The Greek Sovereign Debt Crisis: Policies and Prospects

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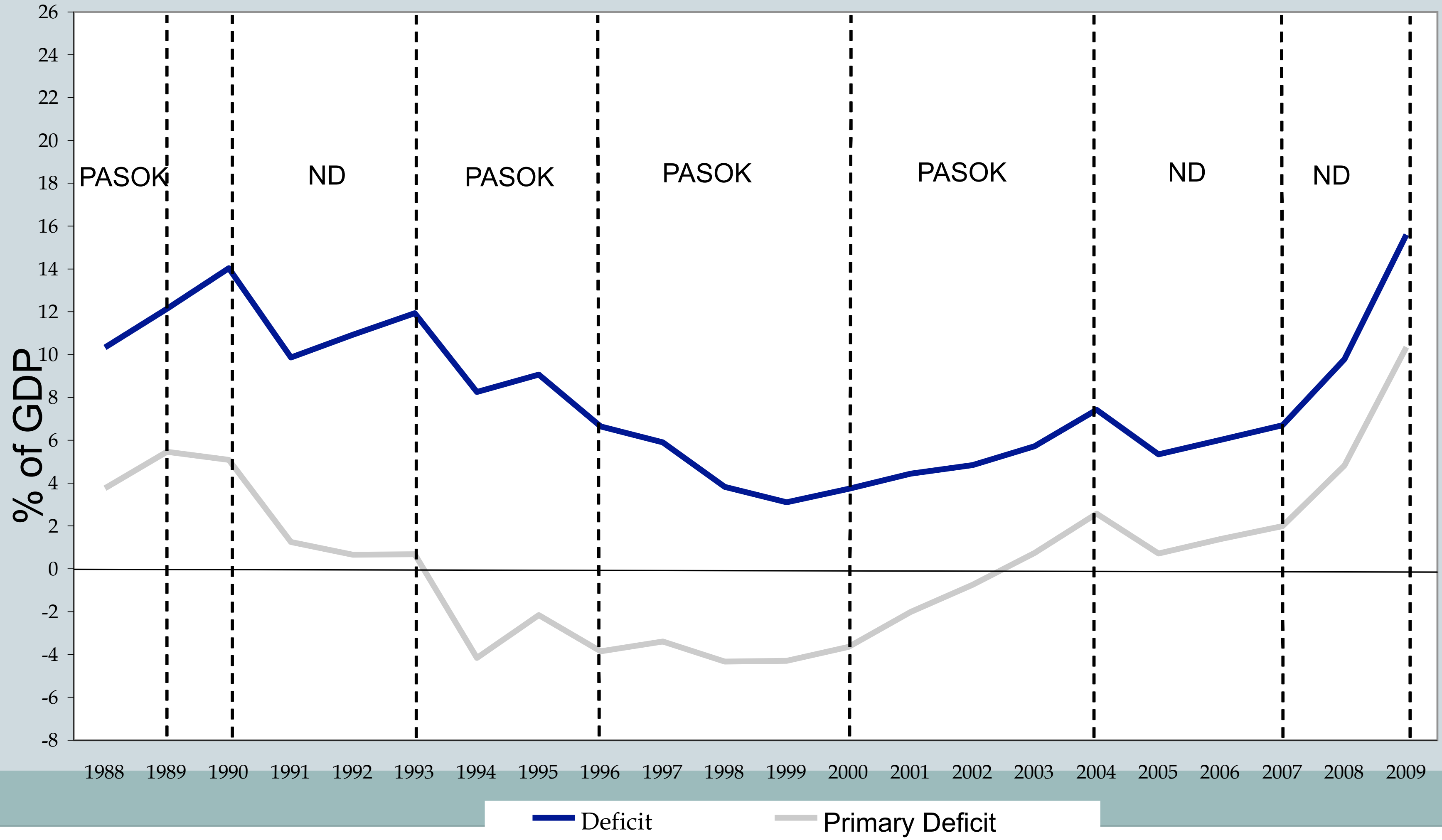
Introduction

