

# THE RESTRUCTURING OF THE GREEK ECONOMY 2010-2014

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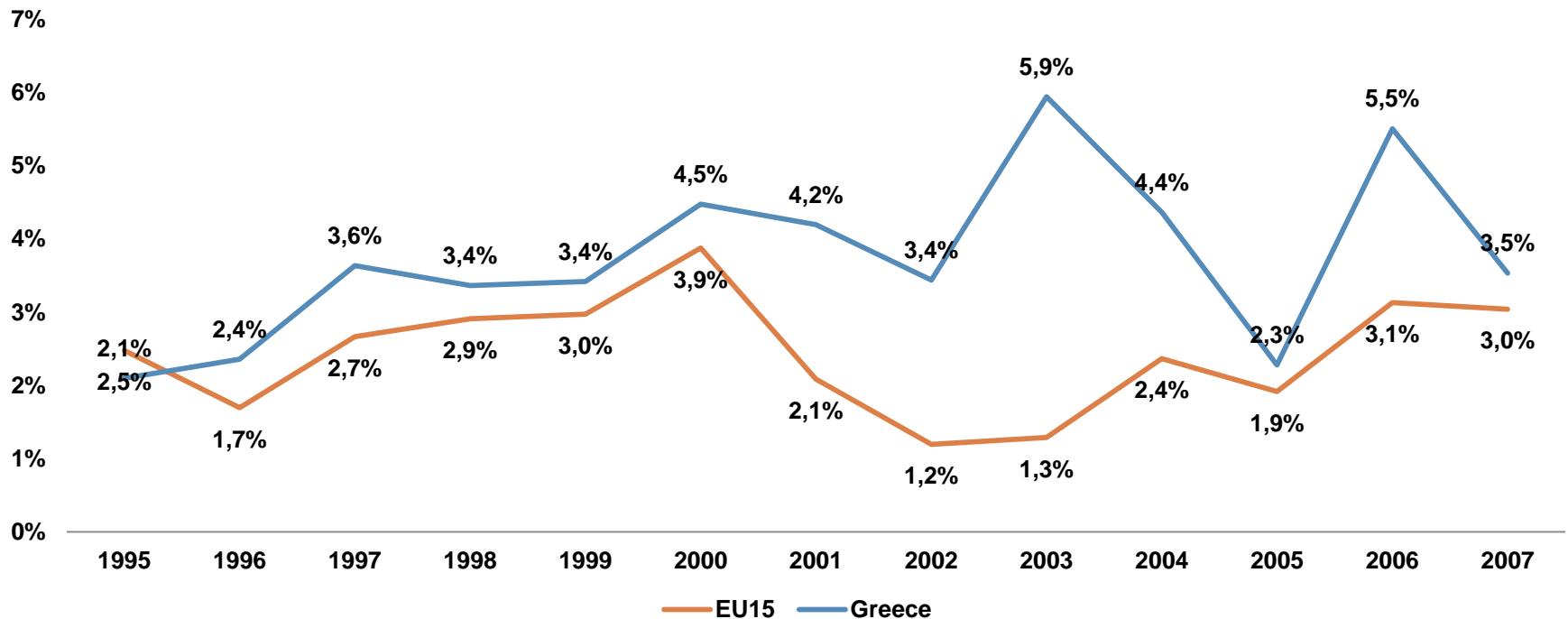
- Getting into the debt crisis
- Fiscal consolidation
- External rebalancing
- Recent developments
- Structural reforms
- Socioeconomic costs of adjustment
- Growth prospects and challenges

# High growth rates

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- From the mid-90's to the beginning of the crisis, the Greek economy was growing at a faster rate than the EU average (3.9% vs 2.4%)
- Growth model based on consumption and borrowing

## GDP growth rate

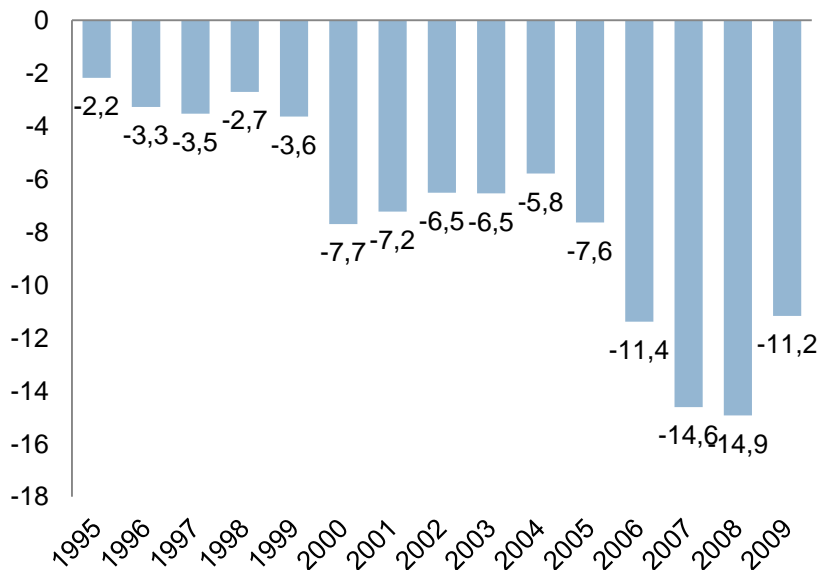


# Twin deficits

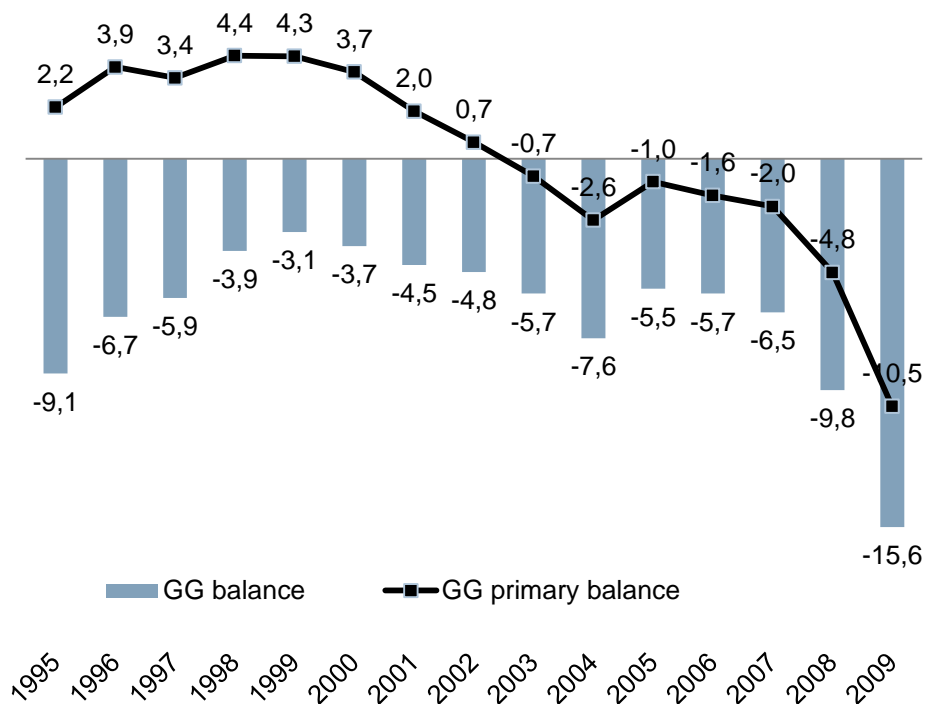
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- Typical case of “twin deficits”
- External deficit trended upwards in the period 1995-2008
- General Government Deficit, although contained before Euro accession, increased afterwards

**Current Account (% GDP)**



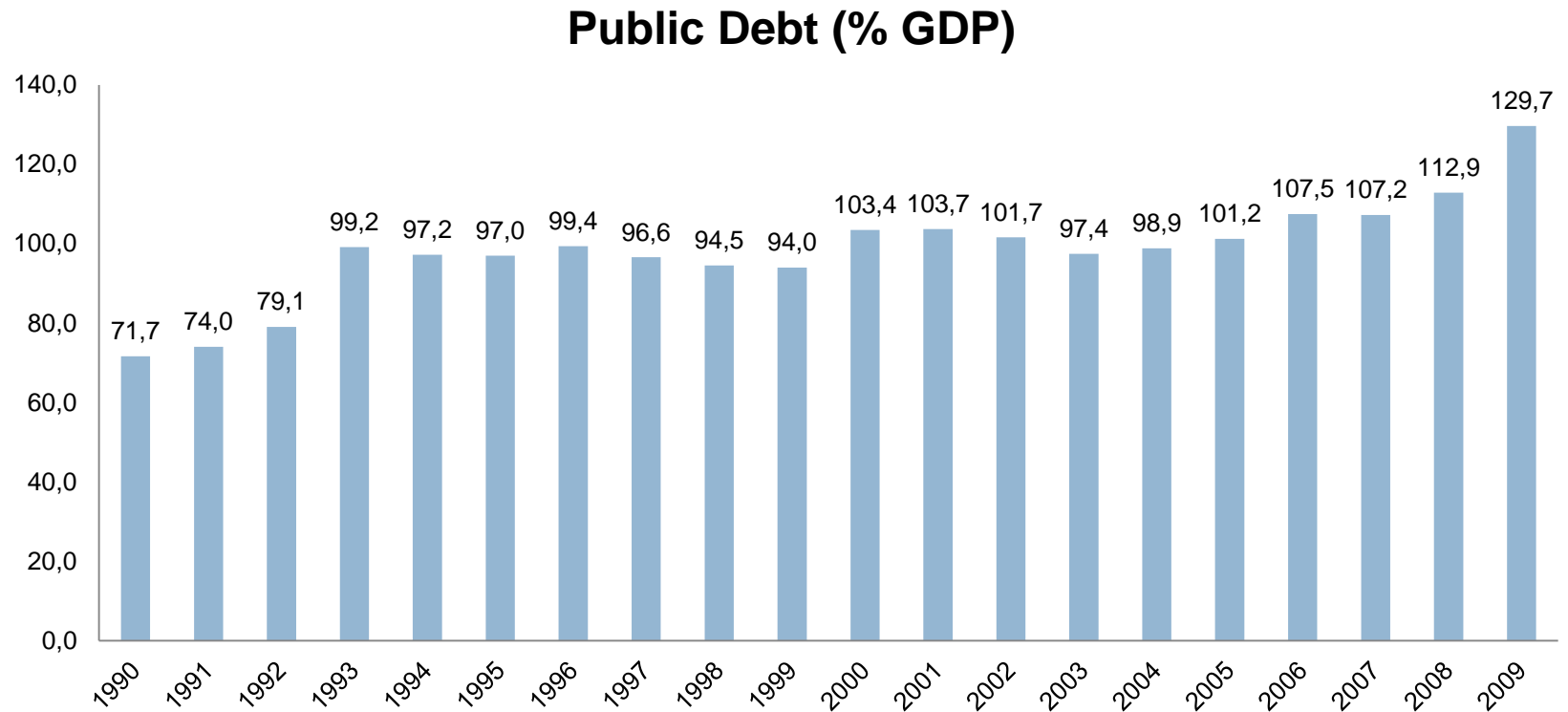
**General Government Balance (% GDP)**



# Public debt

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**In 1990-2009, public debt rose by 60 p.p. of GDP**



