



Greece and the euro area going forward

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4 March 2017

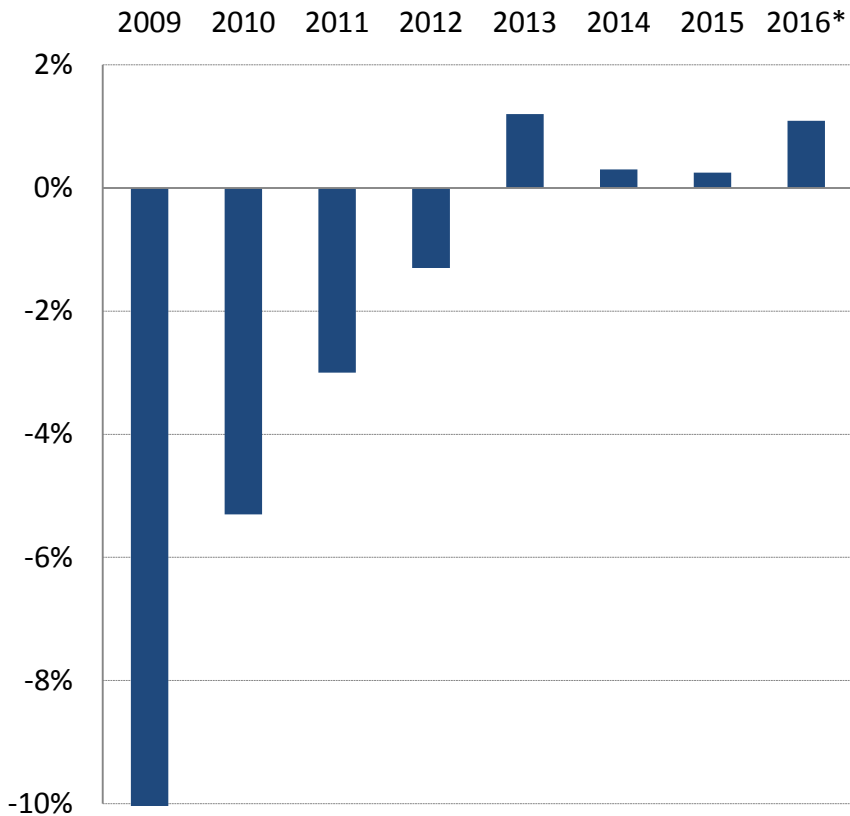
Greece: Current Juncture

The Greek economy is at a turning point

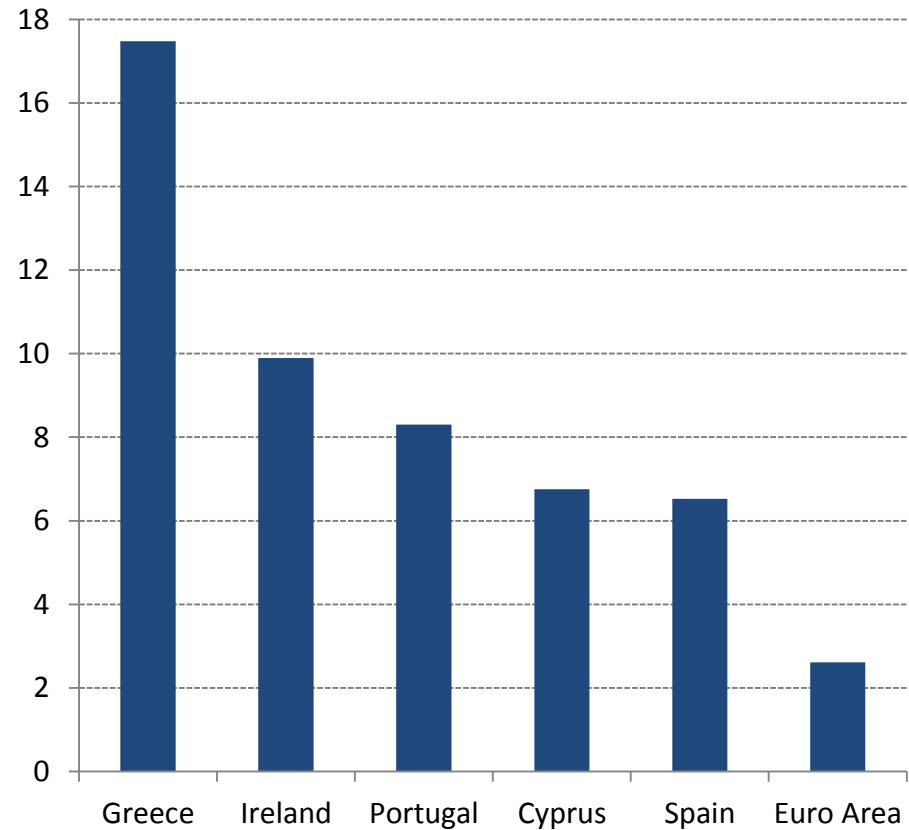
- Growth turned positive in 2016 Q2 and, contrary to initial forecasts, it turned out positive for the year as a whole (0.3%)
- Recent softening of economic indicators relates to delays in the closing of the second review.
- Closure would reduce uncertainty and allow the economy to move quickly to a faster growth path.

Significant fiscal consolidation

General Government Primary Balance (% of GDP, programme definition)



Change in cyclically-adjusted primary balance 2009-2016 (% of potential GDP)

