New Growth Agenda and Structural Reforms

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Success?

- Elimination of twin deficits

  Through recession. Sustainable?
- Competitiveness has been restored

  Primarily, if not exclusively, through decrease in unit labor cost.
- Greece is back to growth.

  Very low, slow and anaemic.
- Greece has stayed in the euro-zone.

  But why was this even put on the table?

Future outlook?

- Can the remaining reforms be done?

  Possibly, as governments can no longer generate growth by borrowing.
- What are growth prospects?

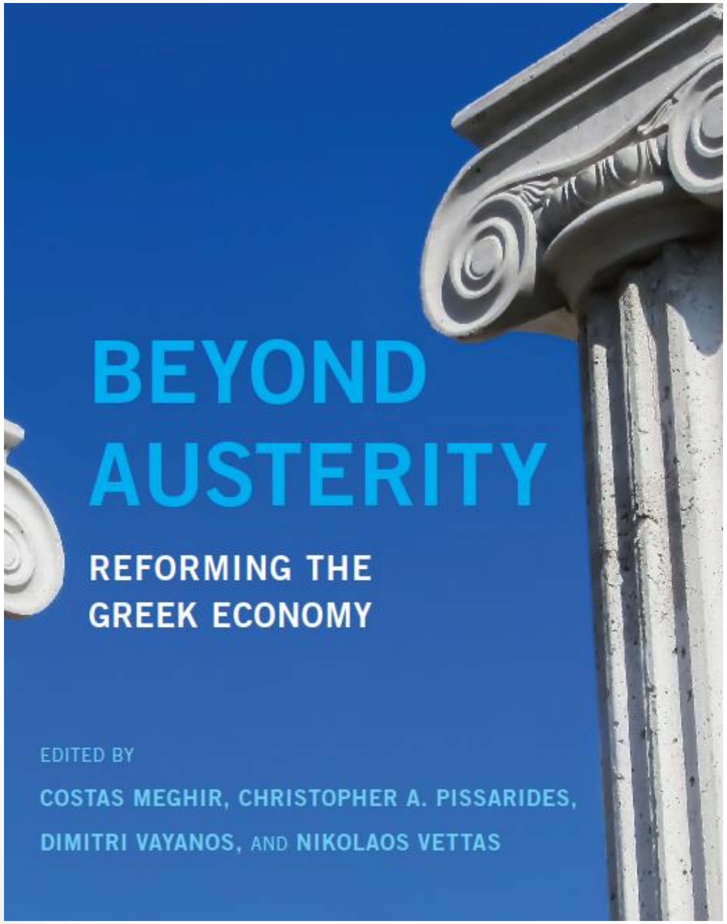
  High, if reforms continue.
- What should be done with the debt?

  Gradual reduction, conditional on reform milestones.
- Does the Euro benefit Greece?

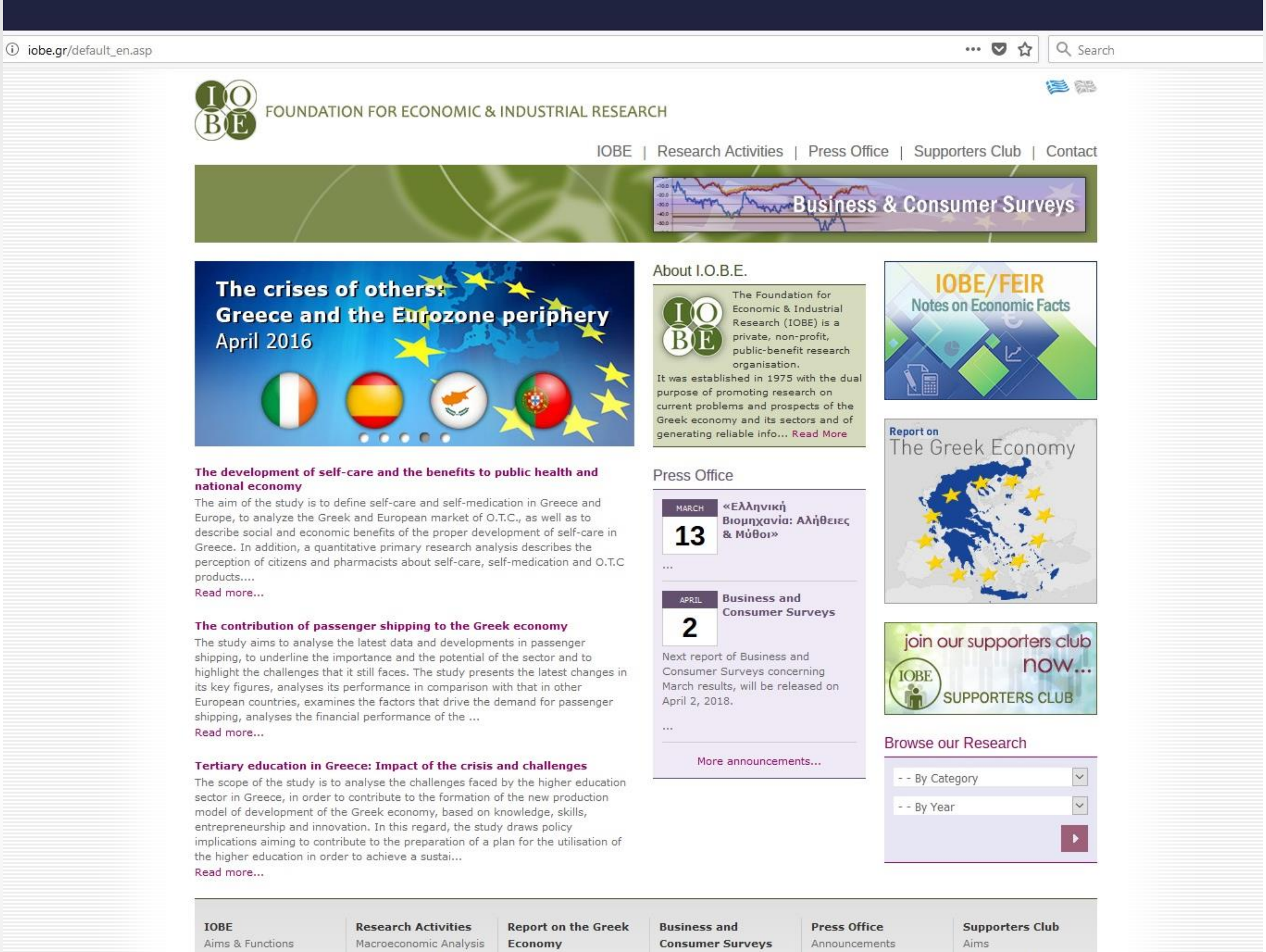
  Yes, discipline to reform (provided EZ architecture is set right).
- The effects of the external environment?