# Getting into the debt crisis

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- In 2010 Greece could not tap the international markets anymore
- Forced to seek borrowing from the European partners and the IMF
  - ▣ 245\* bn Euro (221 bn Euro already disbursed)
    - ▣ 198 from Euro Area countries
    - ▣ 47 from the IMF\*
    - ▣ Private sector Involvement (PSI) to reduce the public debt by 107 billion EUR via bond swapping
- The global financial crisis revealed the chronic problems of the Greek economy
  - Structural rigidities
  - Growth model based on consumption and borrowing

\*Approx. 18 bn refer to IMF's rollover and thus don't add up to the public debt

- Getting into the debt crisis
- **Fiscal consolidation**
- External rebalancing
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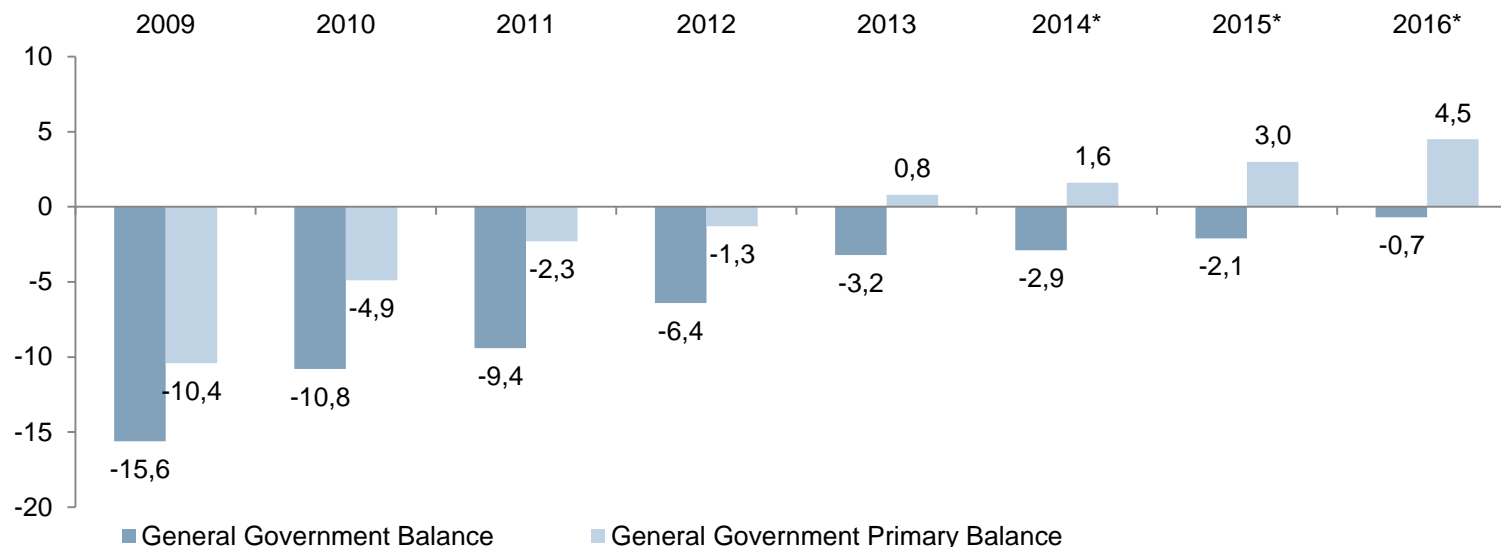
# Fiscal adjustment

\*

In 2009-2013,

- General Government Deficit shrank by 12.4 p.p. of GDP
- General Government Primary Deficit shrank by 11.2 p.p. of GDP, over-performing the Program target for 2013 by 0.8 p.p. of GDP

General Government Fiscal Accounts 2009-2016  
(% of GDP)



\* Economic Program Targets

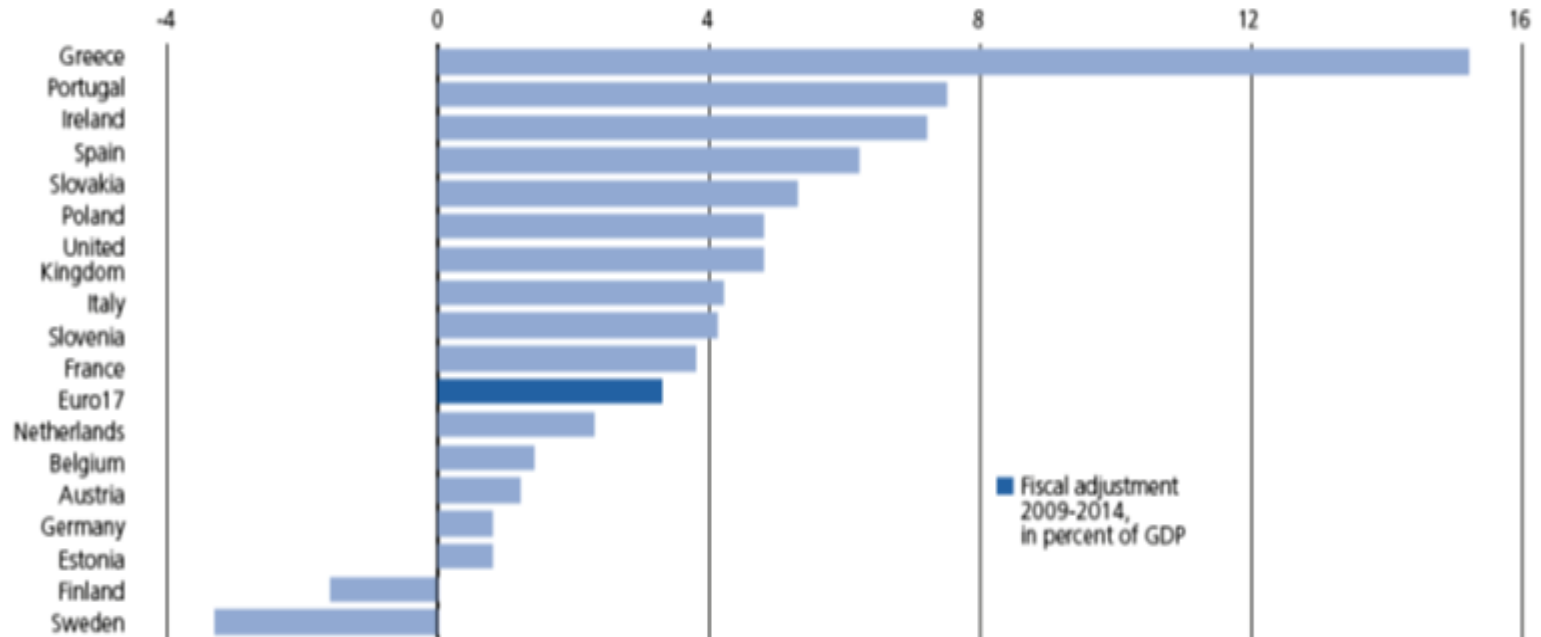


# The biggest cumulative fiscal consolidation in the EA

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In 2009-2014 Greece achieved the biggest cumulative change in the primary fiscal balance in the Euro area

Cumulative change in the primary fiscal balance 2014 over 2009  
(% of GDP)

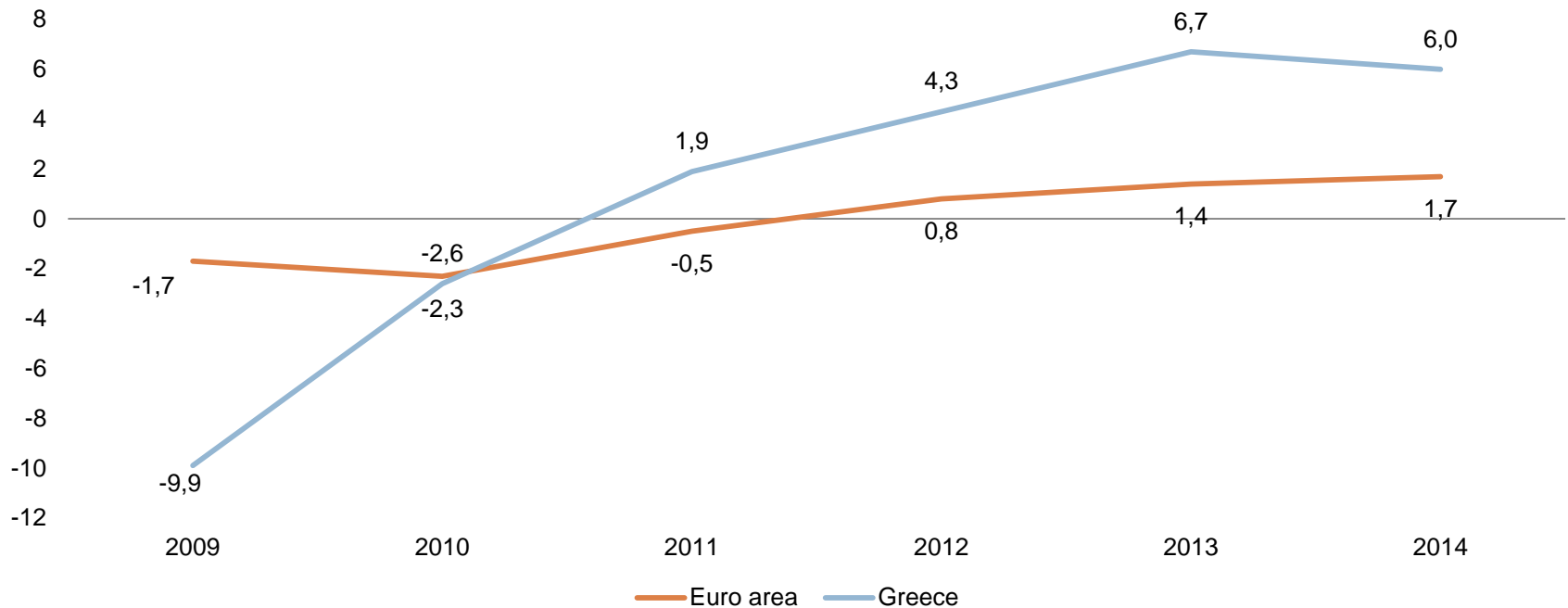


# Fiscal consolidation was carried out in strong pro-cyclical conditions

\*

**Cyclically adjusted primary balance improved by more than 17 p.p. of GDP in 2009-2013 – substantially higher than the EA average**