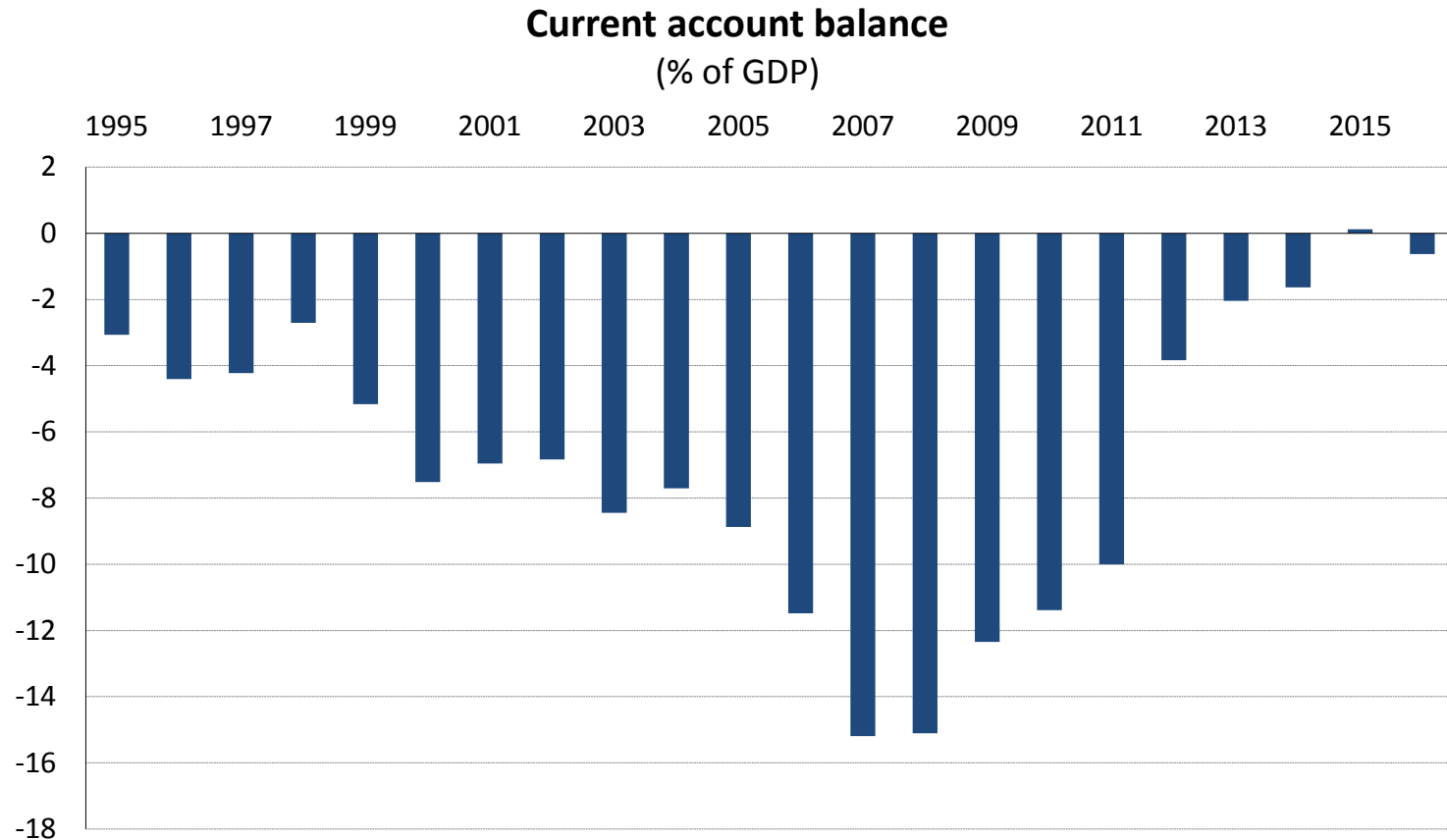


* as published in 2017 Budget Report.

Source: Ministry of Finance

Source: European Commission, European Economic Forecast Winter 2017

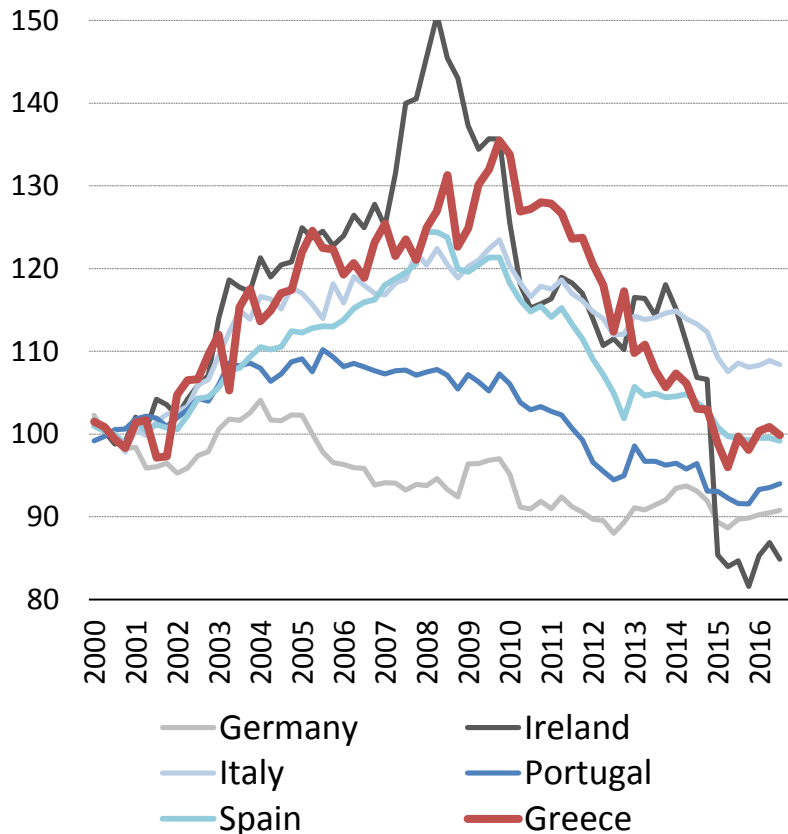
Significant current account adjustment



Source: AMECO

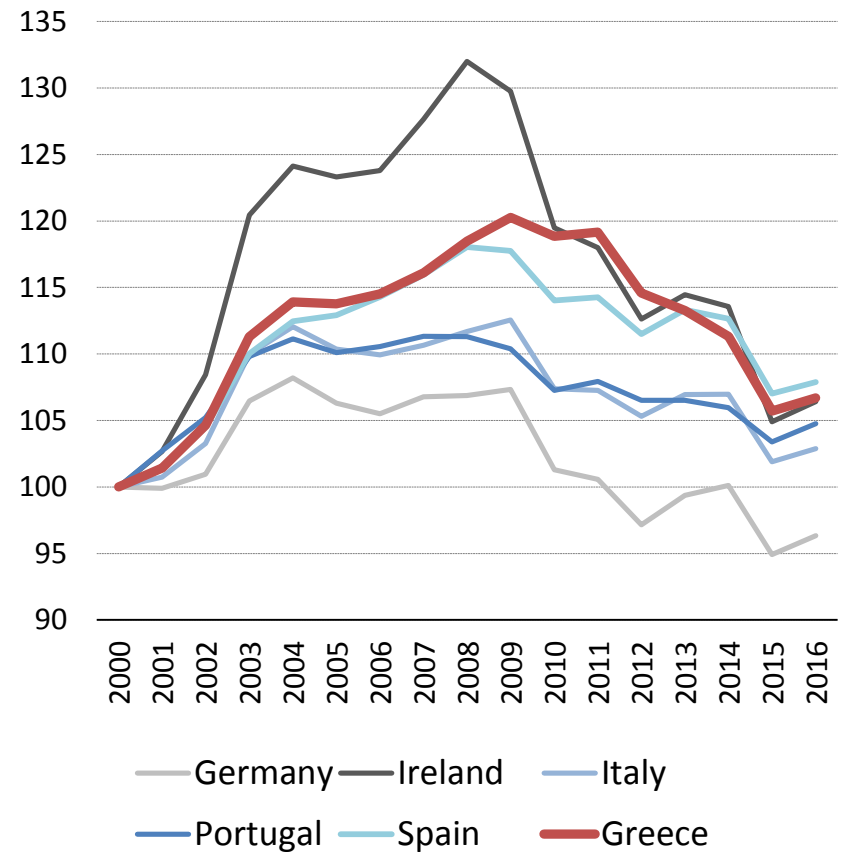
Restoration of competitiveness

**Relative Unit Labour Costs
(Inverse of competitiveness)**
(index: 2000=100; against euro-area countries plus 21 trading partners)



Source: ECB (Harmonized Competitiveness Indicators)

