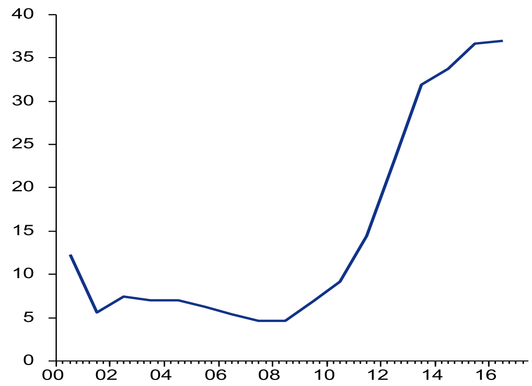
Under the agreement between Greece's creditors on the next stages of the bailout, the IMF is set to formally join the rescue program. However, the fund will only provide financial resources once more clarity on the debt relief offered to Greece allows for an assessment of its debt sustainability. Yet the politically difficult discussion among creditors regarding the measures used to reduce the debt burden – possible options raised include extending the maturities of some loans and defer interest payments by up to 15 years – as well as the scope of the relief looks set to be postponed until the completion of the bailout in 2018.

Figure 5 – 10yr gov. bond spread Greece/Germany



Sources: Thomson Reuters Datastream, Allianz Research

Figure 6 – Non-performing loans (% total gross loans)



Sources: World Bank, Allianz Research

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