**Cyclically Adjusted Primary Balance (% GDP)**



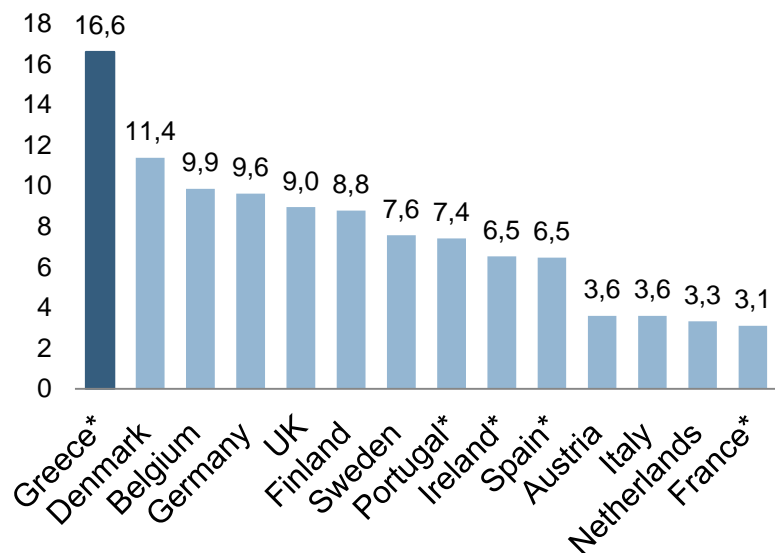
Note: Primary balance defined according to Economic Program

Source: European Commission, Winter Forecast 2014 and 4<sup>th</sup> Review 4/2014

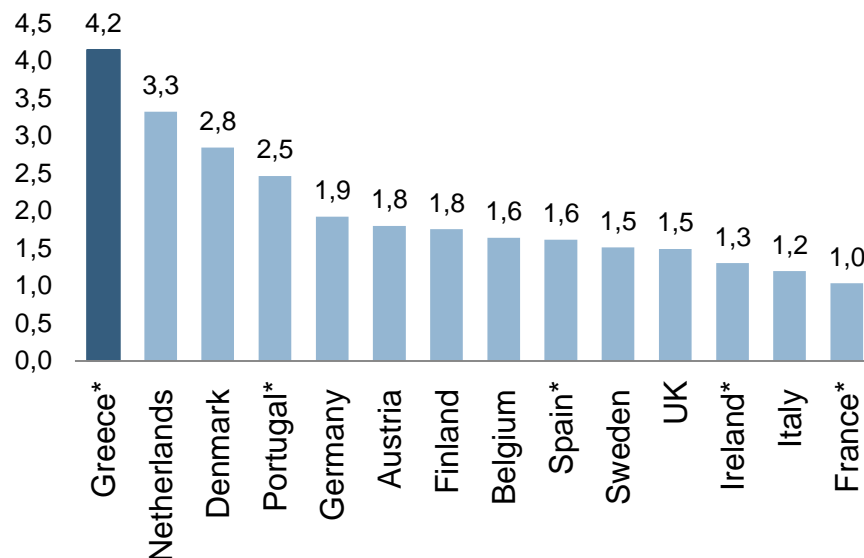
# The biggest and fastest fiscal consolidation among OECD countries

\*

Scores of cyclically adjusted primary balance improvement (% GDP)



Rate of average annual cyclically adjusted primary balance improvement (% GDP per year)



In 2009-2013 Greece achieved the highest and fastest cumulative fiscal consolidation in the developed world in recent years:

✓ of 16.6 p.p. of GDP

✓ at an annual rate of 4.2 p.p. of GDP on average

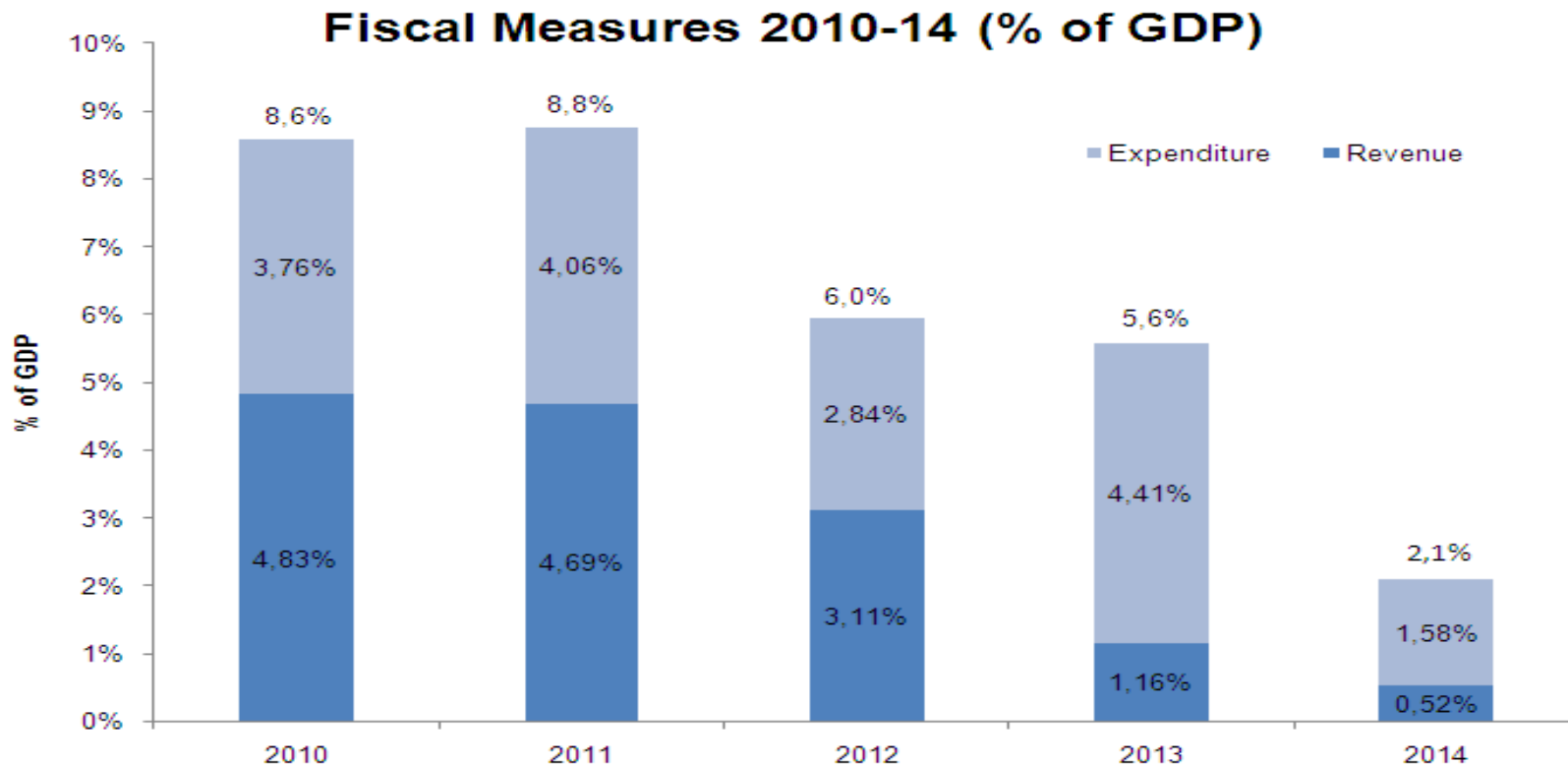
Note: Fiscal consolidation episodes as defined in OECD Economic Outlook 81

Source: AMECO, \* excludes financial sector support

# Measures amounting to over 30% of GDP

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...equally split between expenditure cuts and revenue increases