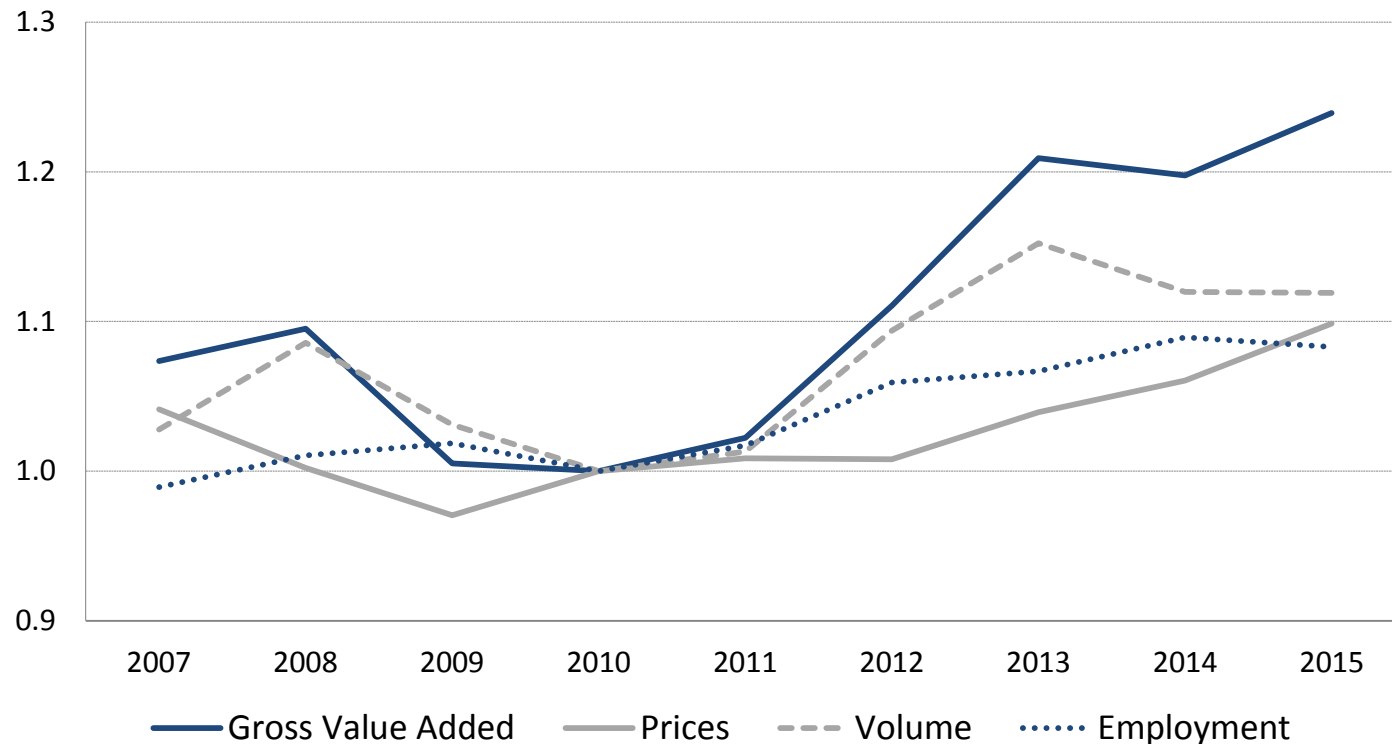
**Relative prices
(Inverse of competitiveness)**
(index: 2000=100; against euro-area countries plus 21 trading partners)



Source: ECB (Harmonized Competitiveness Indicators)

Rebalancing the economy

Relative size of tradeable to non-tradeable sector
(index: 2010=1)

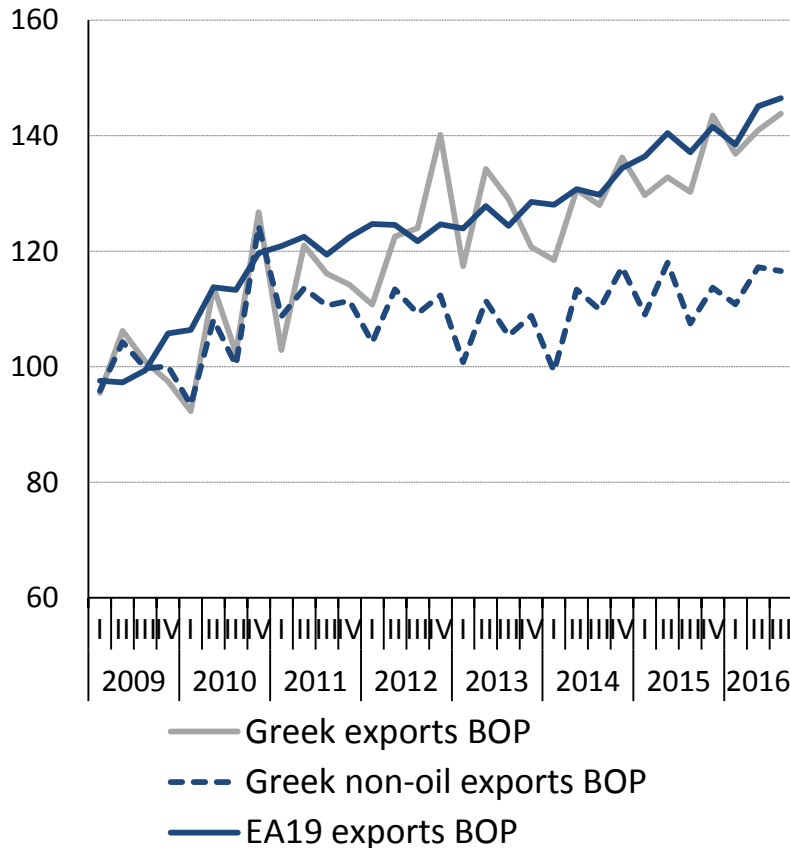


Note: Relative prices are based on (implicit) price deflators of value-added. Tradeables: agriculture, industry, business and financial services, telecommunications and services related to tourism (transport and accommodation and restaurants). Non-tradeables: else except public administration and non-market services.

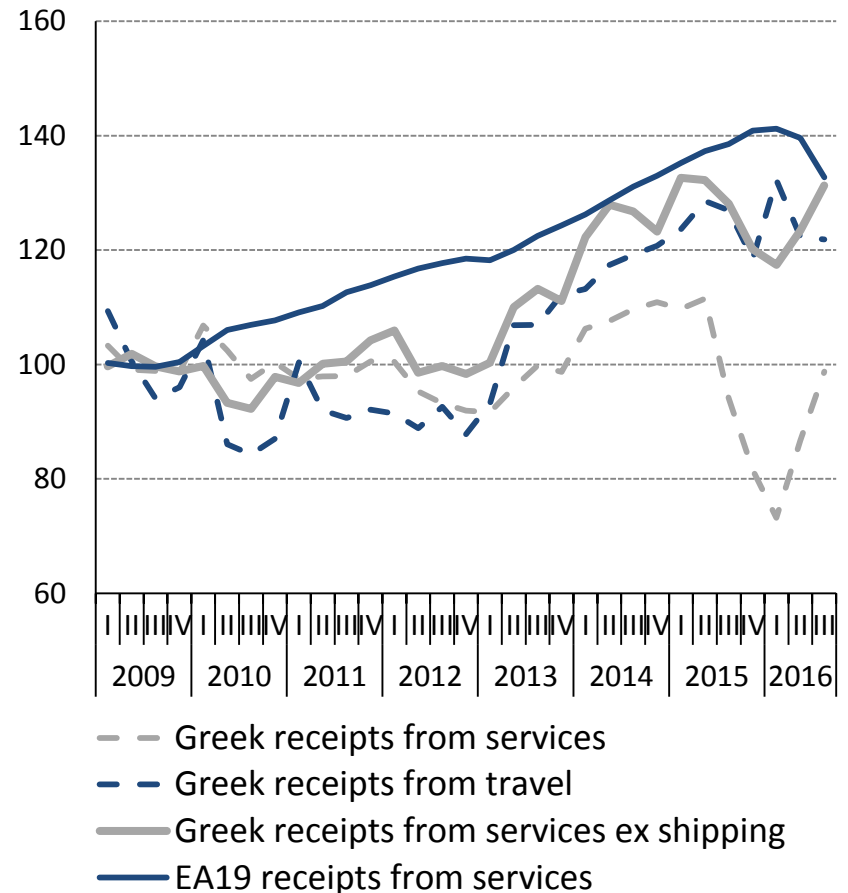
Sources: Eurostat (National Accounts ESA 2010) and BoG calculations

Greater openness: exports of goods and services

Real exports of goods
(index 2009=100)



