Euler Hermes Economic Research

Country Report

Greece

At half time, waiting for the final

General Information

GDP	USD242.2 bn (World ranking 43, World Bank 2013)
Population	11.0 mn (World ranking 78, World Bank 2013)
Form of state	Parliamentary Republic
Head of government	Alexis Tsipras (Prime Minister)
Next elections	2019, Legislative

Strengths

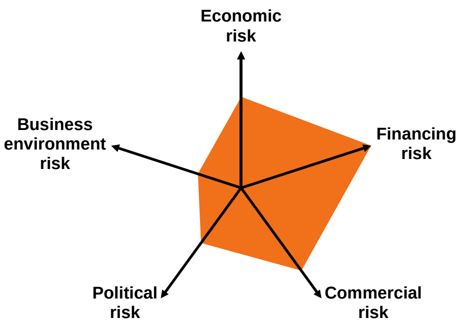
- Geographical hub
- Strong tourism revenues
- Strong adjustment in terms of competitiveness
- Current account surplus

Weaknesses

- Weak business environment
- Weak industrial base
- High fiscal pressure on companies
- High deflationary pressures
- Low R&D expenditures
- Decreasing long term per capita income
- Tight political environment

Country Rating

B3



Source: Euler Hermes

Trade structure

By destination / origin (% of total)

Exports		Rank		Imports
Turkey	12%	1	10%	Russia
Italy	9%	2	10%	Germany
Germany	7%	3	9%	Iraq
Bulgaria	5%	4	8%	Italy
Cyprus	5%	5	5%	China

By destination / origin (% of total)

Exports		Rank		Imports
Mineral Fuels	12%	1	10%	Mineral Fuels
Aluminum	9%	2	10%	Pharmaceuticals
Pharmaceuticals	7%	3	9%	Machinery
Machinery	5%	4	8%	Electrical Equipment
Plastics	5%	5	5%	Ships, floating structures

Source: ITC, (2014)

Temporary agreement with the Troika

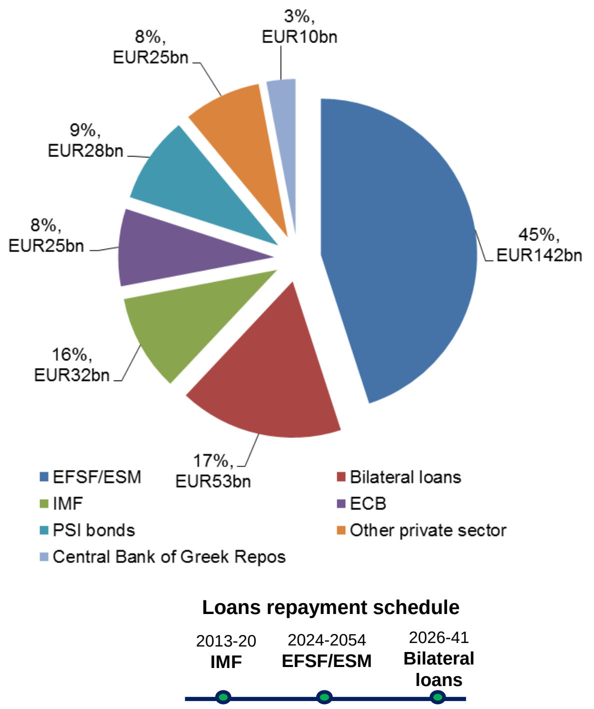
The Eurogroup agreed with the first list of reforms that Greece proposed. This was a pre-condition of the four-month bailout extension that expired on February 28th. The reforms include: action to limit corruption, tax evasion and bureaucracy; delay in introducing a minimum wage; further measures relating to pensions; continuation of the privatisations; and pledges to implement stricter control of public spending. The list of reforms will be finalized by end of April, but the Eurogroup expects some of the announced reforms to be already voted in the Greek Parliament in order to allow the disbursement of the remaining EUR7.2 bn of the bailout (ESM: EUR1.8 bn; IMF: EUR3.5 bn; NCB profit redistribution: EUR1.9 bn). The OECD has been also involved in the reforms' implementation process. In addition, we expect this will be accompanied by an increase of the Bills limit issuance (from the current reached limit of EUR15 bn to above EUR20 bn).