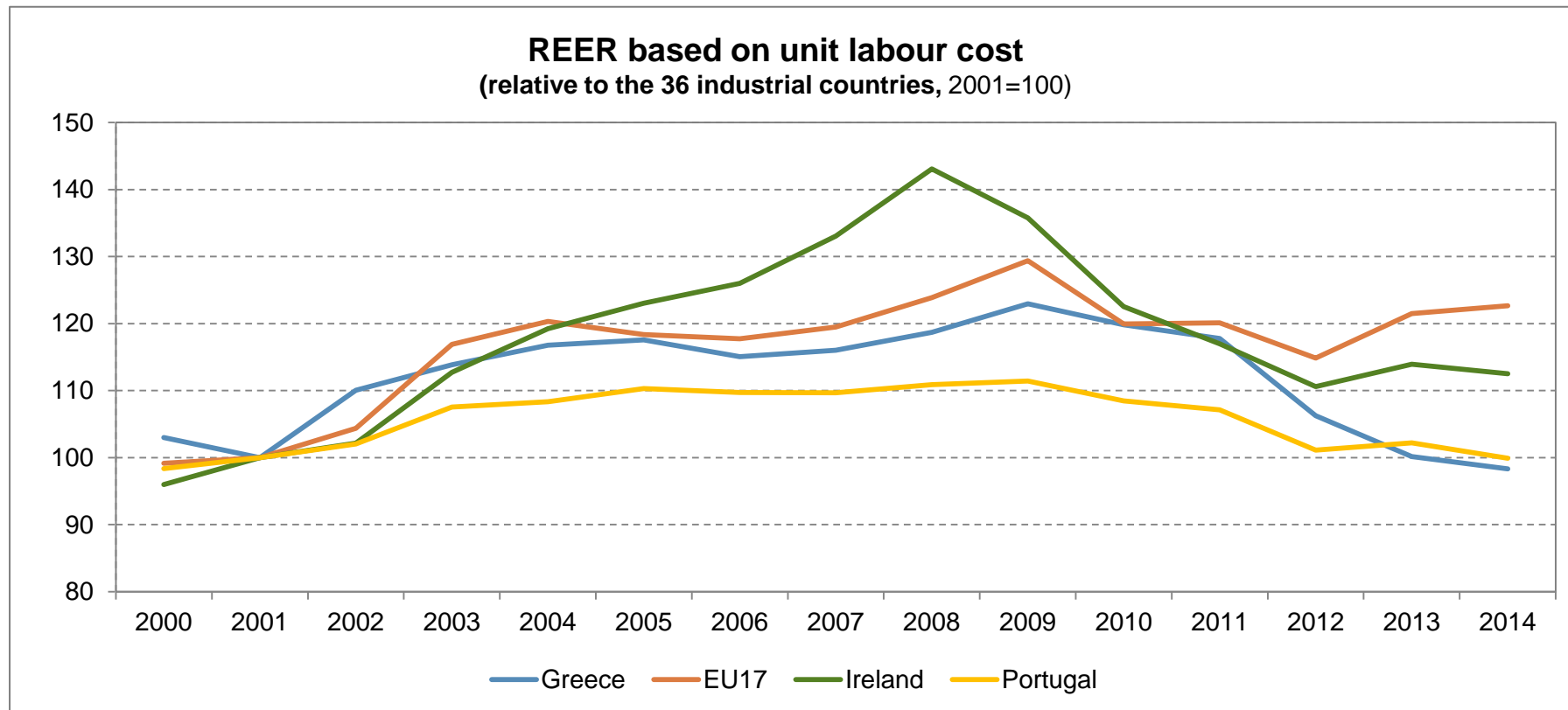


- Getting into the debt crisis
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# Labour cost competitiveness is recovering

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Between 2010 and 2013 Greece managed to regain the labour cost competitiveness lost during 2000-09

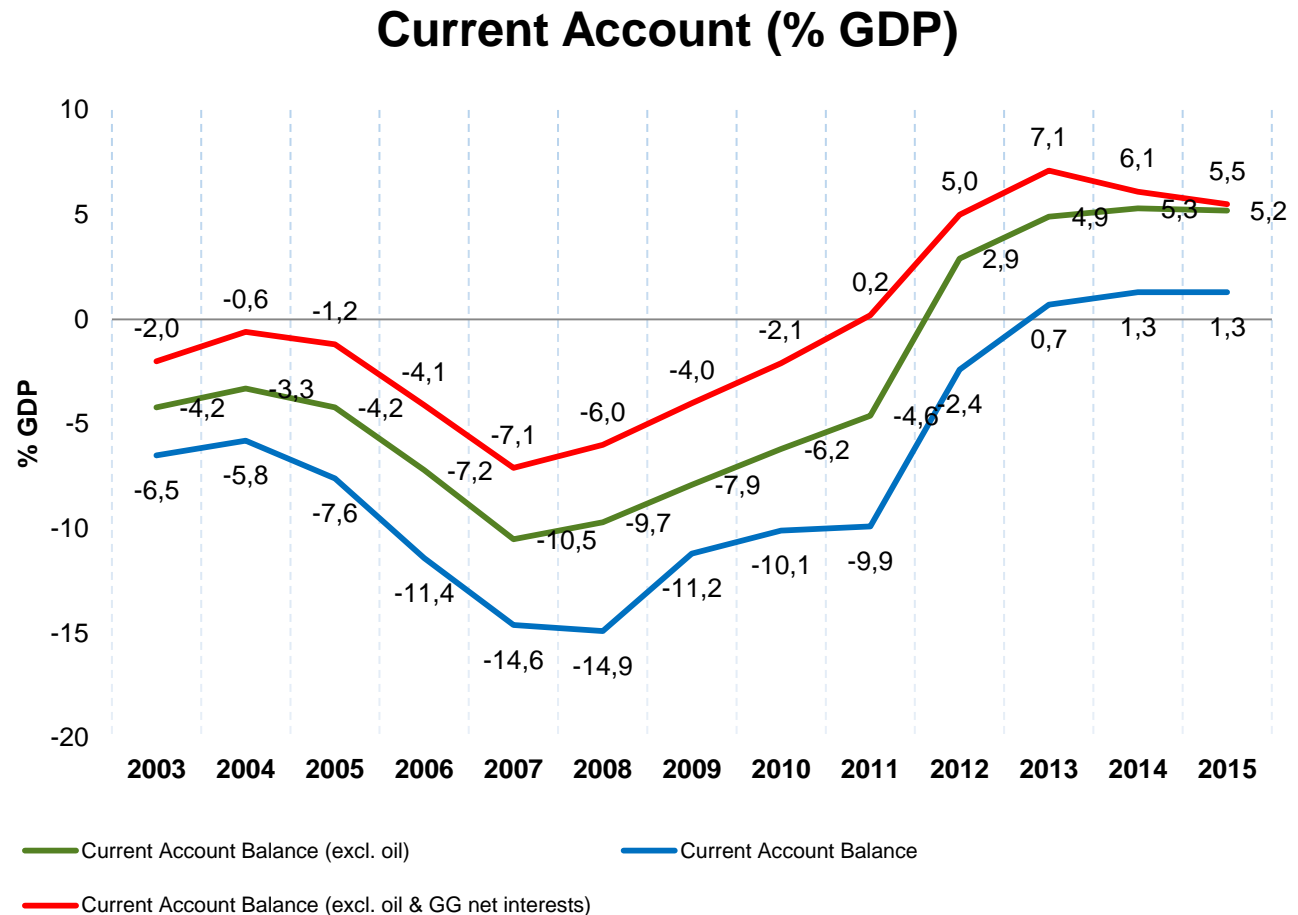


# Current account deficit has been eliminated

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Current Account Deficit fell by 15.6 p.p. of GDP between 2008 and 2013

Current Account in surplus in 2013 for the first time after many decades



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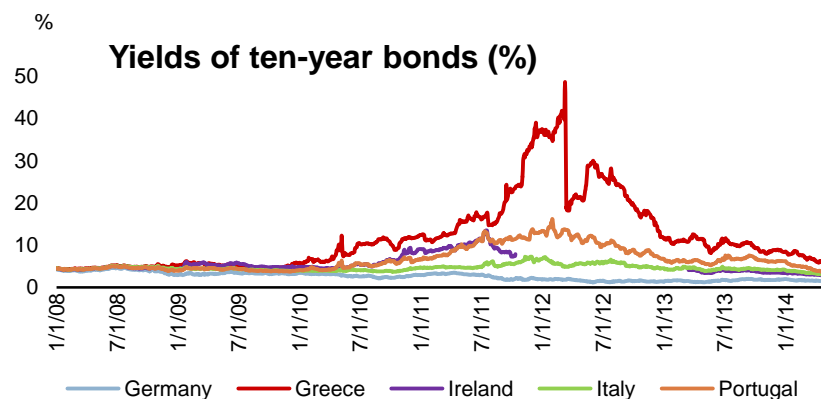


# Recent developments 1/2

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## Performance in 2013 better than expected:

- -3.9% GDP growth compared to expected -4.2%
- Unemployment rate declined in the last three quarter of the year after more than three years of constant increases
- General Government balance -3.2% of GDP compared to a target of -4.1%
- General Government primary surplus 0.8% of GDP compared to a target of 0%
- 0.7% GDP surplus in the Current Account compared to expected -0.8%
- €5.8 billion of public sector expenditure and tax refund arrears to private enterprises and households cleared.
- 10-year bond yields declined by 298 bps