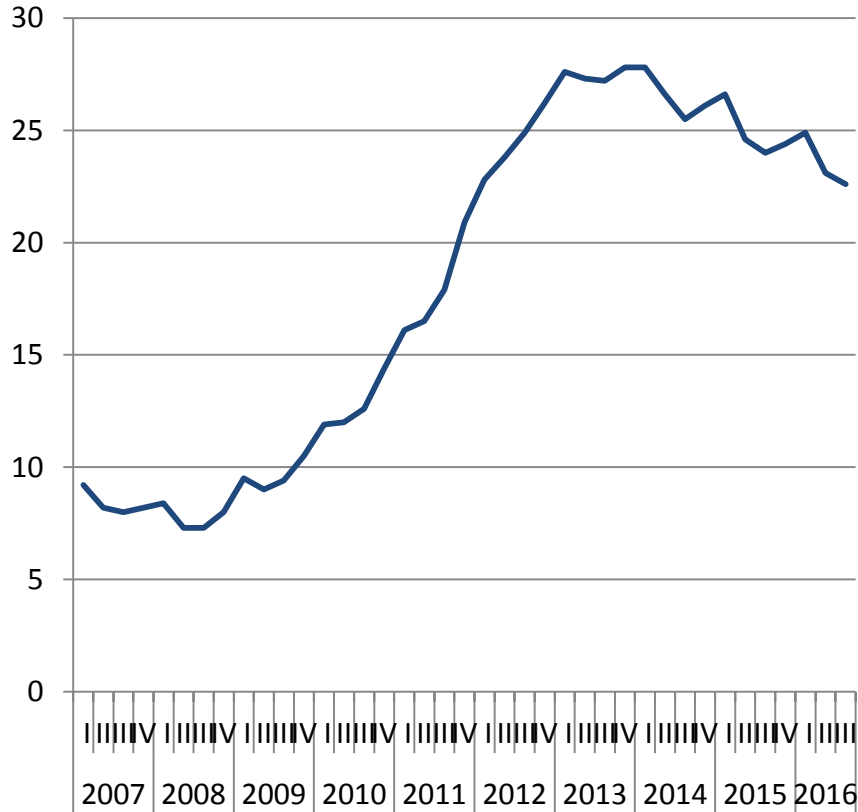
Real exports of services
(index 2009=100)



Source: Bank of Greece (BoP statistics) and Eurostat (for EA 19)

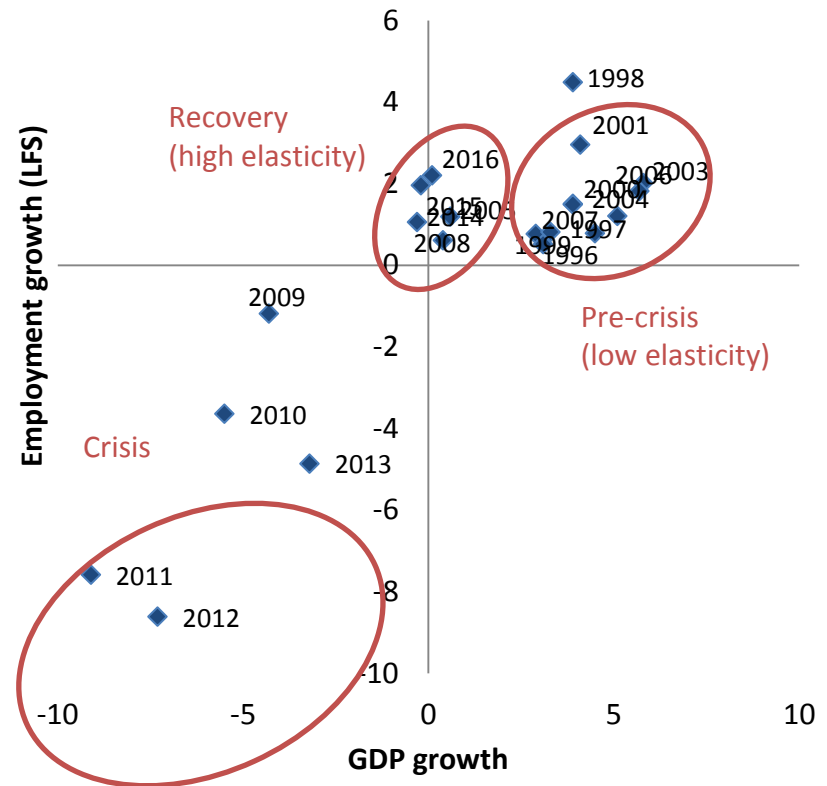
Stock disequilibria remain: unemployment

Unemployment (%)



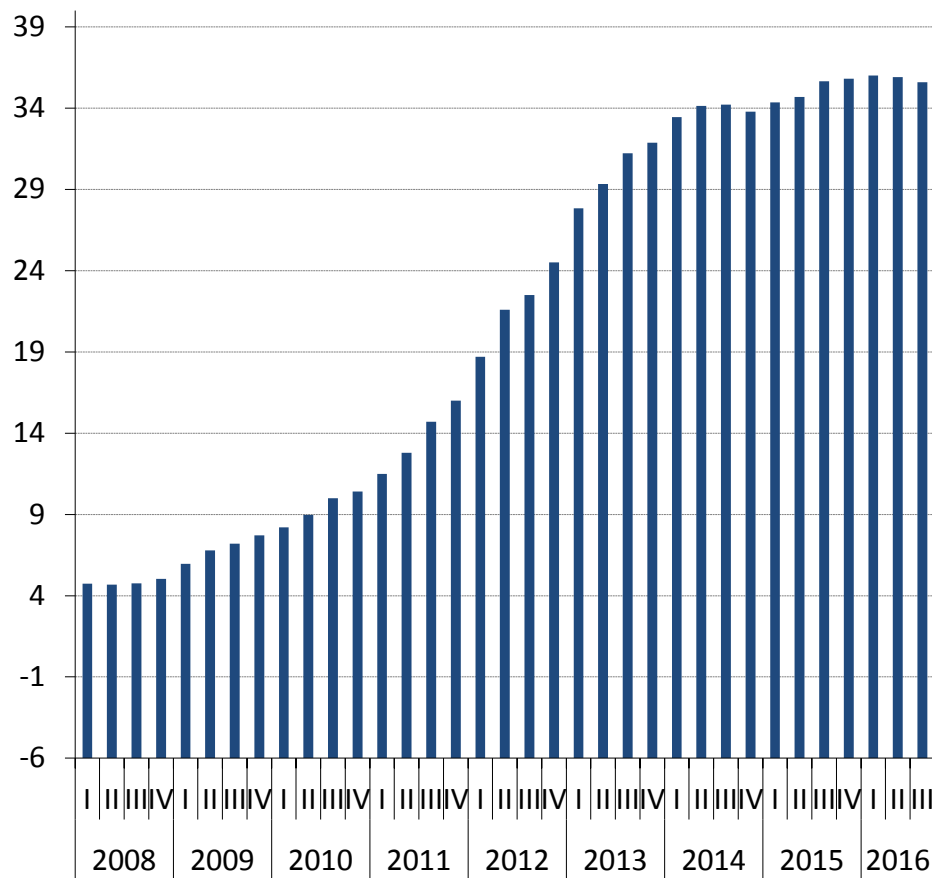
Source: Labour Force Survey

Output vs. employment growth (annual % change)



Non-performing loans

Greek commercial banks – NPL ratio (%)