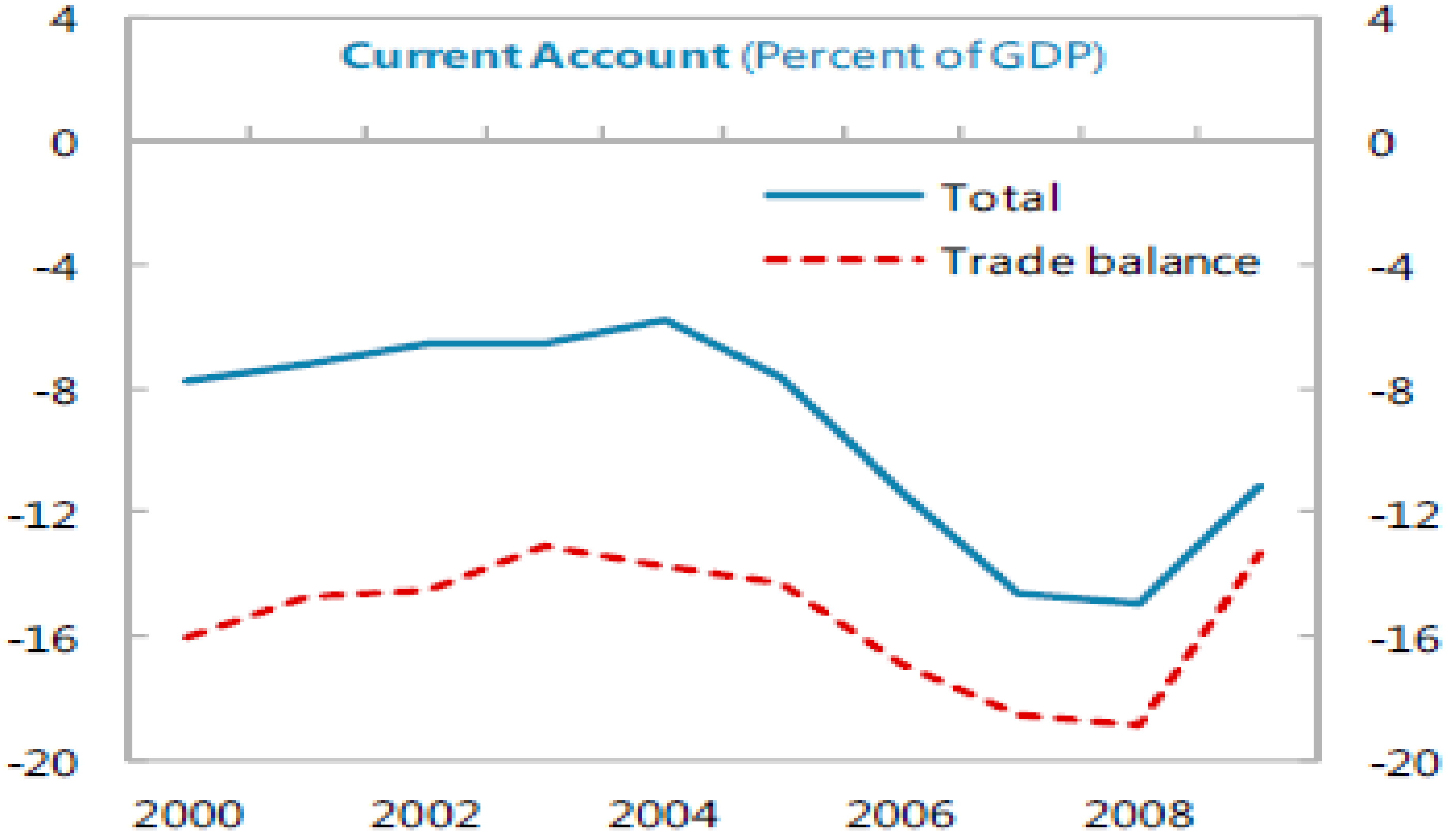
- Since 2010, the Greek Economy has been in an austerity and default trap and in a debt-deflation process.
- The austerity trap has been enforced by the bailout agreements between Greece and Troika (IMF, ECB, EC) and has been accommodated by the conservative Greek governments.
- The default trap followed the fiscal crisis that began when Greece approach default in May 2010.

The Greek Economy in 2009-2010

Deficit of General Government, % of GDP, Greece 1988-2009 (Eurostat)