Source: Bloomberg

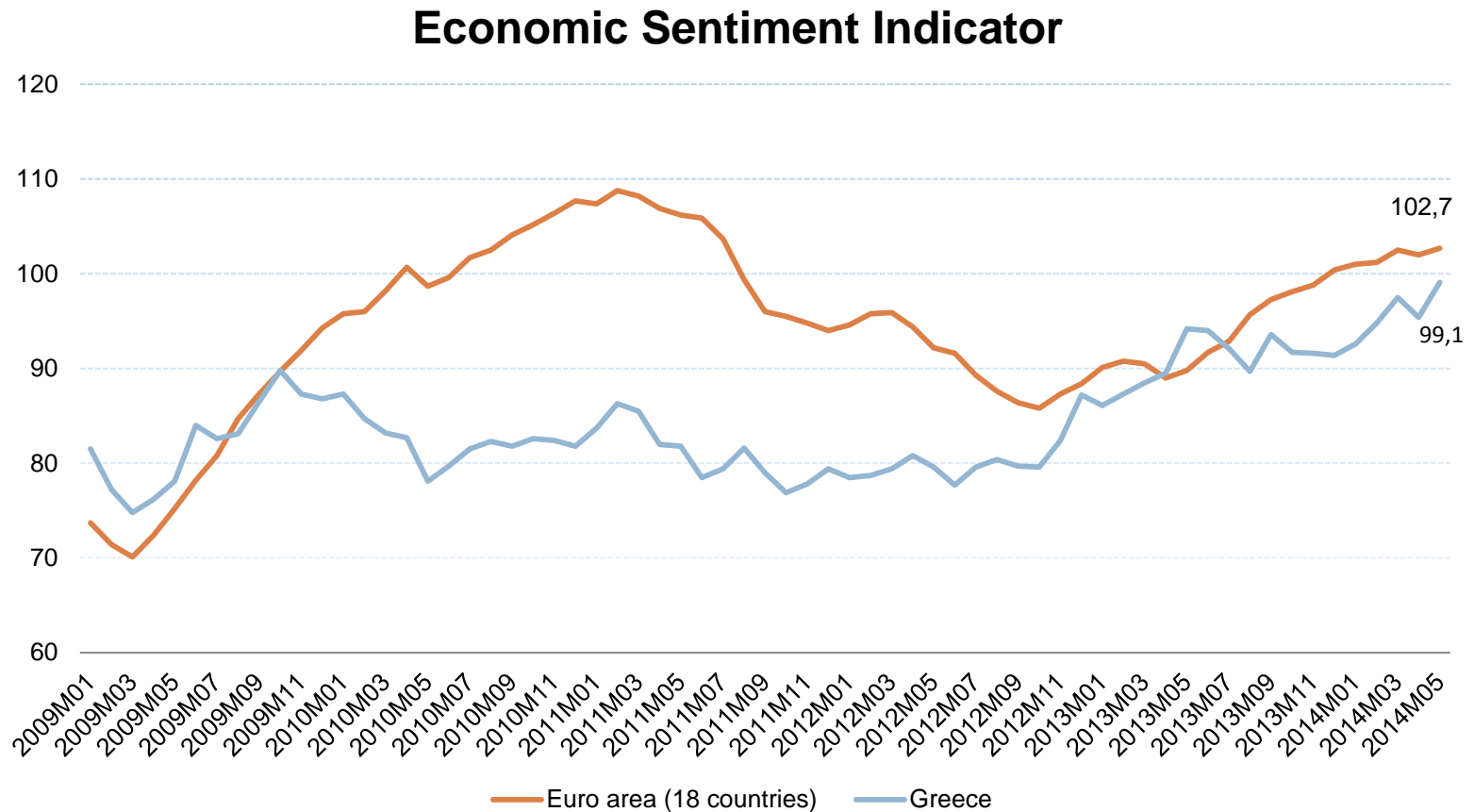
# Recent developments 2/2

\*

## Performance in 2014 is also promising:

- -1.1% GDP growth in Q1 2014 compared to -6.0% in Q1 2013
- -1.0 bn Current Account deficit in Q1 2014 compared to -2.2 bn in Q1 2013
- Unemployment rate remains on a decreasing path (1.2 p.p. cumulative decline since peak)
- General Government deficit €-2.8 bn in Jan-Aug 2014 compared to a target of €-4.1 bn
- General Government primary surplus €1.9 bn in Jan-Aug 2014 compared to a target of €1.9 bn
- 10-year bond yields declined further by 240 bps
- In April, after four years with no access to the international capital markets, the Greek sovereign raised €3 bn at a coupon rate of 4.75% through the sale of 5-year bonds that was almost seven times oversubscribed  
*Further issuance of €1.5 bn in 3-yr paper in July, plus another €1.7 bn (5-yr and 3-yr) in exchange of T-bills in September*
- In Q1 2014, the four systemic banks raised additional capital of €8.5 bn, comfortably in excess of the needs identified by the supervisor (€6.4 bn) and all of them have placed medium-term bonds for the first time since 2009 to boost their liquidity (€2.25 bn in total).

# Economic sentiment is improving



- Getting into the debt crisis
- Fiscal consolidation
- External rebalancing
- Recent developments
- **Structural reforms**
- Socioeconomic costs of adjustment
- Growth prospects and challenges

# Overview of structural reforms (1/5)

\*

## **Important reforms undertaken in all sectors of economic activity**

Indicatively:

### **Pension system**

- Radical reform with pension benefits tightly linked to lifetime contributions
- Increase in statutory retirement age by 2 years (from 65 to 67)
- Pension fund consolidations
- Clear separation of social insurance and social assistance functions
- Among the most viable pension systems in EU according to EC peer review
- Introduction of strict budget neutrality rules for supplementary pensions and lump sum pensions

### **Social protection**

- Increased use of means-testing for the provision of benefits
- Pilot scheme for the introduction of a minimum income guarantee scheme
- Redesigning of activation policies focused especially on long-term unemployed

# Overview of structural reforms (2/5)

\*

## Health system

- Incorporation of eight social insurance funds into a single organization, covering almost the entire population
- Introduction of automatic claw-back mechanisms for pharmaceuticals, diagnostics and private clinics to ensure compliance with spending ceilings
- Wider use of generics/off-patent pharmaceuticals (with benchmarking to EU)
- Establishment of e-prescription system for pharmaceuticals and diagnostic tests and increase in co-payments

## Labour market

- Average public sector salary cut by 23% between 2010-2012
- 22% reduction in minimum wage (32% for young workers)
- 11% cut in social security contribution rates
- Facilitation of collective bargaining at the firm level
- Significant cut in severance payments
- Complete overhaul of the mediation-arbitration system
- Facilitation of flexible forms of employment (fixed term, part time, rotation etc).

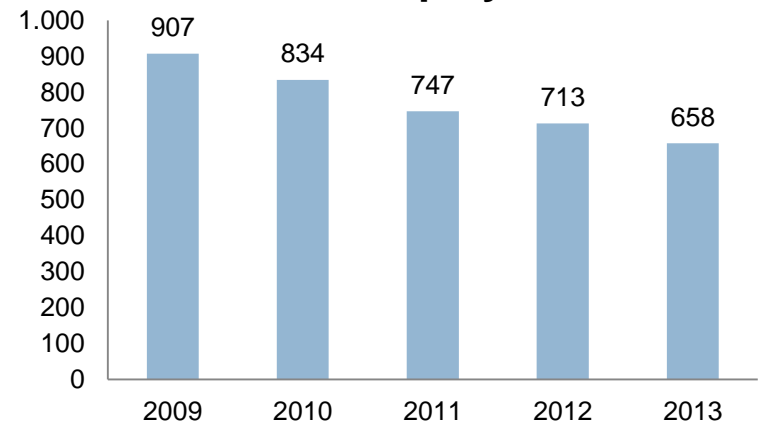
# Overview of structural reforms (3/5)

\*

## Public administration

- Drastic reduction in public sector employment from over 900,000 in 2009 to less than 660,000 in 2013
- Introduction of unified wage grid, staffing and evaluation plans for the entire public sector
- Establishment of mobility scheme, including mandatory exits
- Rapid expansion of e-government

### 27.4% reduction of public sector employees



## Fiscal Structural

- A complete new fiscal framework in line with the new EU governance framework, envisaging multiannual planning, binding expenditure ceilings, numerical fiscal rules and strong expenditure monitoring mechanisms.
- Introduction of automatic corrective mechanisms when targets are missed for Central Government, State-owned Enterprises and Local Government.
- Establishment of an independent Fiscal Council

# Overview of structural reforms (4/5)

\*

## **Tax system**

- Establishment of a semi-autonomous post of General Secretary for Tax Administration with sweeping powers to tackle tax evasion legacy
- Tax code simplification and repeal of the Code of Books and Records
- New IT system interconnecting all tax offices and compulsory electronic submission of tax declarations
- Full scope audits according to risk-based criteria.
- Consolidation of tax offices into larger units and compulsory rotation of the heads of local tax offices
- Creation of 23 tax-related court units



# Overview of structural reforms (5/5)

## **Competition**

- Sweeping market liberalization with particular emphasis on retail trade, tourism, construction materials, food processing, road haulage and energy markets
- Opening up of “closed” or regulated professions
- Elimination of minimum fees for services
- Abolition of cabotage rules related to cruise vessels

## **Business environment**

- “One-stop-shop” to set up a business in 1 day
- Removal of the 30 most important barriers to entrepreneurship
- Fast track process for investments.
- Simplification and modernization of the customs procedures

# Privatizations

\*

## Portfolio Structure of HRADF (Privatization Agency), September 2014

Asset Category	Number
Corporate Assets	10
Infrastructure Assets	22
Real Estate	1000

## Project execution

Privatization tenders		September 2013	September 2014
	Completed	7	17
	In progress	11	19
	Under preparation	22	13

Total transaction value €5bn, of which €3bn already received

# The international ranking of the Greek economy regarding structural reforms is improving quickly

\*

## **“Product Market Regulation” indicator (OECD) from 2008 to 2013**

- ✓ 5 positions improvement
- ✓ Greece is the country with the biggest improvement

## **“Doing Business” (World Bank) from 2009 to 2013 improvement by**

- ✓ *97 positions in “starting a business”*
- ✓ *70 positions in “protecting investors”*
- ✓ *24 positions in the “ease of doing business”*
- ✓ *9 positions in “paying taxes”*

## **“Adjustment Progress Indicator” (Lisbon Council & Berenberg Bank)**

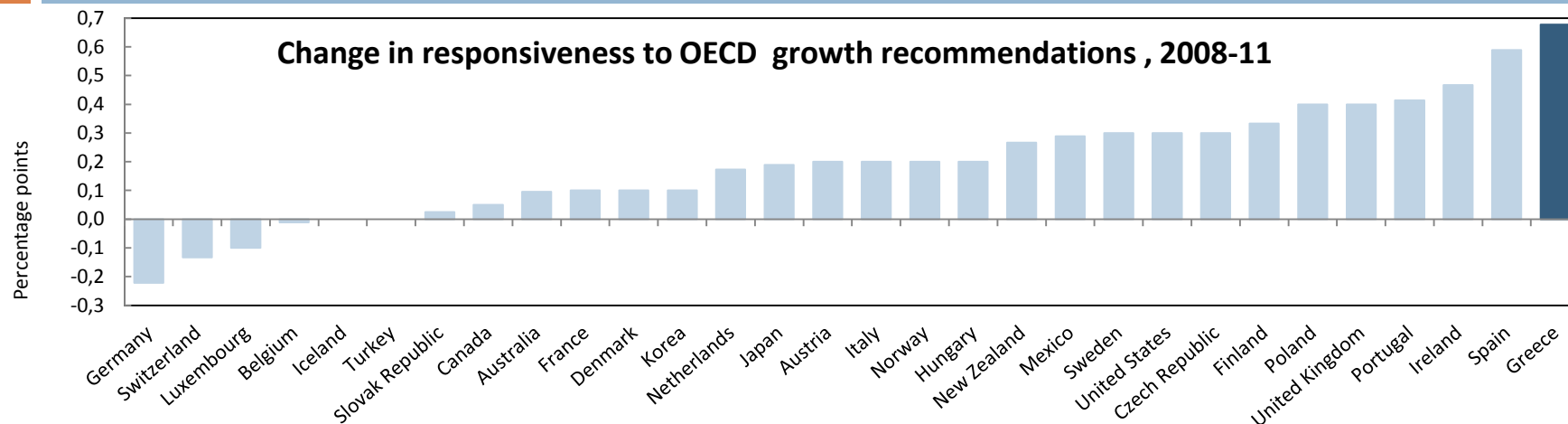
- ✓ *Greece ranks 1<sup>st</sup> in 2012, 2013 and 2014*