Two scenarios post-June: (1) a 4-6 month bailout extension followed by a program; (2) a program + further debt relief

Greece has more time to negotiate the conditions of a new programme (a precautionary credit line, ECCL with a maturity of at least 12-months), which we expect in July (around EUR11.1 bn of financing needs in Q3) accompanied by further debt relief at the end of the year in the form of frozen interest payments on EU and IMF loans, for a limited period of time, and longer loan maturities. Indeed, the unsustainability of Greek debt (circa 175% of GDP) and the fact that more than 80% of that Greek debt is held by the EU, the ECB and the IMF (see Chart 1) with an average maturity of around 20 years – more than twice as high as Italian or French debt – bodes well for further debt relief by the Troika (read our Economic Insight **Greece and Europe: The sequel, Political will, Time and Value-at-Risk**).

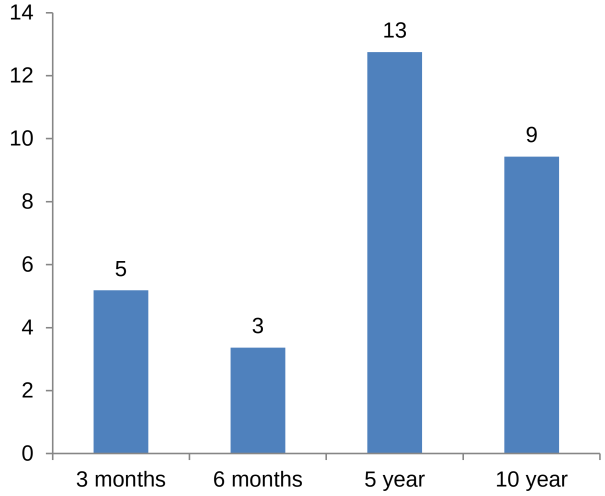
However, if the debt relief measures are not immediately agreed by the Troika, then another bailout extension is likely, for 4 to 6 months, that would allow more time for negotiations (see Figure below). As a reminder, Greece's overall financing gap remains elevated this year, with EUR7 bn of bonds maturing in July-August, EUR7.9 bn of IMF repayments and EUR12 bn of maturing bills. If the idea of bond issuance is far from realistic given the loss in investor confidence (if 9 months ago Greece had issued 10-year bonds at 5% interest, today the interest rate would have doubled), Greece could continue issuing T-bills, but even for them the interest rate has soared (at 5% for 3-month maturity, see Chart 2).

Chart 1: Breakdown of the Greek debt

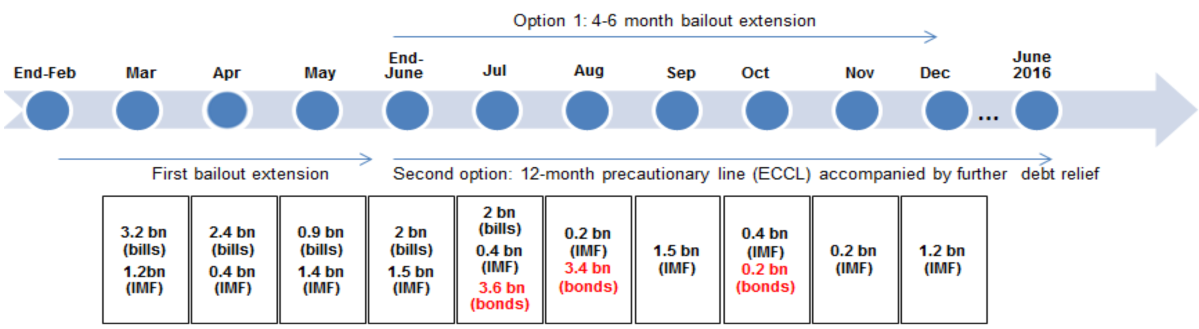


Sources: ESM, Euler Hermes

Chart 2: Greek sovereign bill/bond yields by maturity (February 2015), %



Sources: Bloomberg, Euler Hermes



Tough year ahead, risks of recession have increased

In the short-term, risks remain on the stability of the governing coalition since there seems to be increasing disagreement within Syriza on the government's policy. Risks remain on the downside for the Greek economy where we see increasing headwinds for the recovery and we expect growth at +0.6% in 2015 (from +1.0% previously) – see Table 1. We expect GDP growth will remain in negative territory in Q1 and Q2, although at a softer pace, and the risk of recession in 2015 has increased lately. Indeed, currently people are delaying payments and the liquidity is tight. We expect business insolvencies to remain on the rise in 2015 after increasing by more than 200% since 2007. Signs of weakness have already started to be visible with Q4 2014 GDP growth back in negative territory after 3 consecutive quarters of positive growth. Public consumption contracted by -1.1% q/q and net exports contributed negatively to growth (-2.3pp). Private consumption growth moderated to +0.2% q/q after +1% in Q3. In 2015, the loss of confidence and the uncertainty related to the bailout are expected to cause a slowdown in investment and to restrain consumer sending from growing at a faster pace compared with 2014. Public spending is expected to fall at a stronger pace.