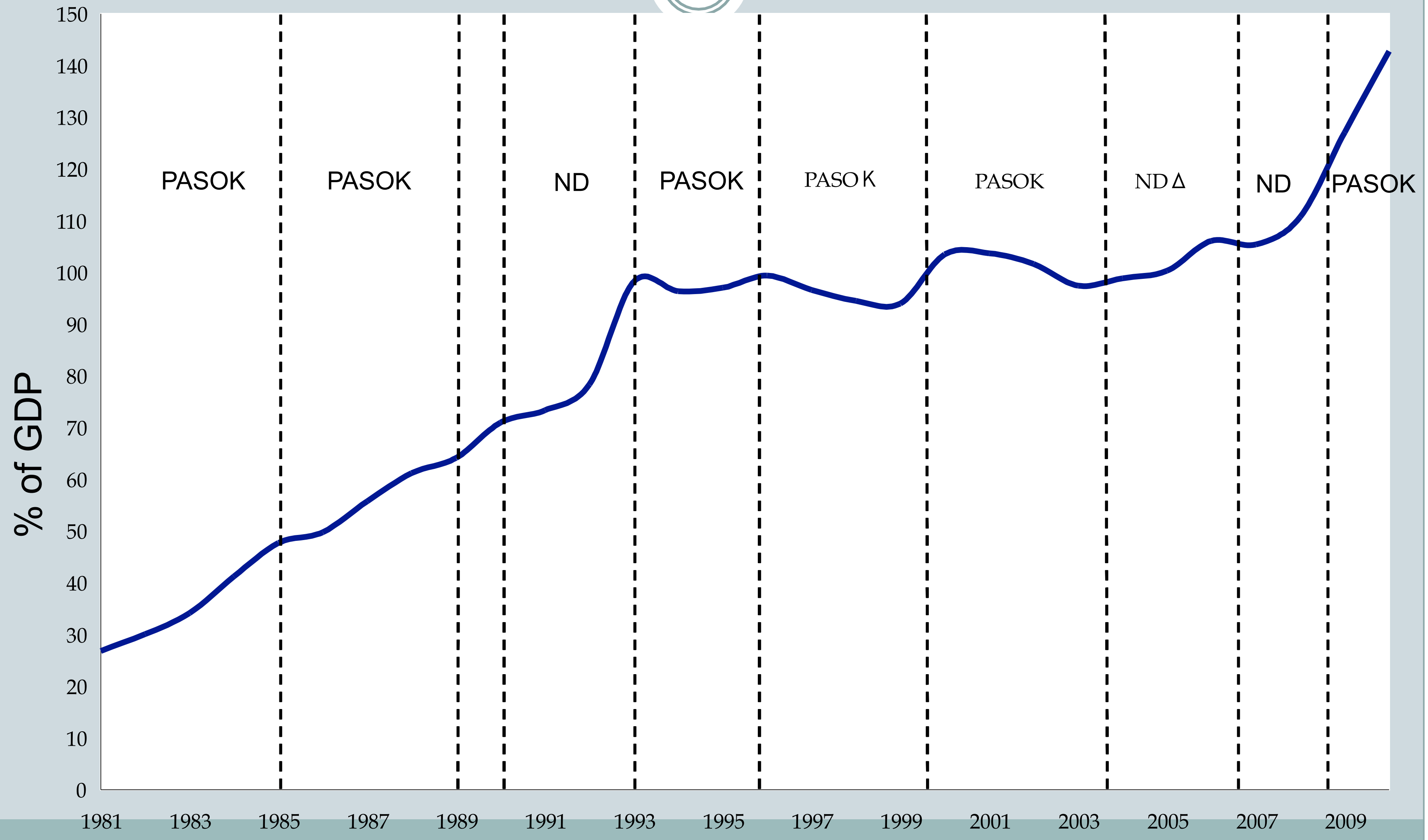


Current Account Deficit, Greece 2000-2009 (IMF, June 2013)

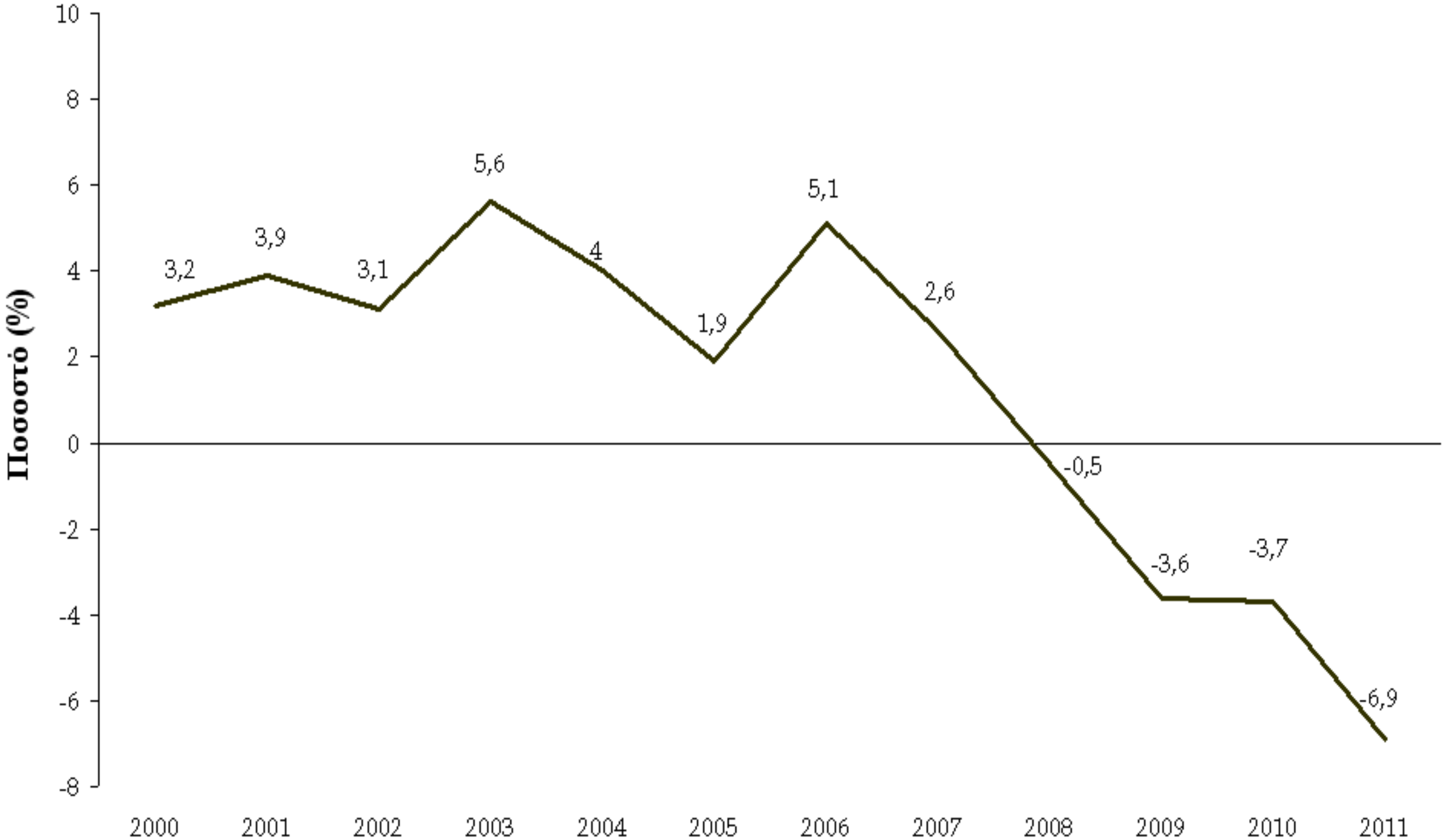


Sources: Bank of Greece; Elstat; and IMF staff calculations.

Government Debt, % of GDP, Greece 1981-2010 (Eurostat)



Growth Rate, Greece 2000-2011 (Eurostat)



Πηγή : Eurostat

ΠΑΡΑΤΗΡΗΤΗΡΙΟ ΙΝΕ ΓΣΕΕ

Plus

- The Unemployment rate was about 9%, and

- The economy gradually, especially during 2010, was getting insolvent and marginalized by the private bond markets.

- What type of macroeconomic policy could help Greece to deal with the abovementioned macroeconomic imbalances?

Troika's Policy Framework

- Since May 2010 Greece has committed to apply two Memorandums of Economic and Financial Policies as part of the two bailout agreements with Troika. The two Memorandums consist from three pillars:

- **The first pillar targets the reduction of the fiscal deficit**. The required adjustment in the primary balance during the period 2010-2014 was 14.5% of GDP and the required measures amounting to 16% of GDP.