Source: Bank of Greece

Measures taken

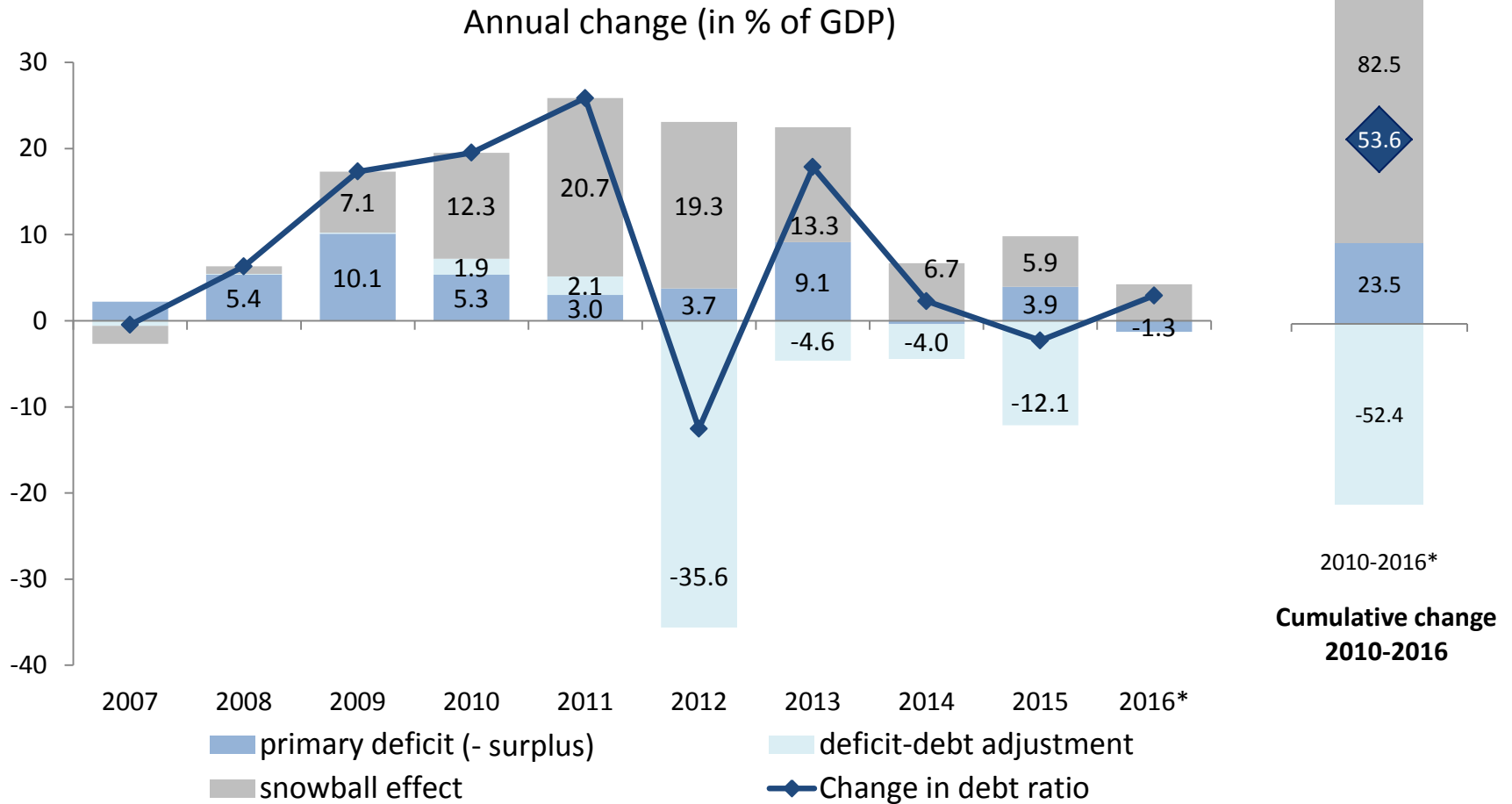
- BoG guidelines for enhanced governance framework
- Set of ambitious operational targets agreed by banks and BoG/ECB, NPEs' reduction by 40% by 2019
- New households' insolvency law
- Amended Code of Civil Procedure
- Enhanced capacity and efficiency of judicial system
- Setup of a secondary market for NPLs.

Ongoing initiatives

- Revision of out-of-court workout
- Revision of bankruptcy law
- Legal protection
- Creation of a Credit Score Bureau and debt info/counseling centres
- E-auctions

General government debt

Snowball effect (i – g): the main driver



* 2017 Budget Report

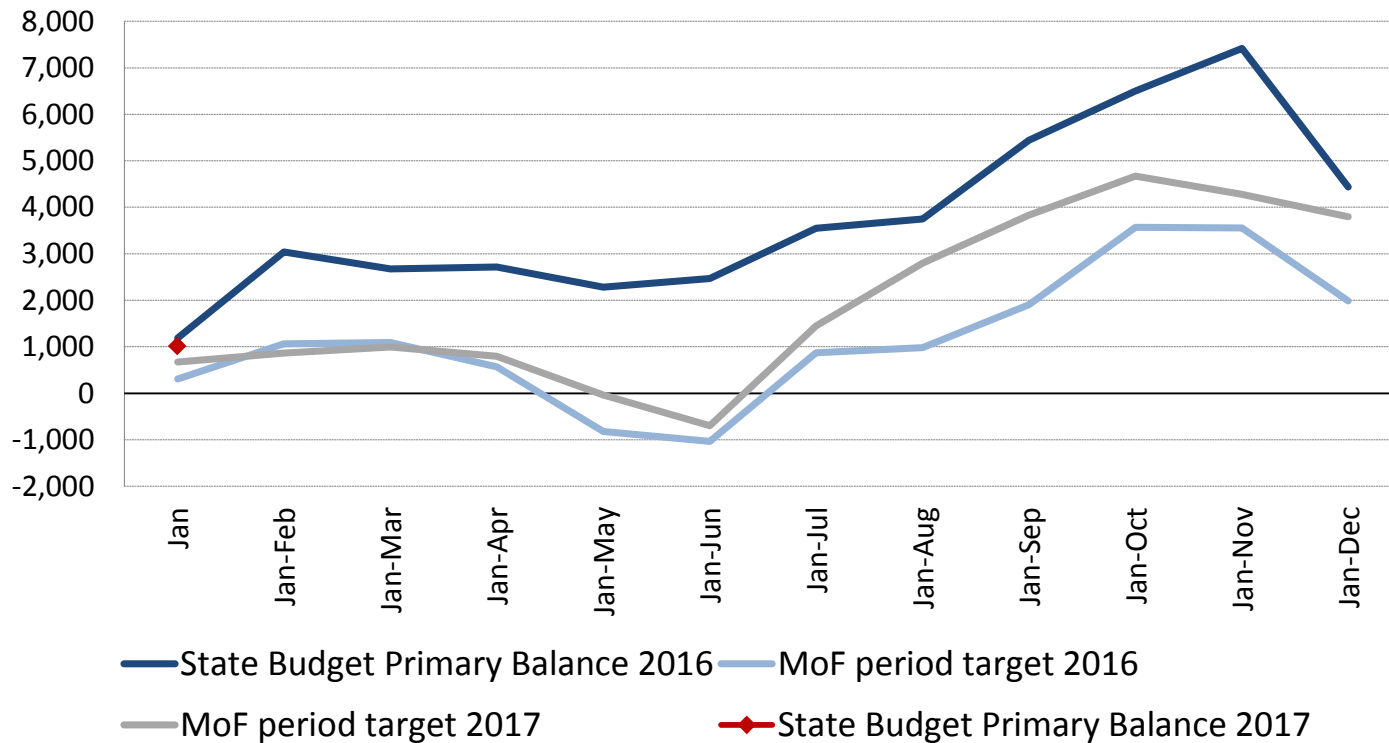
Source: ELSTAT and Ministry of Finance

Short-term economic outlook

- Strong positive growth rates are expected over the short and medium term for as long as the output gap closes.
- Consumption continues to rebound, driven by the increase of employment.
- Investment and exports increase as confidence is restored and credit conditions improve.

State budget execution

State budget primary balance against MoF's period targets in 2016-2017 (€ million)



Source: Ministry of Finance.