Table 1: Key indicators

Greece		poids	**2013**	**2014**	**2015**	**2016**
GDP		100%	**-4.0**	**0.7**	**0.6**	**1.7**
Consumer Spending		69%	**-2.2**	**1.4**	**1.4**	**1.9**
Public Spending		22%	**-5.1**	**-0.8**	**-3.5**	**-1.6**
Investment		16%	**-9.5**	**3.0**	**2.4**	**2.7**
Stocks	*	0%	**-1.5**	**-0.7**	**-0.2**	**0.0**
Exports		24%	**1.5**	**8.8**	**8.9**	**7.0**
Imports		31%	**-2.9**	**7.4**	**7.3**	**5.5**
Net exports	*	-7%	**1.3**	**0.2**	**0.3**	**0.4**
Current account	**		**1**	**2**	**2**	**3**
Current account (% of GDP)			*0.6*	*0.9*	*1.1*	*1.8*
Employment			**-4.9**	**0.4**	**0.9**	**1.0**
Unemployment rate			**27.5**	**26.5**	**24.6**	**23.3**
Wages			**-10.7**	**0.6**	**1.1**	**1.3**
Inflation			**-0.9**	**-1.4**	**-1.2**	**0.7**
General government balance	**		**-23**	**-7**	**-6**	**-5**
General government balance (% of GDP)			*-12.7*	*-4.0*	*-3.5*	*-3.0*
Public debt (% of GDP)			*175.1*	*175.3*	*170.4*	*158.3*
Nominal GDP	**		182	179	177	181

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

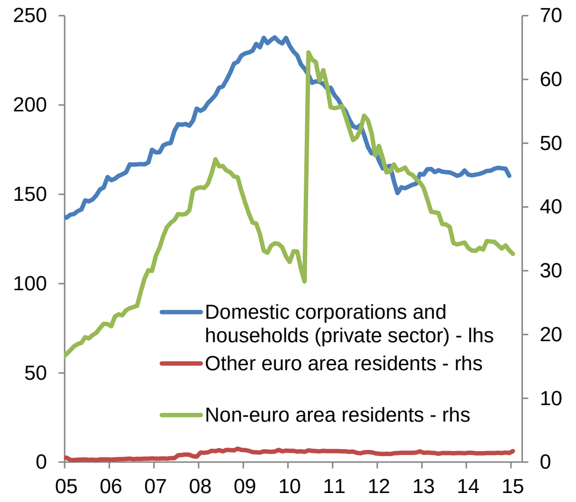
Sources: IHS, Euler Hermes

The banking system remains fragile

The banking system remains fragile on the back of the accelerating deposit outflows since last December. In January 2015 deposit outflows were 3 times higher in comparison with December and stood well above the EUR9 bn deposit contraction in May 2012 ahead of the legislative elections (see Chart 3). Of the total of EUR12 bn of deposit outflows in January, EUR8.8 bn came from households and EUR3 bn from non-financial corporations. Overall, since December EUR16 bn was withdrawn from Greek banks, but the trend is expected to have moderated in February.

The Emergency Lending Assistance (ELA) was introduced for Greek banks at the beginning of February since the ECB couldn't accept any more Greek bonds/bills from banks in exchange for liquidity. As a consequence of the accelerating deposit outflows, the ECB increased the ELA funding by EUR500 mn (to EUR69.4 bn) in March, and we expect the ECB will be supportive of the Greek banks whenever necessary as long as the Greek government is under official negotiations with the Troika. Further, once the Troika review is finalized and Greece reimburses the bond maturing in July (currently held by the ECB), the ECB should be able to buy Greek bonds on the secondary market through its QE program (up to EUR9 bn of the existing secondary Greek market).

Chart 3: Deposits, EURbn



Sources: Bank of Greece, Euler Hermes

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