Troika’s Policy Framework

- **The second pillar targets structural reforms especially in the labor market that create processes of** internal devaluation to boost economic growth.
- Troika has estimated a 20-30% competitiveness gap that has to be addressed until 2014 through decreasing wages in the private sector.

Troika's Policy Framework

- **The third pillar targets to preserve financial stability.**
- The 2nd bailout program includes €50 billion new debt fro Greece for the recapitalization of the Greek banks after the 2012 haircut.
- It is crucial to note that since 2008, Greek banks have received a total amount of about €100 billion for their recapitalization, which is 30% of the total amount of country's public debt.

Catastrophic Macroeconomic Outcomes

IMF's "mea culpa"

- **The IMF (June 2013) published a paper entitled "Greece: Ex Post Evaluation of Exceptional Access under the 2010 Stand-By Arrangement", and admits that there were notable failures in the adjustment programs of Greece.**

- Real GDP in 2012 was 17 % lower than in 2009, compared to a 5.5% decline projected in Troika's adjustment programs.
- The unemployment rate in 2012 was 25 % compared to the programs projection of 15 %.
- Market confidence was not restored,

- The banking system lost 30% of its deposits, while bank balance sheets have weakened due to a dramatic increase in the NPLs.
- Public debt remains non viable and unsustainable.
- Competitiveness improved somewhat on the back of falling wages, while productivity gains proved elusive.
- Prices fell by less than the decline in wages in part reflecting continued rigidities in product markets.

Greece Selected Economic Indicators, 2009-2014 (IMF June 2013)

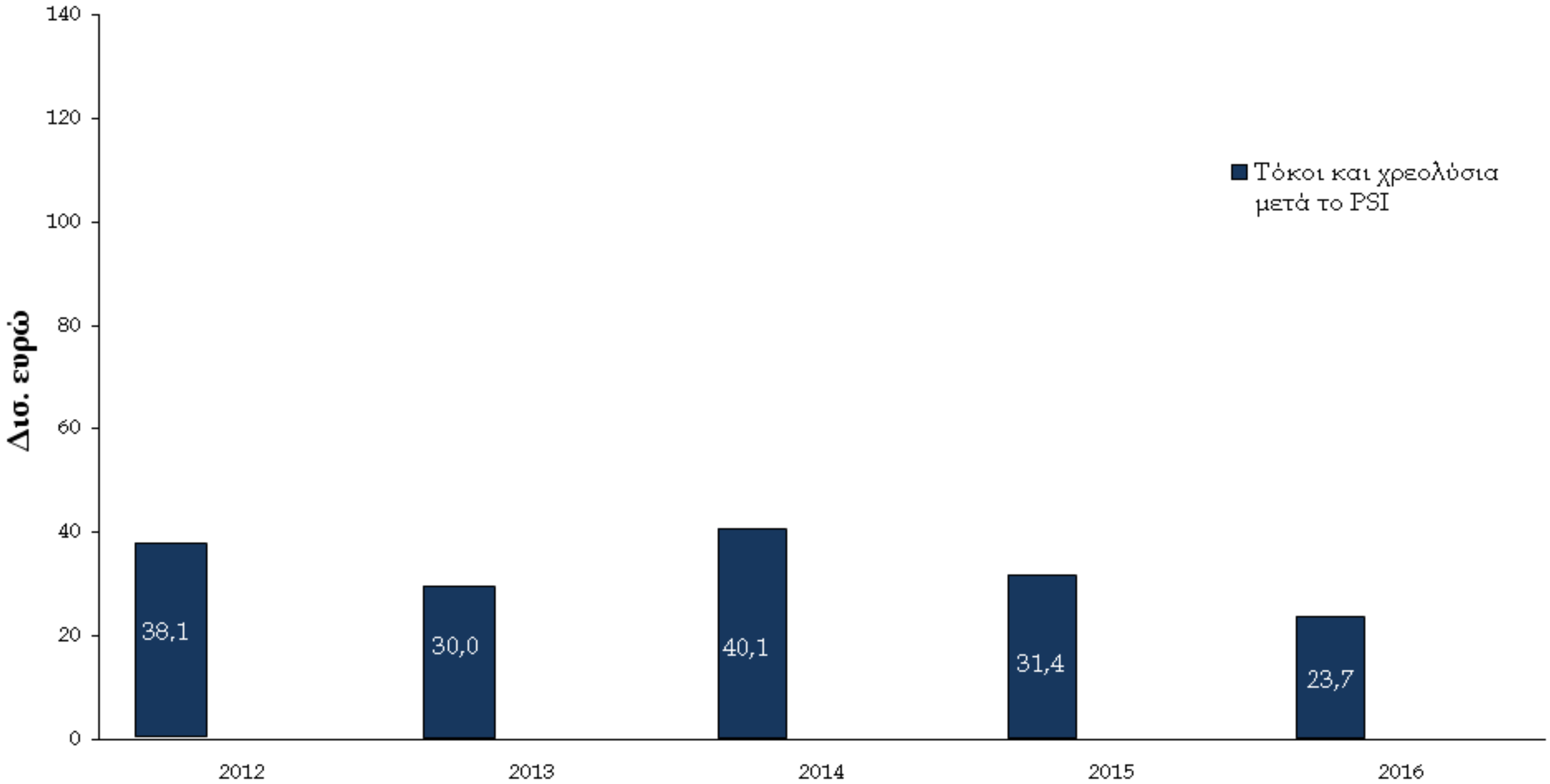
	2009	2010	2011	2012		2013	2014
				Prog.	Est.	Proj.	
	(Percentage change, unless otherwise indicated)						
Domestic economy							
Real GDP	-3.1	-4.9	-7.1	-6.0	-6.4	-4.2	0.6
Output gap (percent of pot. output)	7.3	3.3	-2.6	-7.3	-7.7	-10.6	-9.5
Total domestic demand	-5.5	-7.0	-8.7	-8.7	-10.4	-5.6	-1.1
Private consumption	-1.6	-6.2	-7.7	-7.7	-9.1	-6.9	-1.6
Public consumption	4.9	-8.7	-5.2	-6.2	-4.2	-4.0	-6.2
Gross fixed capital formation	-13.7	-15.0	-19.6	-14.4	-19.2	-4.0	8.4
Change in stocks (contribution)	-1.2	0.7	-0.4	0.4	0.0	0.4	0.0
Foreign balance (contribution)	3.0	3.0	2.4	3.3	3.7	2.6	1.7
Exports of goods and services	-19.4	5.2	0.3	-1.2	-2.4	3.0	4.6
Imports of goods and services	-20.2	-6.2	-7.3	-11.5	-13.8	-6.4	-1.9
Unemployment rate (percent) 1/	9.4	12.5	17.5	24.4	24.2	27.0	26.0
Employment 1/	-1.0	-2.7	-6.6	-9.2	-8.2	-3.7	0.6
Unit labor costs	4.2	-2.6	-4.3	-8.1	-4.2	-7.0	-1.5
Consumer prices (HICP), end of period	2.6	5.2	2.4	1.3	0.8	-0.6	-0.1
Consumer prices (HICP), period average	1.2	4.7	3.3	1.2	1.5	-0.8	-0.4
Core prices, period average 2/ 3/	2.3	2.6	1.1	...	-0.3	3.6	...
GDP deflator	2.3	1.1	1.0	-0.5	-0.8	-1.1	-0.4