## **“Strictness of Employment Protection indicator” (OECD)**

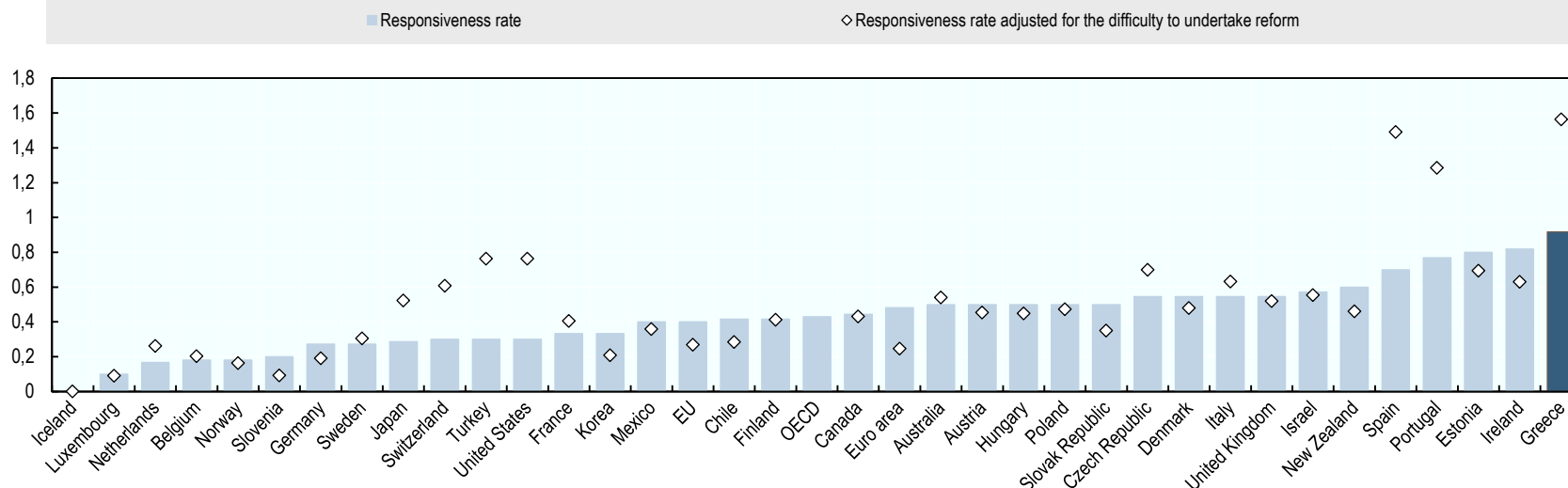
- ✓ *10 positions improvement (from 2008 to 2013)*

# Greece is changing fast

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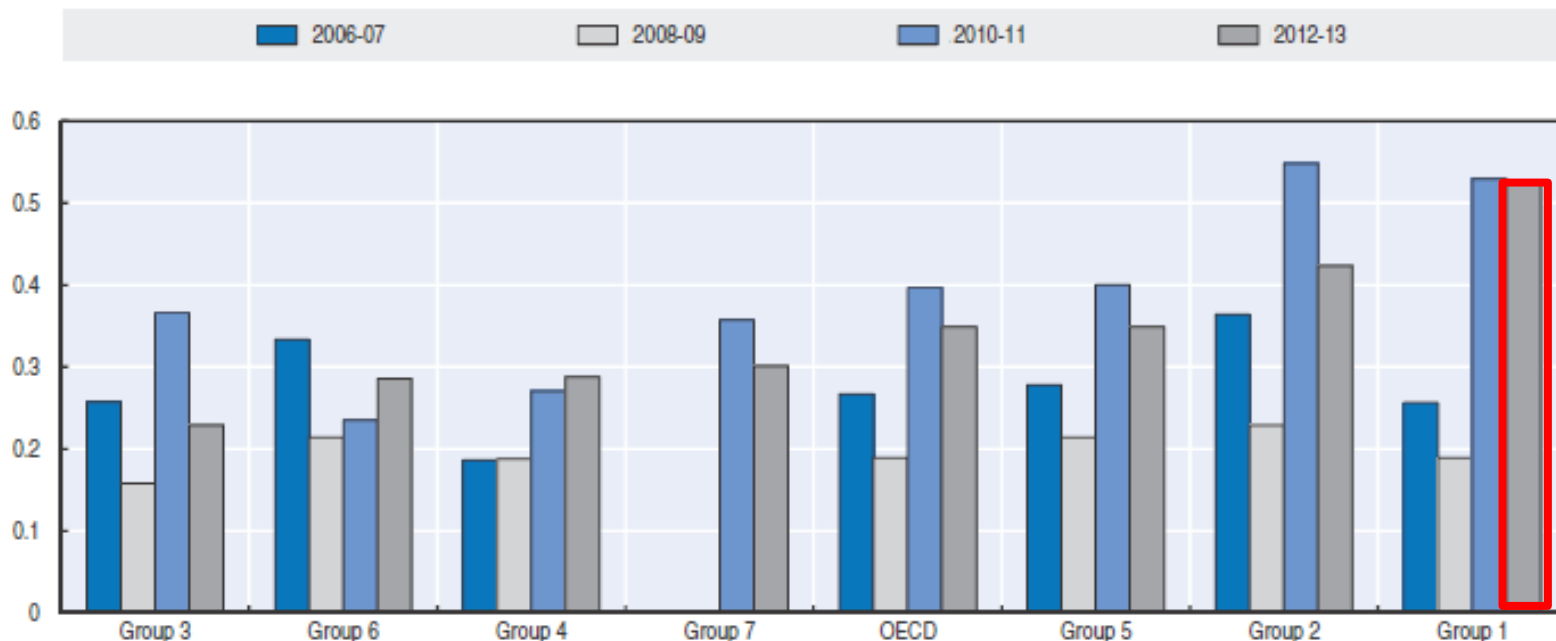
**Responsiveness to Going for Growth recommendations across OECD countries, 2011-12**



# Greece is changing fast (cont.)

- Similar picture in latest “Going for growth report”, but no country rankings
- Best performance in 2012-2013 by “Group 1” countries (Greece, Italy, Portugal, Slovenia & Spain)
- Implicitly, main driving force in sub-indicators: Greece

Figure 1.11. **Reform activity in structural policies**  
Reform responsiveness to past *Going for Growth* recommendations



Source: OECD, Economic Policy Reforms: *Going for Growth Interim Report* 2014

# Structural reforms continue

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**Further reforms planned for many areas with emphasis placed primarily on:**

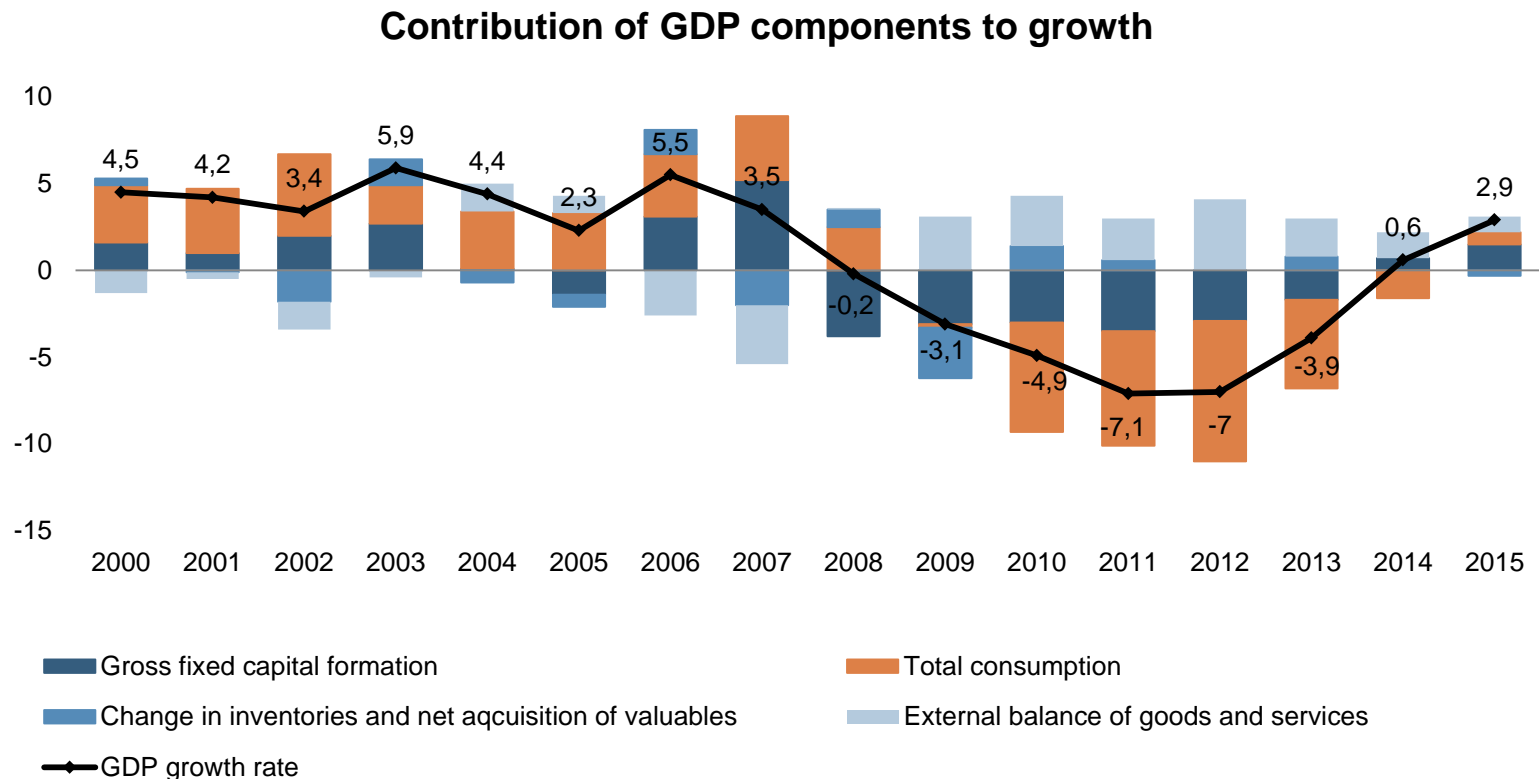
- Further market liberalization with emphasis on wholesale trade, manufacturing, telecommunications and e-commerce (*new OECD “toolkit”*)
- Further reforms to reduce the administrative costs to the firms
- Business environment improvement including simplification of investment licensing, upgrading logistics, streamlining rules for land use, liberalizing residential rentals, opening up regulated professions
- Key steps in network industries: transport liberalization, ambitious reform of energy markets
- Public Administration modernization
- FDI attraction