EC winter forecasts

	2017	2018
GDP	2.7	3.1
Private consumption	1.6	1.6
Public consumption	0.2	0.0
Gross fixed capital formation	12.0	14.2
of which: equipment	13.4	15.2
Exports (goods and services)	3.9	4.7
Imports (goods and services)	3.2	4.2
Primary balance (% of GDP)*	2.0	3.5

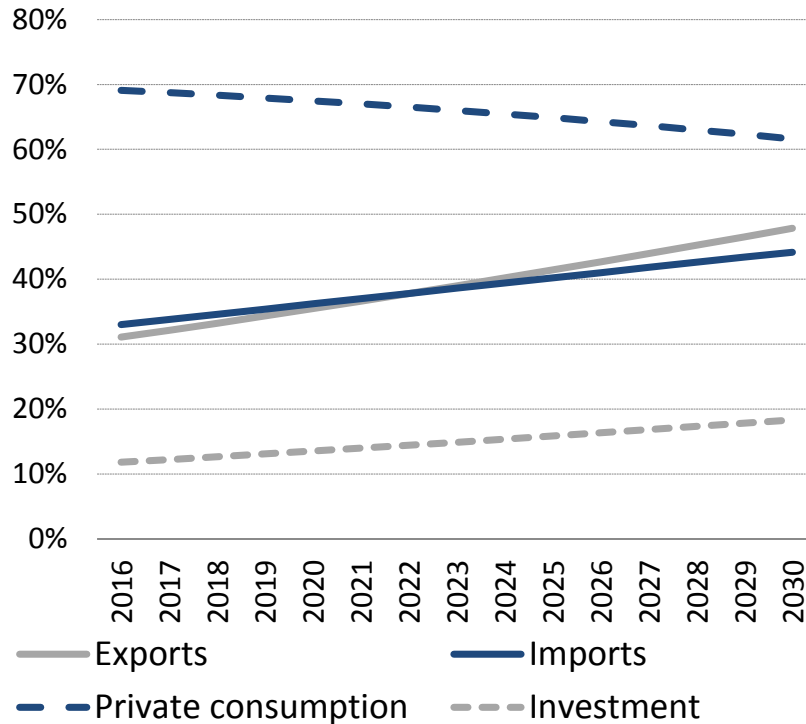
* Programme definition, excludes transfers to the state of profits from ANFA and SMP portfolios held by the Bank of Greece. Bank of Greece calculation.

Long-term economic outlook

Growth rate assumptions

Private consumption	1%
Investment	5%
Exports	5%
Imports	4%

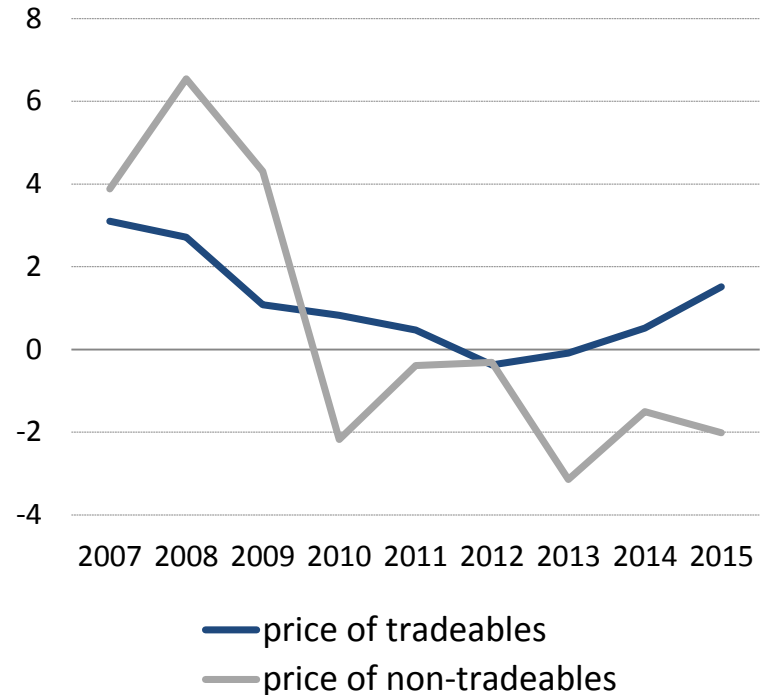
Rebalancing of the economy (Baseline Scenario, % of GDP)



Sources: Eurostat and BoG calculations.

Rebalancing the economy from the demand side: Investment and exports will fill the gap of effective demand from lower public and private consumption, reaping the returns of improved competitiveness.

Value-added deflators (annual % change)



Sources: Eurostat and BoG calculations

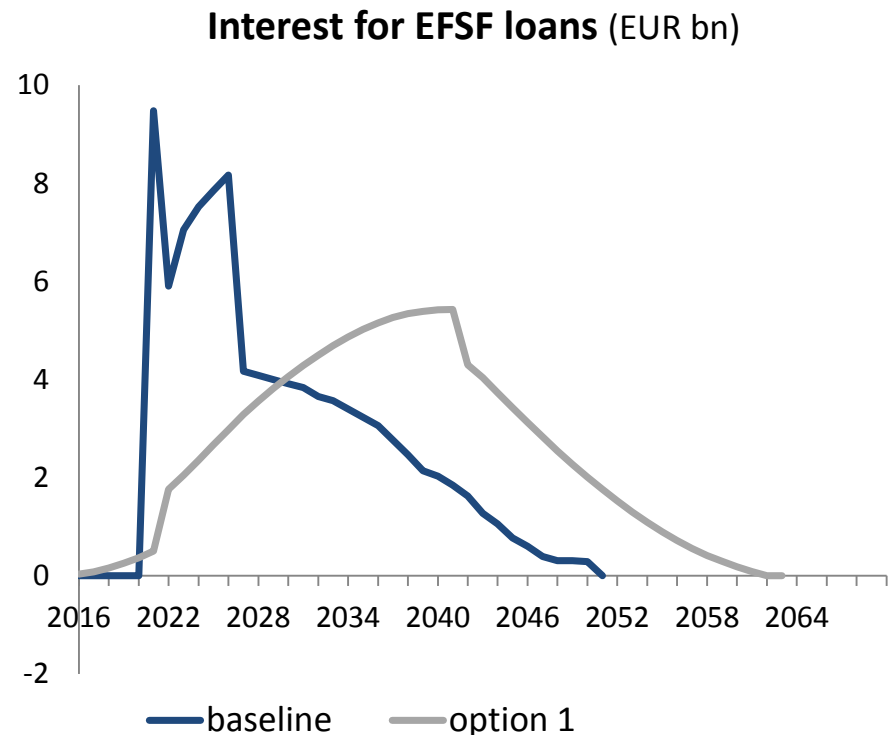
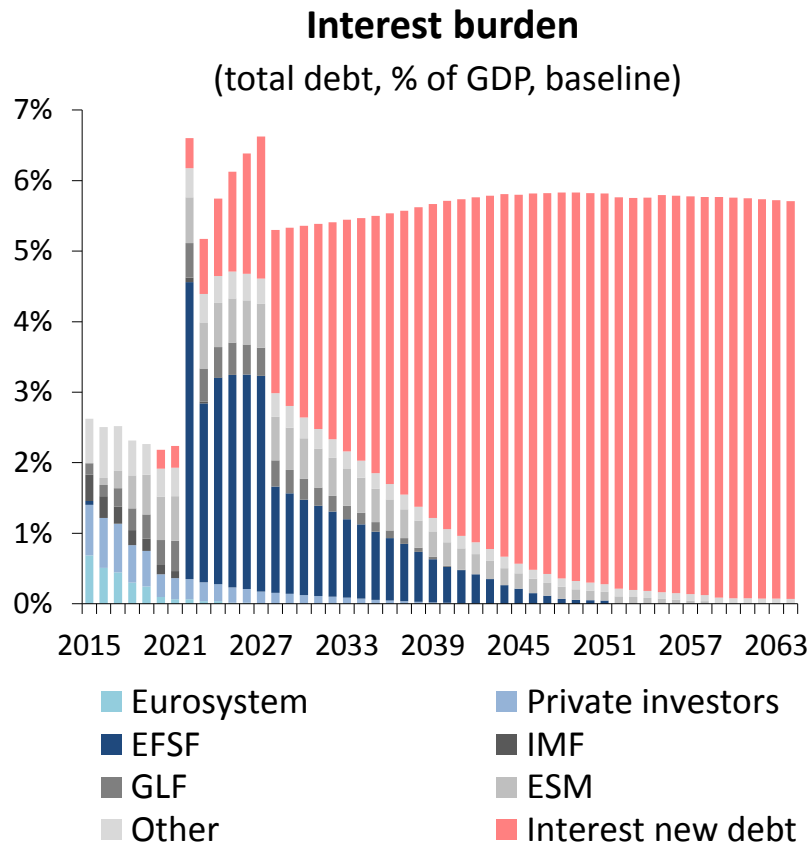
Rebalancing the economy from the supply side: The shift in relative price inflation since 2010 makes production of tradeables more profitable.