Greece in an Austerity T rap

- Greece is an austerity trap, which moves from a decline in domestic demand, due to fiscal and incomes austerity, to negative growth that reduces tax revenues, which in turn trigger new spending and income cuts.
- Deviations from Troika's fiscal and growth targets create political pressures for deeper austerity.

Greece is also in a Default Trap due to the Non-Viable Bailout Agreement

Interest Payments and Amortizations after the PSI



Πηγή: IMF (2012)

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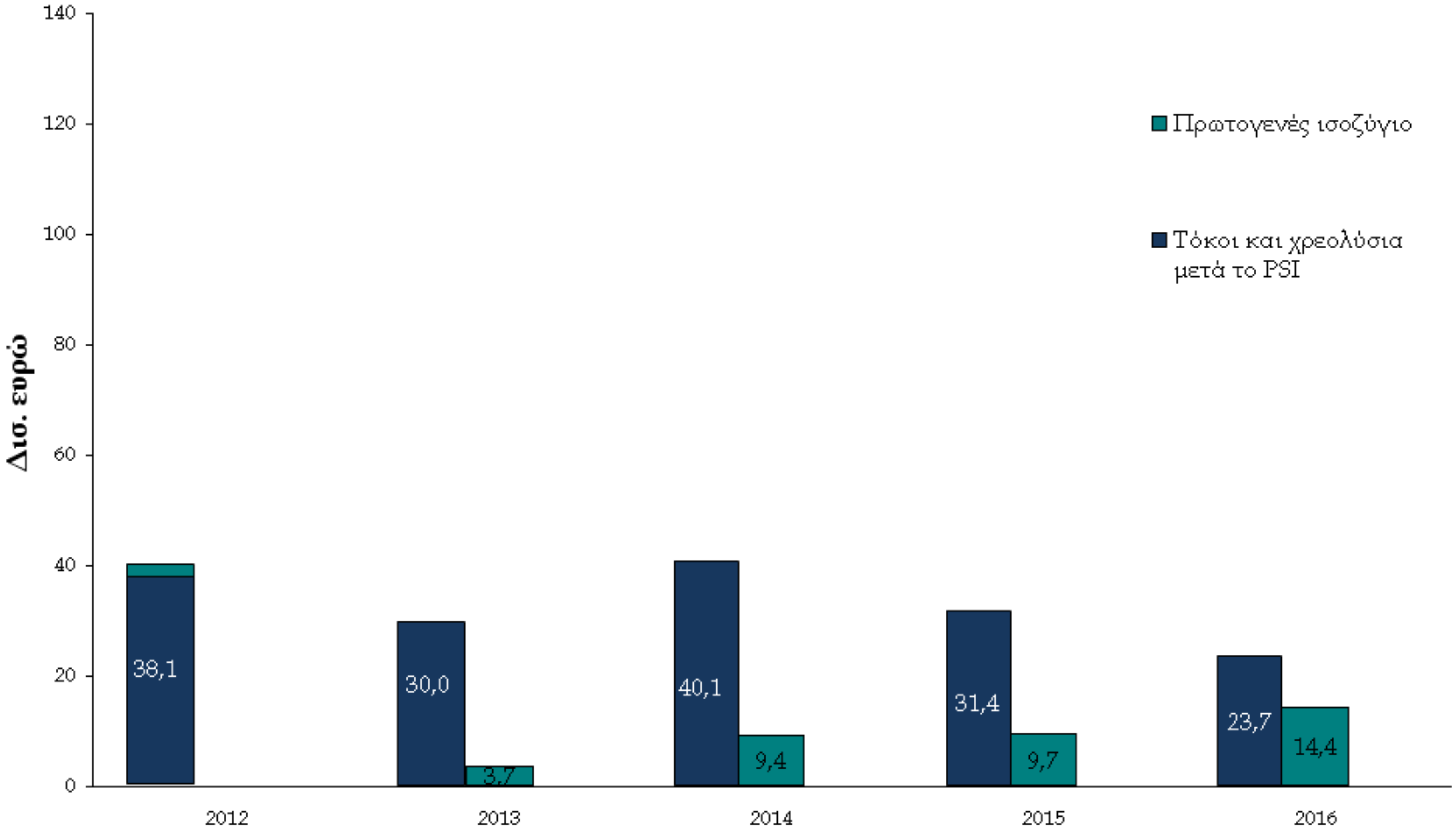
The Structure of Financing Greece's Debt Obligations