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- **Socioeconomic costs of adjustment**
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# Adjustment has come at a very high socio-economic cost

\*

Between 2008 and 2013 the Greek economy has lost almost 25% of GDP but is expected to start growing again in 2014



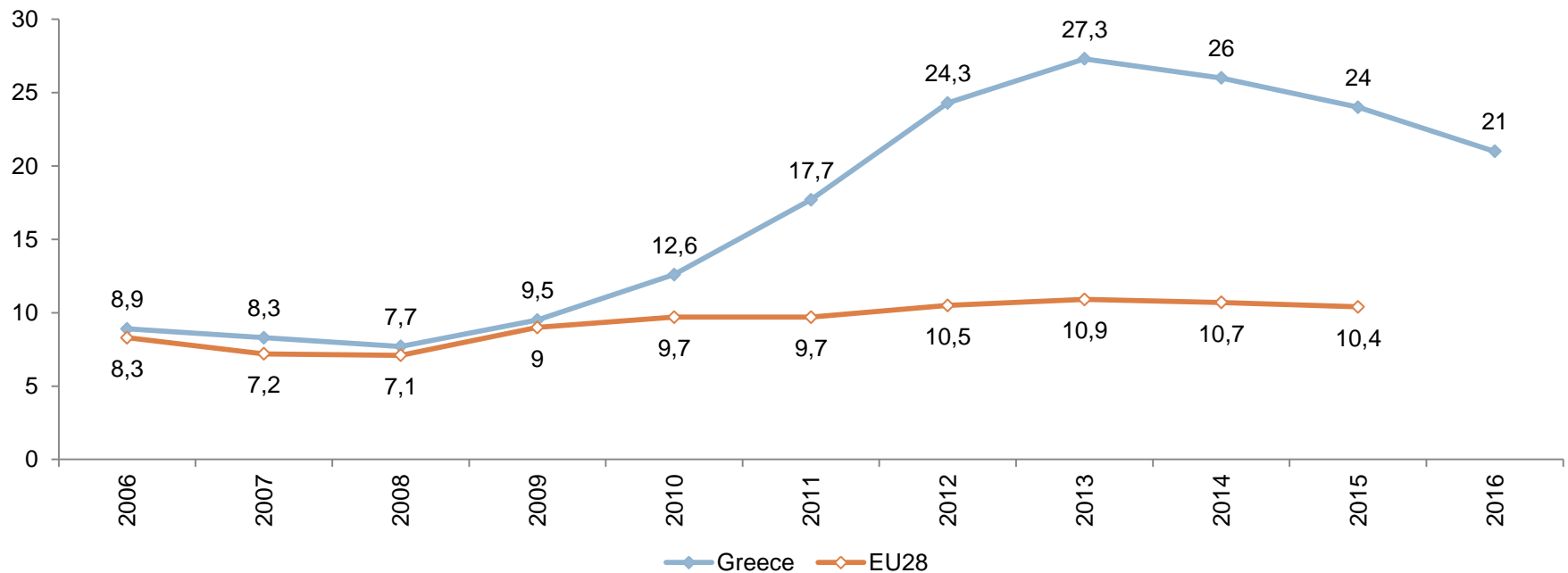


# Unemployment has skyrocketed...

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- Unemployment in 2013 above 27% of the labour force
- Youth unemployment the highest in the Euro-area (58%)
- Long-term unemployed 18% of the active population or 65% of all unemployed

## Unemployment rate



# Sharp worsening of social indicators

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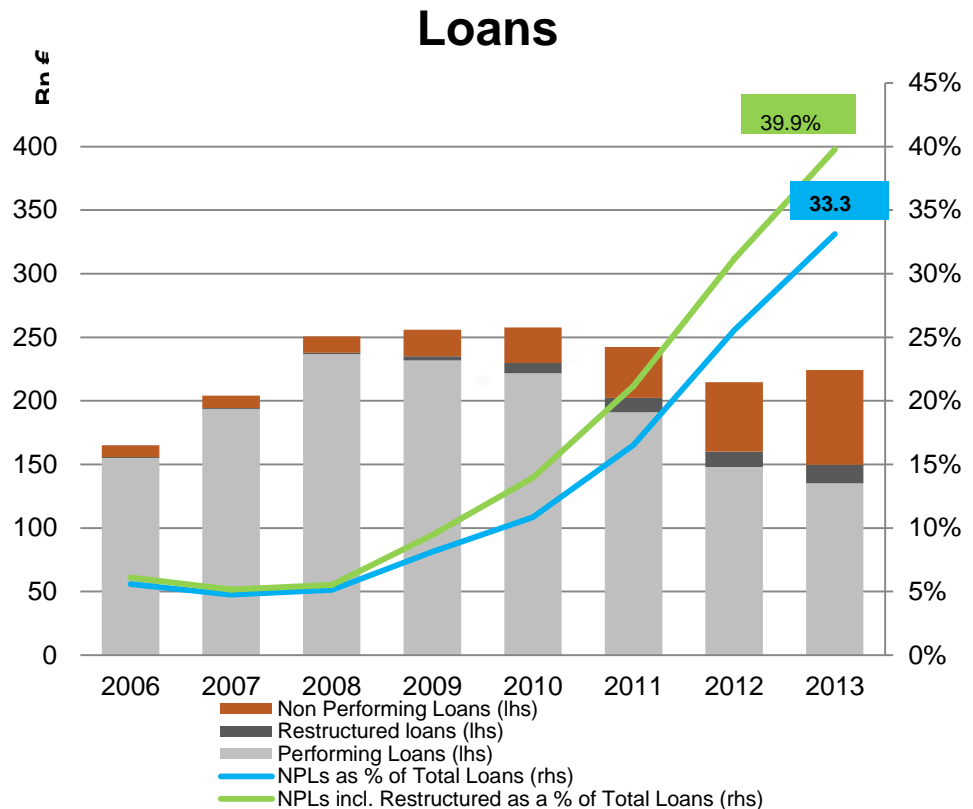
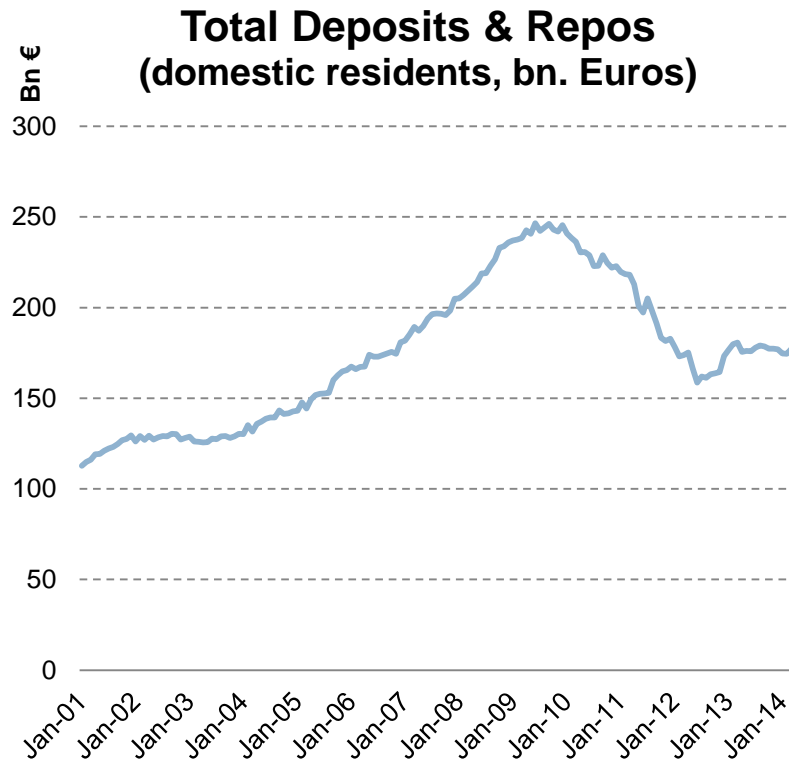
Between 2009 - 2013:

- Average disposable income declined by over 35%  
(due to sharp decline in economic activity and part reliance on tax increase in fiscal consolidation)
- Share of population at risk of poverty or social exclusion rose from 28% to 34%
- Gini index of inequality rose by 10% (despite relatively well-targeted measures)

# Deposits were depleted and Non-Performing loans increased

\*

- ✓The deposit base has been eroded with a peak-to-trough decline of almost EUR 84 billion
- ✓One out of three loans is non-performing



- Getting into the debt crisis
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# Growth prospects 1/2

\*

✓The whole effort aims to shift resources from consumption to investment and increase substantially the share of exports in GDP