BoG Proposals: fiscal policy and government debt

- Fiscal mix: taxes versus spending.
- Fiscal target: reduction from 3.5% to 2% of GDP after 2021 consistent with debt sustainability if combined with structural reforms and mild debt relief measures.
- Debt relief measures:
 - Short-term measures – Eurogroup, 5 December 2016.
 - Medium-term measures: extending maturities and/or smoothing the interest burden.

Mild debt relief exercise

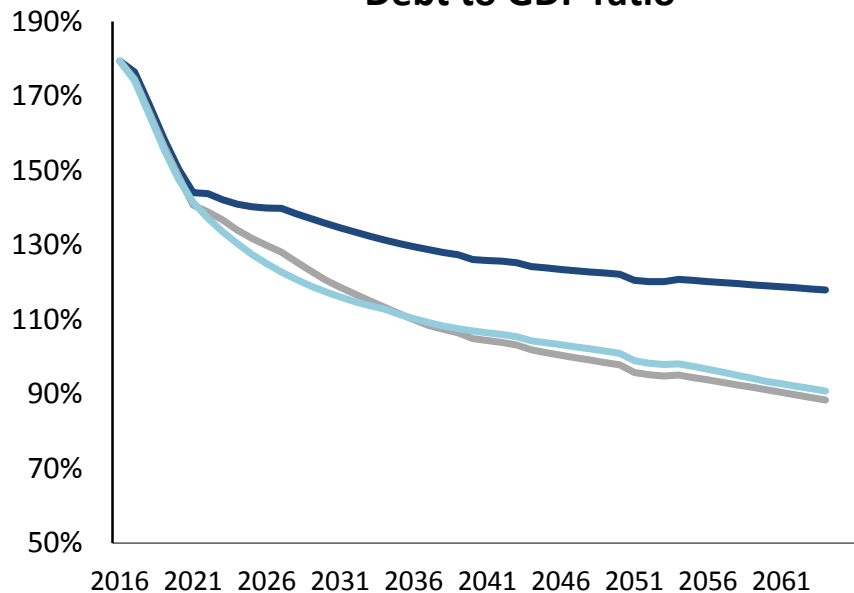
- Option 1 defers interest for EFSF loans using the rule: interest due in year t is deferred to next 20 years in equal installments and capitalized. Weighted average maturity of EFSF interest payments increases by 8.5 years. Includes ANFA and SMP.



Mild debt relief exercise

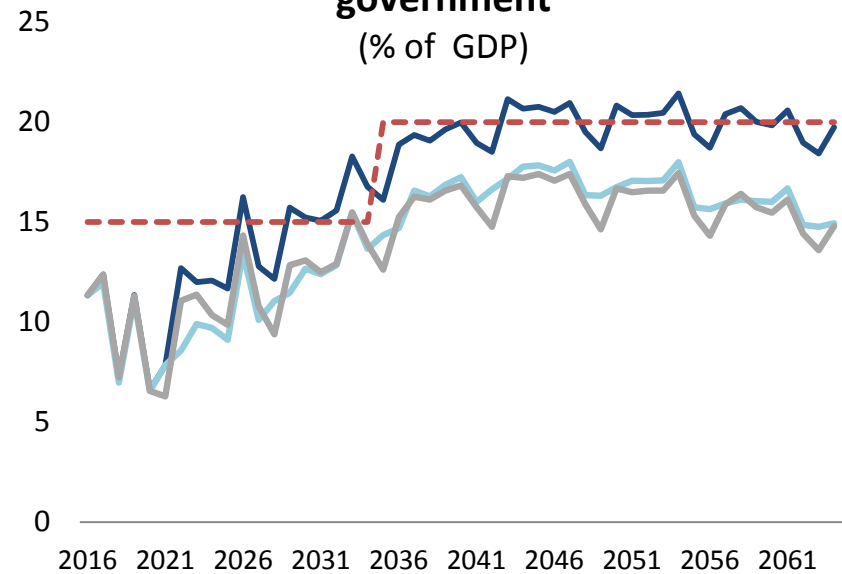
- **Baseline high surplus:** Primary surplus of 3.5% until 2027, gradual decline to 2% by 2037
- **Baseline low surplus:** Primary surplus of 3.5% in 2018-2020, 2% afterwards
- **Option 1:** Baseline low surplus + increase in WAM of interest payments for EFSF loans by 8.5 years (smoothing of EUR 101 bn of projected interest payments to EFSF until 2060) + ANFA + SMP
- **GDP growth:** 1.5% after 2022
- **Inflation:** 2% after 2019
- **Interest rates:** GGBs: 5%, ESM: gradual increase to 3.0% until 2021, 3.5% after 2027

Debt to GDP ratio



— Baseline low surplus — Baseline high surplus
— option 1

Gross Financing Needs of general government (% of GDP)



— baseline low surplus — option 1
— baseline high surplus - - - Threshold

The euro area: addressing the sovereign crisis

- ECB monetary policy response (SMP-2010, OMT-2012, QE-2015)
- Financial Stability Response: Macroprudential policy tools
- GLF → EFSF → ESM
- Banking Union:
 - Single Supervisory Mechanism (SSM)
 - Single Resolution Mechanism (SRM)
 - European Deposit Insurance Scheme (EDIS, incomplete)
- Fiscal and economic surveillance (Six pack – Two pack)
- European Semester, Country Specific Recommendations
- Macroeconomic Imbalances Procedure (MIP)