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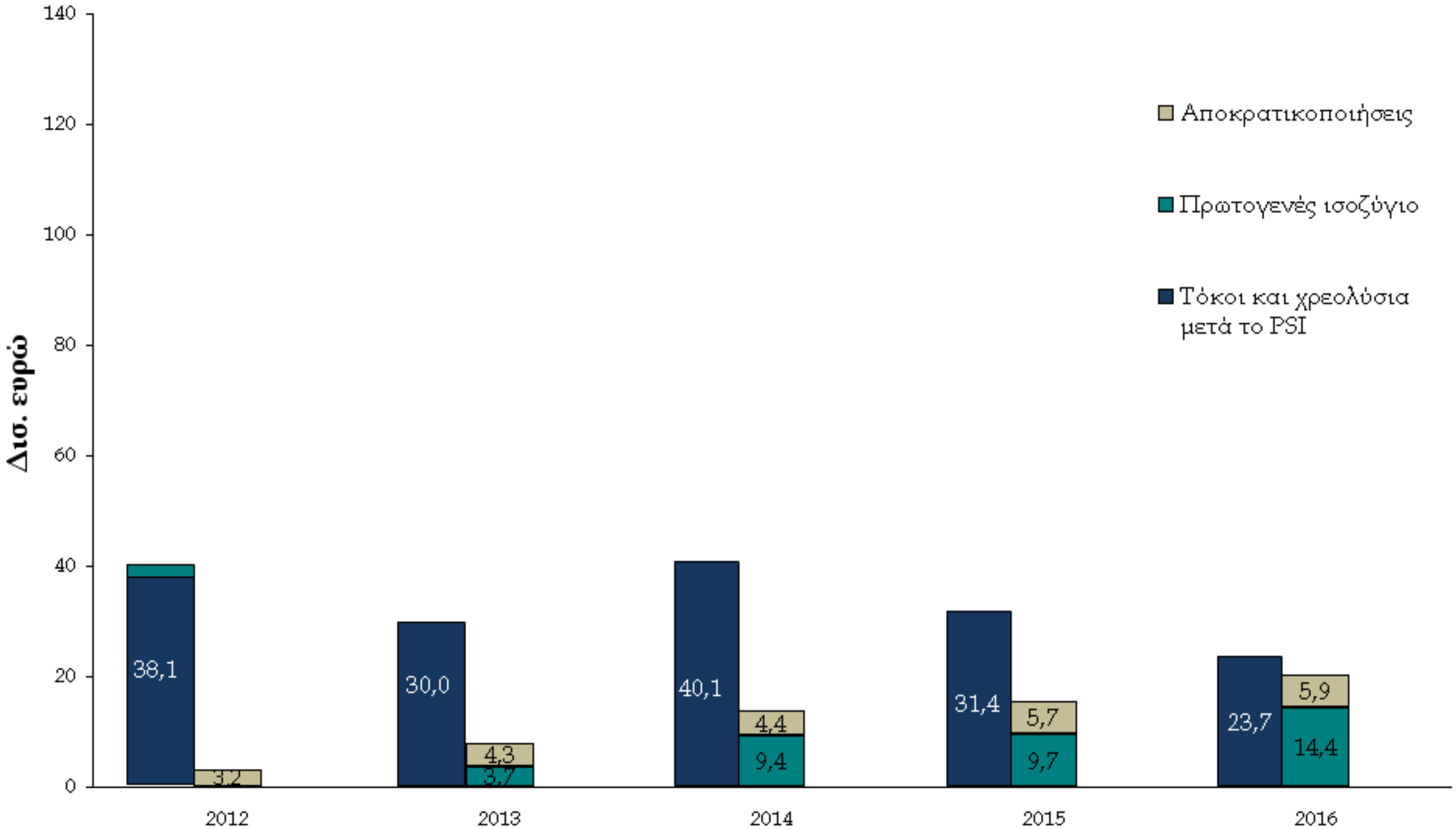