Independent studies commissioned by the government suggest excellent growth prospects

- |   |   |
|---|---|
| <ul style="list-style-type: none"><li>• Tourism</li><li>• Primary sector and agro-food industry</li><li>• Logistics and interoperability</li><li>• Energy</li><li>• Shipping-related activities</li></ul> | <ul style="list-style-type: none"><li>• Pharmaceuticals</li><li>• Research, technology and innovation</li><li>• Metal and construction materials industries</li><li>• Tradable services</li></ul> |
|---|---|

*Not all sub-sectors exhibit the same comparative advantage  
Sub-sectors outside the below periphery might exhibit comparative advantage*

Well educated human capital is the real comparative advantage

# Growth prospects 2/2

\*

✓To shift the resources of the Greek economy to higher value added production, these studies\* suggest further reforms

## Horizontal reforms

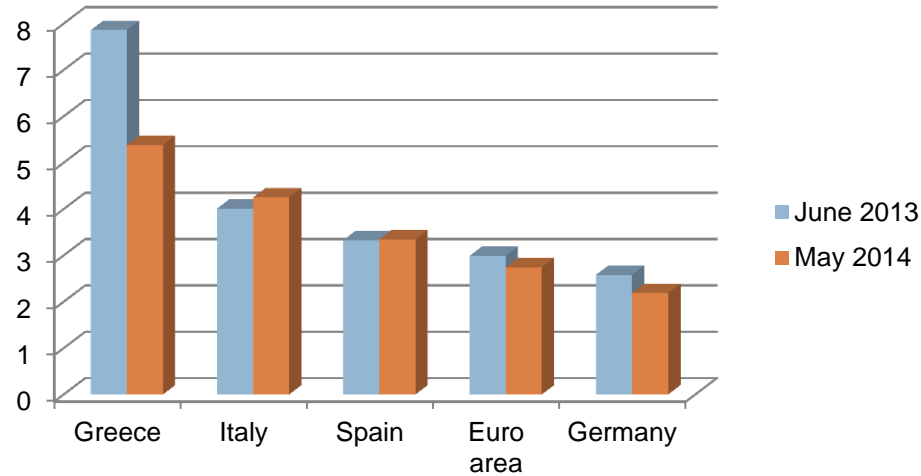
- Creation of favourable investment climate and facilitation of business activities
- Elimination of barriers to entry- reinforcement of competition and competitiveness
- Valorization of public property-privatizations
- Facilitation of international trade-extroversion
- Improvement of tax policy
- Increase labour market flexibility and security
- Emphasis on innovation
- Reorganization of public administration and improvement of the services to the citizens
- Investment in human capital
- Fight against corruption and enhancement of reliability and transparency
- Acceleration and improvement in the justice system
- Reinforcement of social cohesion

# Challenges

## Short term: Liquidity constraints

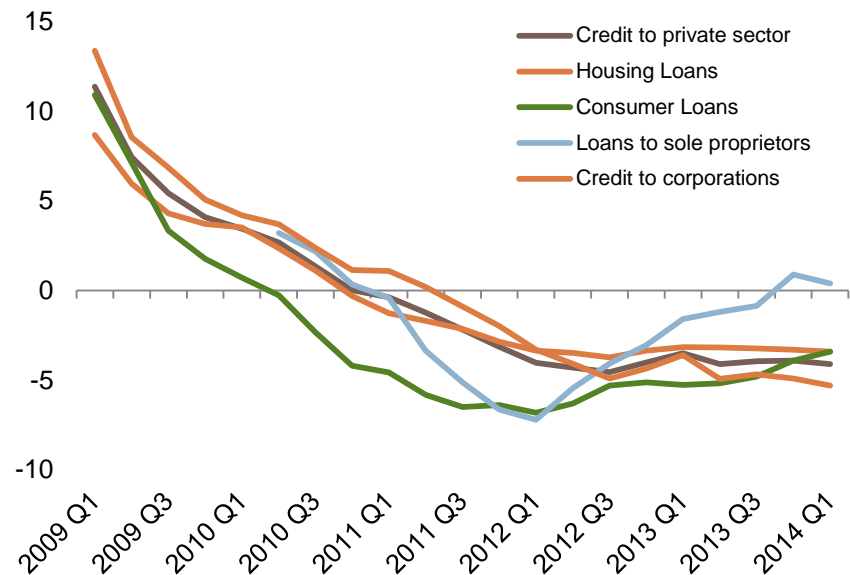
### Interest rates on loans to non-financial corporations

(May 2014 / June 2013; (new business, 1 to 5 yrs, over 1 mn)



Source: ECB

### Credit growth



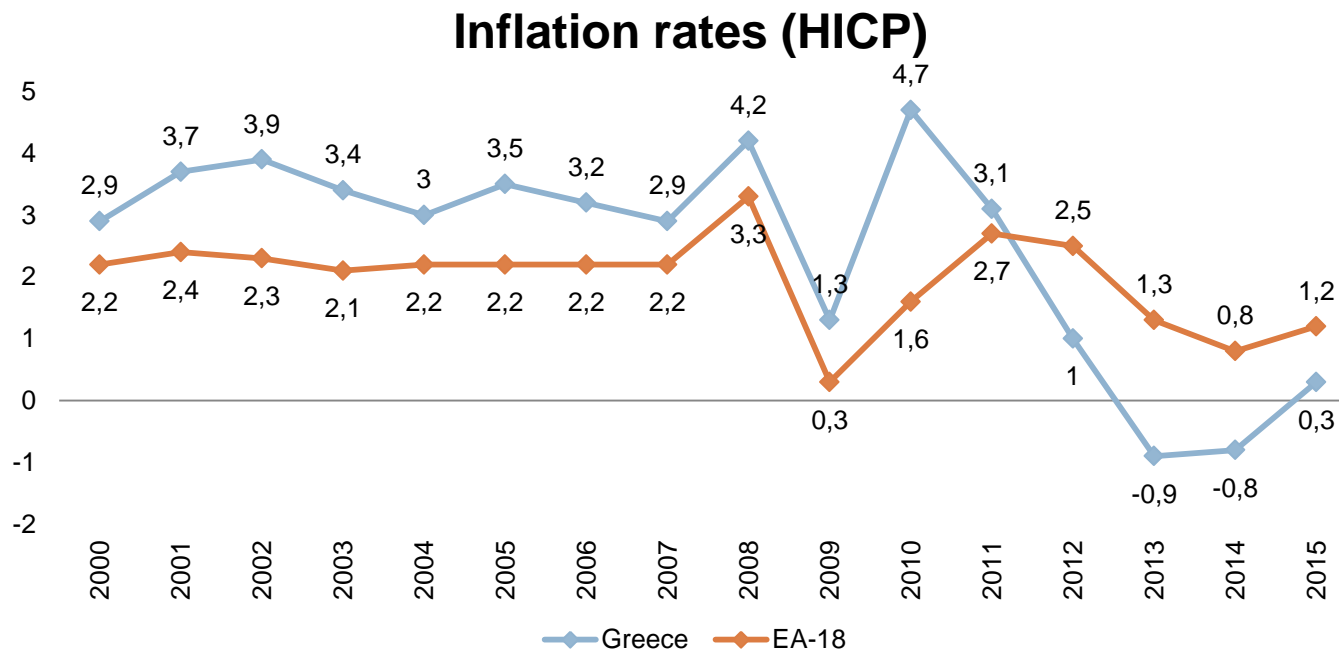
Source: Bank of Greece

- ✓ Sharp decline in sovereign risk
- ✓ Decline in savings reversed
- ✓ Large Greek firms started tapping international markets
- ✓ Increased EIB lending, particularly for SMEs
- ✓ Banks were fully recapitalized, restructured or resolved; have already re-accessed capital markets
- ✓ Creation of specialized Development Fund (IfG) in cooperation with EIB, KfW and private sector institutions, targeting SMEs and infrastructure projects

# Challenges

## Medium term: Deflation

- ✓ Improvement in competitiveness
- ✓ Increases purchasing power of consumers
- ✓ But, ceteris paribus, deteriorates Debt/GDP ratio



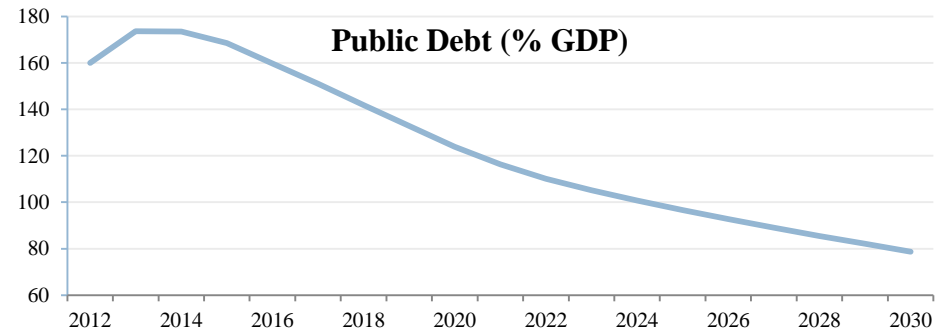


# Challenges

## Long term: Debt sustainability & brain drain

### Debt sustainability

- ✓ Manageable in the medium term
- ✓ Long average maturity (17 yrs)
- ✓ Low average interest rate (2%)
- ✓ Only 29 bn held by the private sector
- ✓ Approx. 80% of the public debt with the official sector
- ✓ Low debt servicing costs for the next 8 years (approx. €6 billion per annum or 3% of GDP vs 4.6% on average for Euro Area periphery peers)
- ✓ EU commitment to help Greece reduce debt to substantially below 110% of GDP in 2022 if needed



Source: European Commission

### Brain drain

- ✓ Several structural fund supported programs targeted to young scientists with high qualifications
- ✓ Establishment of R&D centres by a number of multinational firms in Greece

# Concluding

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- Greece made an enormous adjustment in restoring internal and external balances in a short period of time
- The economy is in a far healthier state than it has been for a long time
- The whole effort aims to shift resources from consumption to investment and increase substantially the share of exports in GDP
- Bold structural reforms have already been implemented and further reforms are planned for the near future

**Greece is changing!**