Euro area recovery

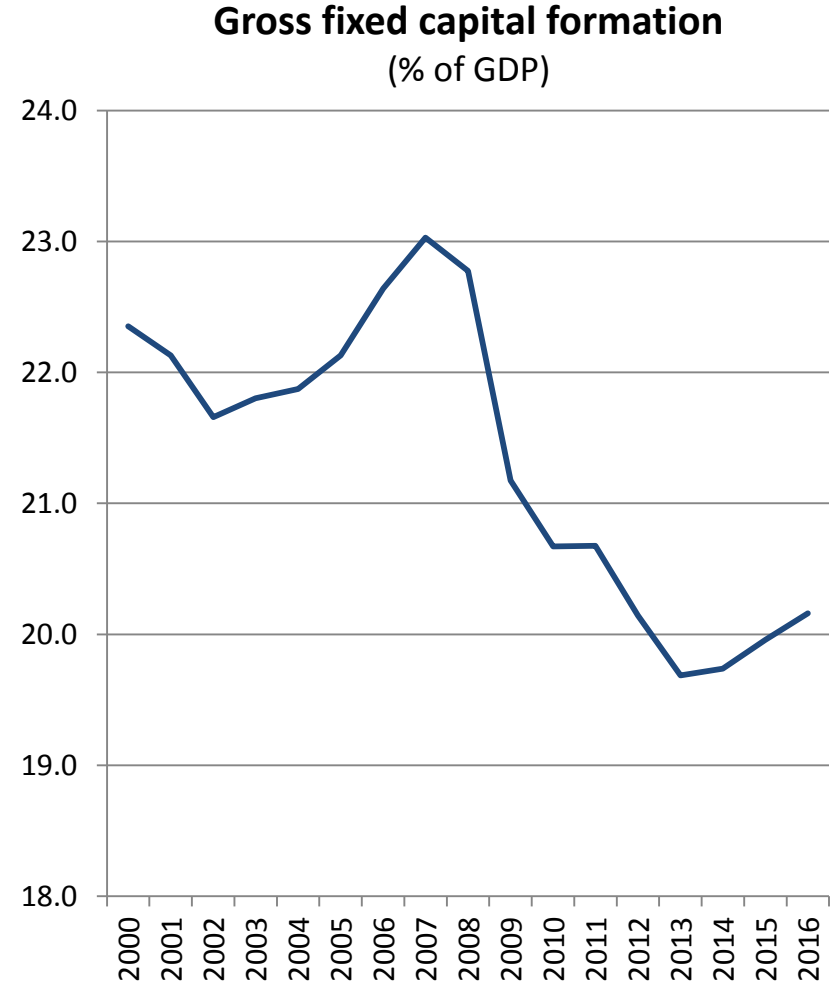
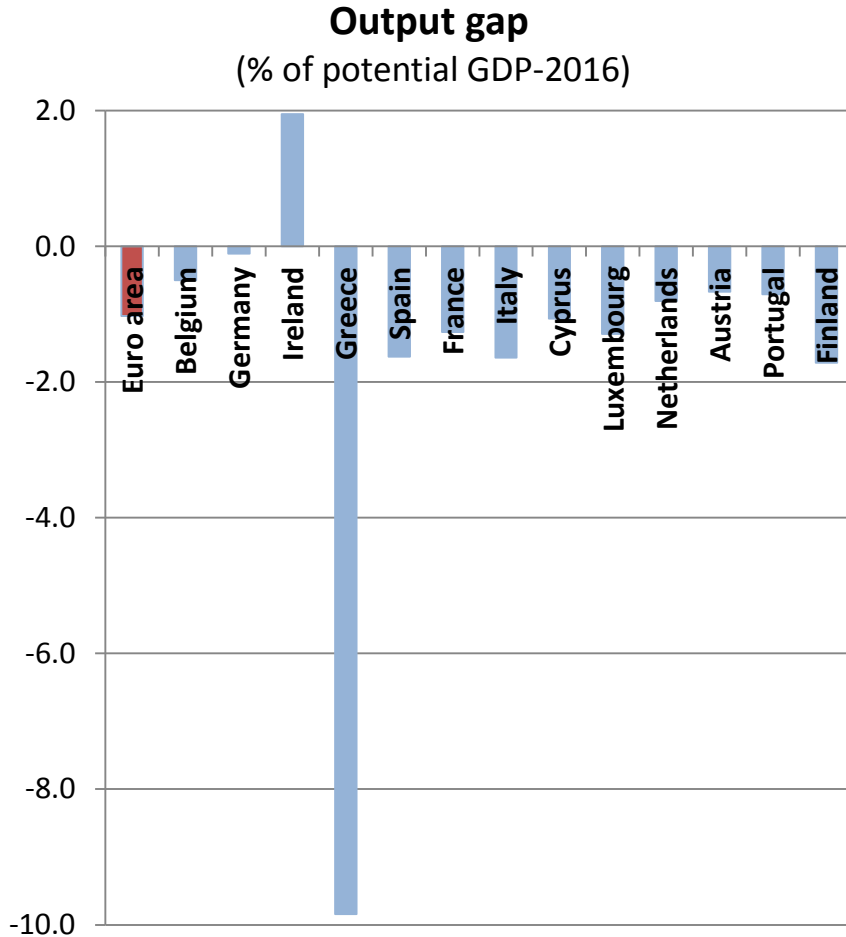
Euro Area Recovery faces headwinds I

A. Political - Social

- Political uncertainty – Incoming general elections
- Populism – Anti EU rhetoric
- Protectionism as a response to globalisation and technical progress:
Not a first best response
- Income distribution: Inability of governments to tax the winners
and subsidise the losers
- Refugee crisis
- Terrorism
- Brexit
- Uncertainty related to US policies vs the financial sector (Repeal of
Frank-Dodd?)

Euro Area Recovery faces headwinds II

B. Economic: Weak Internal Demand

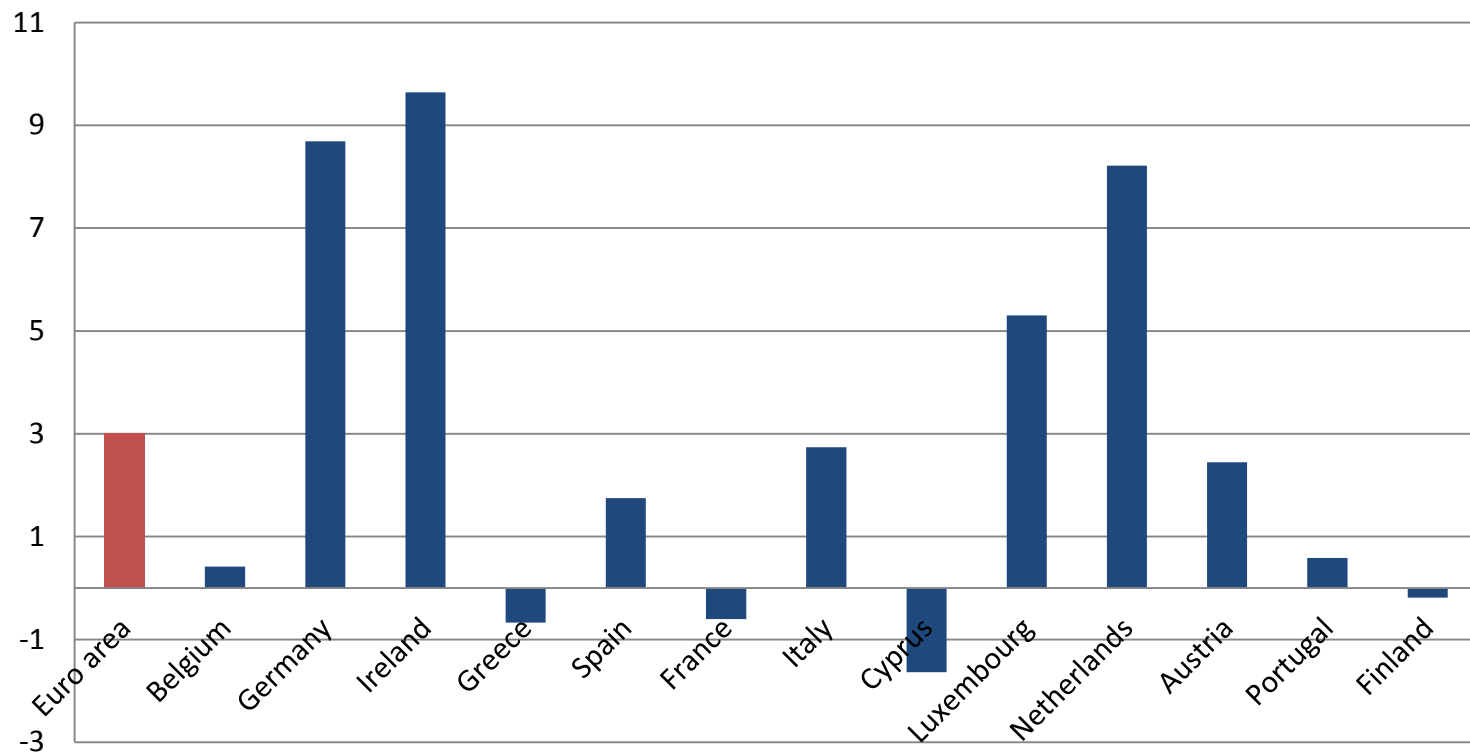


Source: Ameco

Euro Area Recovery faces headwinds III

B. Economic: Weak Internal Demand (continued)

Current account balance
as % of nominal GDP (2016)



Source: Ameco

Improving resilience of the Euro Area I

At the level of Member States we need to strengthen resilience by:

- Introducing wide-ranging structural reforms which remove rigidities in labour, product, services markets
 - Price flexibility
 - Wage flexibility
 - Easier entry and exit of firms
- Consequences
 - Increased capacity to absorb shocks internally
 - Increased productivity and long-term growth
 - Increased uncertainty → introduce flexicurity: market flexibility, social protection

Improving resilience of the Euro Area II

At the level of the euro area we need to reform the institutional setting of EMU:

- Enhanced real and cyclical convergence through closer policy coordination
- More symmetric adjustment: Member States with current account space should also adjust
- Private risk-sharing in EMU: True Financial Union (Banking Union, Capital Markets Union)
- Public risk-sharing in EMU: Common Fiscal Stabilisation Tools
- Reform-for-investment policy
- Common unemployment insurance scheme
- “Rainy Day” fund
- ESM replaced ultimately by a European Monetary Fund