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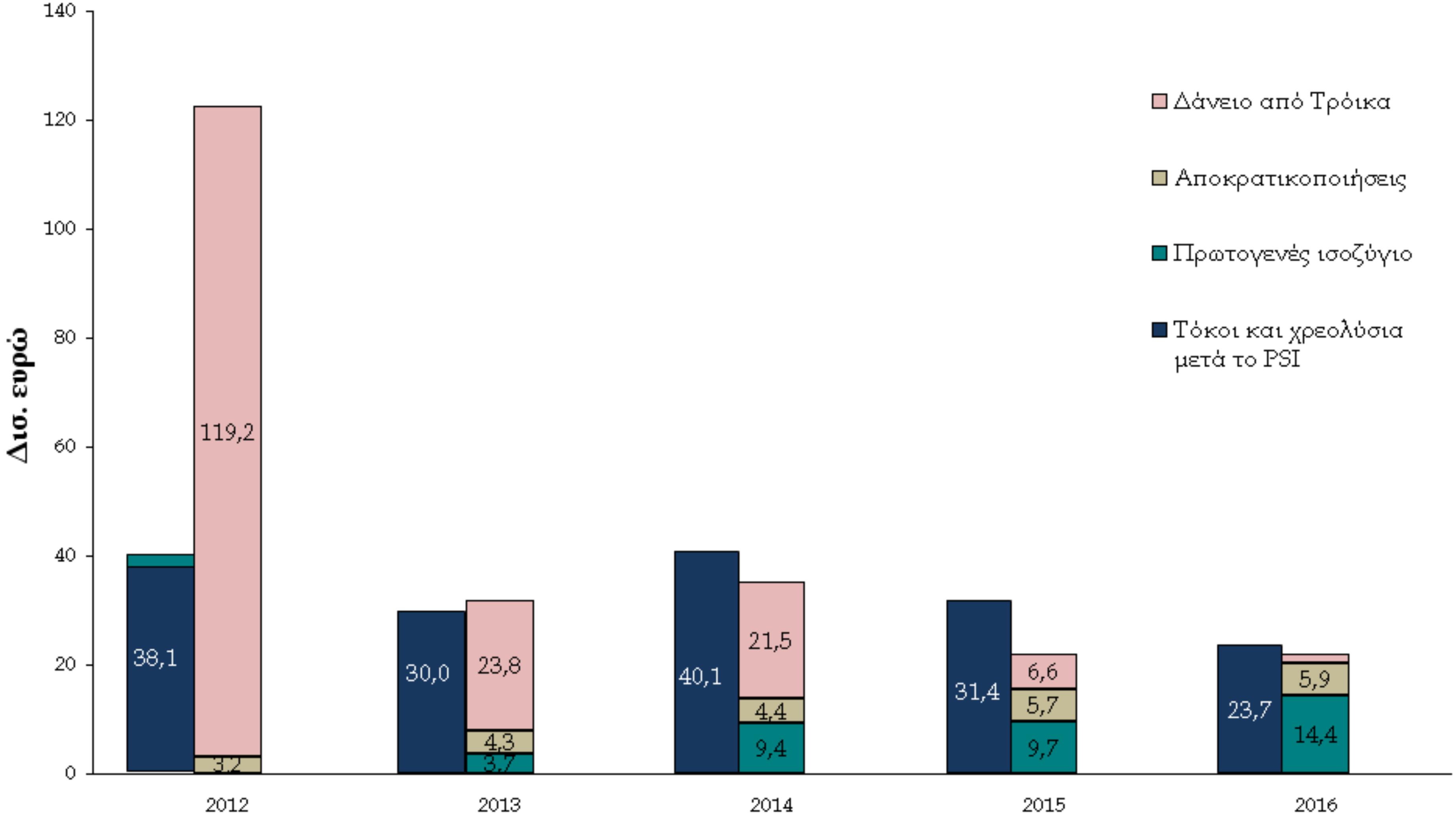

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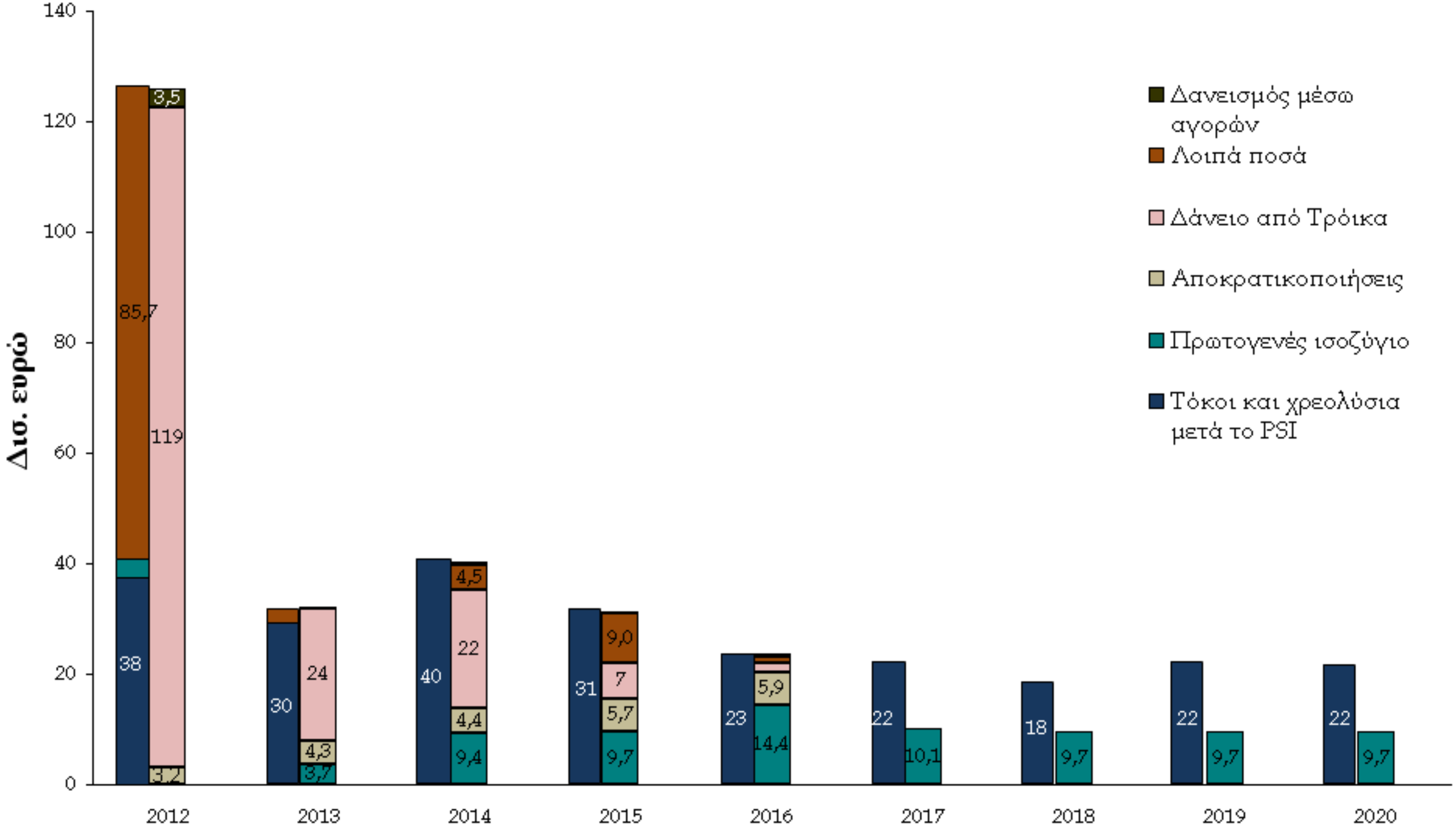

Πηγή: IMF (2012)

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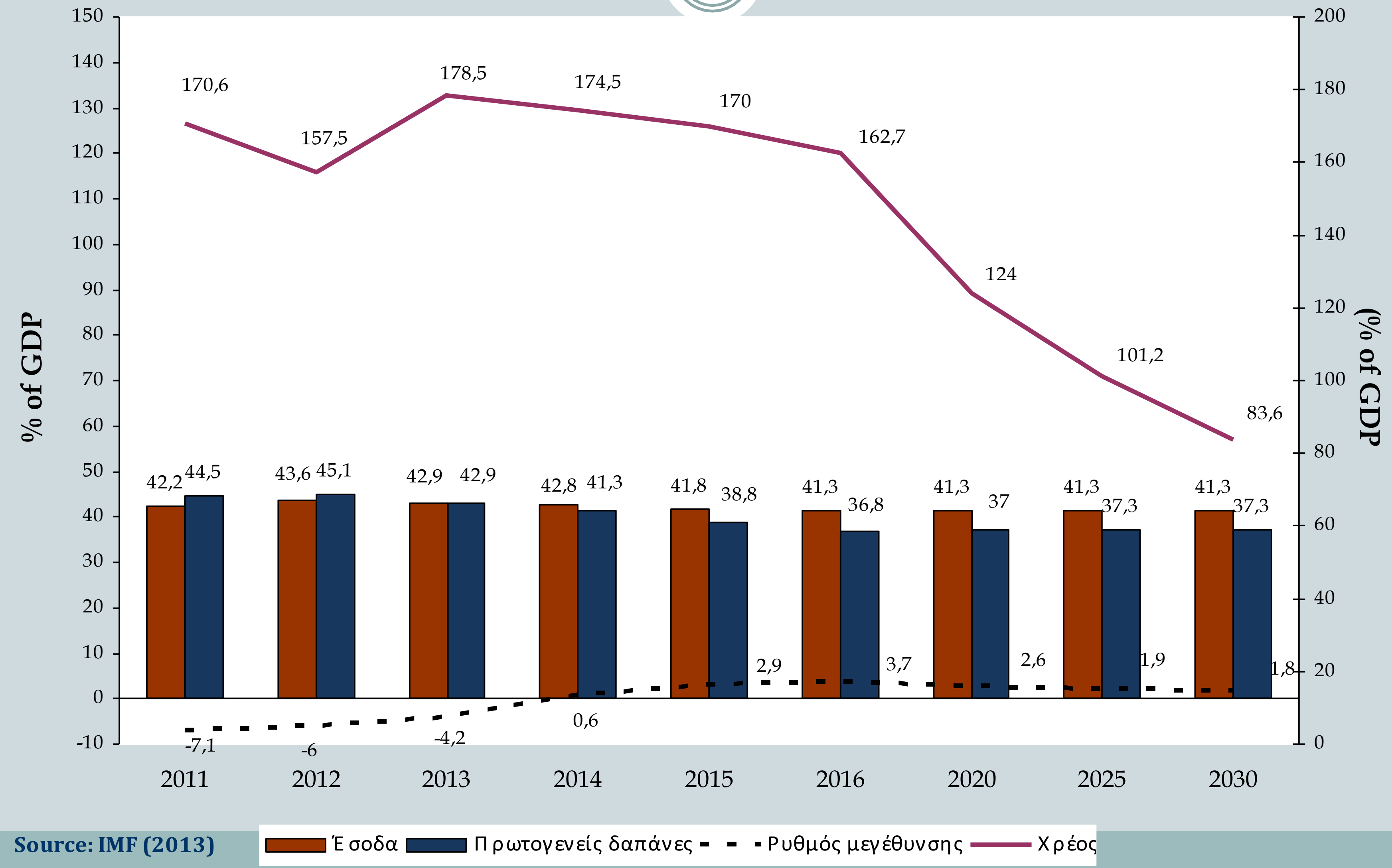
Greece's Devil's Triangle (the baseline scenario)



Source: IMF (2013)

Overall

- The default and the austerity traps form a vicious and self-defeating cycle of austerity and recession that:
  - trigger high currency risk expressed by the euro versus drachma dilemma,
  - increase the credit risk of the government sector,
  - destabilize the financial sector,
  - create liquidity and solvency problems that destroy growth and employment possibilities, and
  - cause detrimental prosperity effects for the vast majority of the population.

IMF again

- In the last report, IMF claims that the Adjustment program that Greece has to apply is necessary because it has helped the country to remain in the euro avoiding a disorderly default and has limited euro-wide contagion.

For how long?

Thank You