  Debt management, fiscal monitoring, deposit insurance, incentives for structural reform

A book



- "Beyond Austerity: Reforming the Greek Economy", MIT Press.
  - https://mitpress.mit.edu/books/beyond-austerity
- Economic institutions and resulting incentives, across wide range of areas.
  - Pre-crisis situation.
  - Changes during crisis.
  - Policy proposals going forward.
- Collective effort of Greek economists in Greece and diaspora.



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Key background points

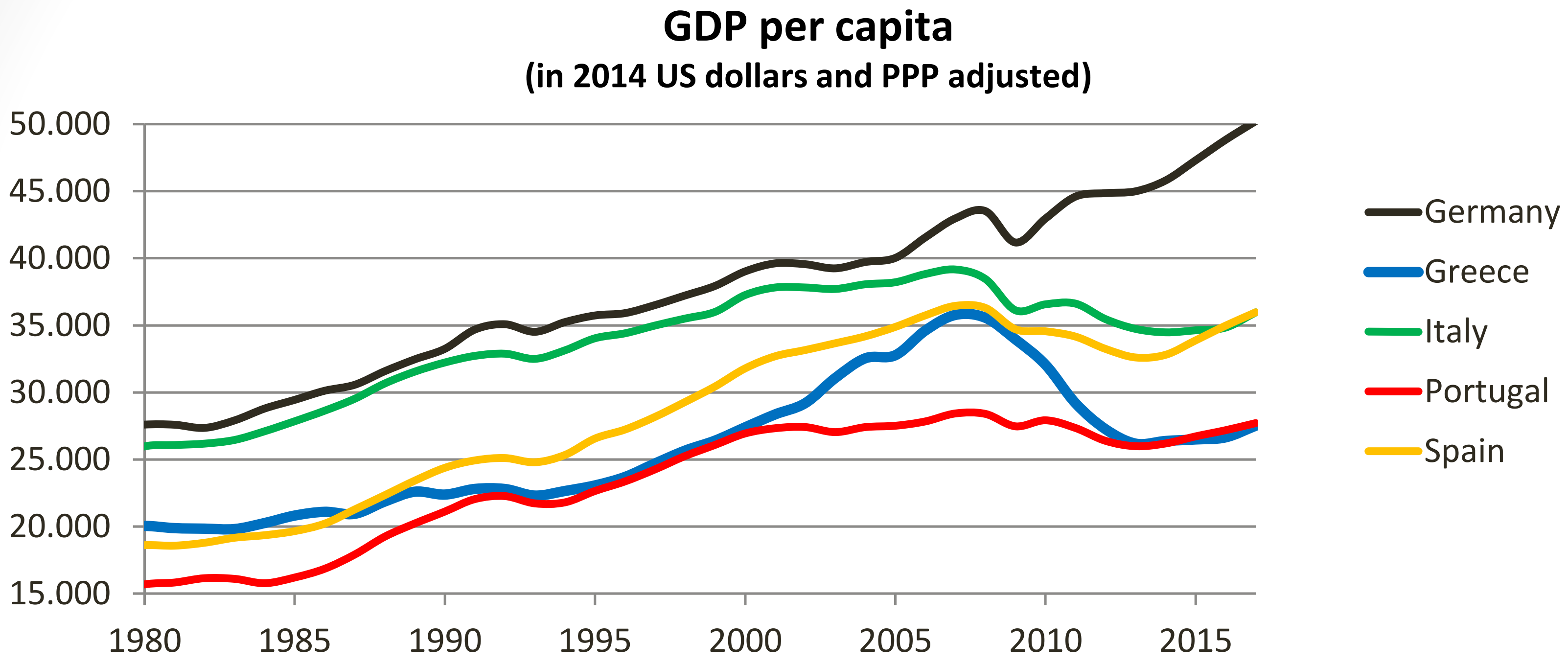
- Crisis partly due to long-term domestic problems:
  - Low long-term growth.
  - Low corporate investment and FDI.

- Crisis exacerbated by flows in EZ architecture that facilitated excessive borrowing and current account deficits.
  - No framework for sovereign default within EZ.
  - Weak bank-regulation framework.

- Euro entry had some positive outcomes for Greece.
  - Increase of productive (corporate) investment.

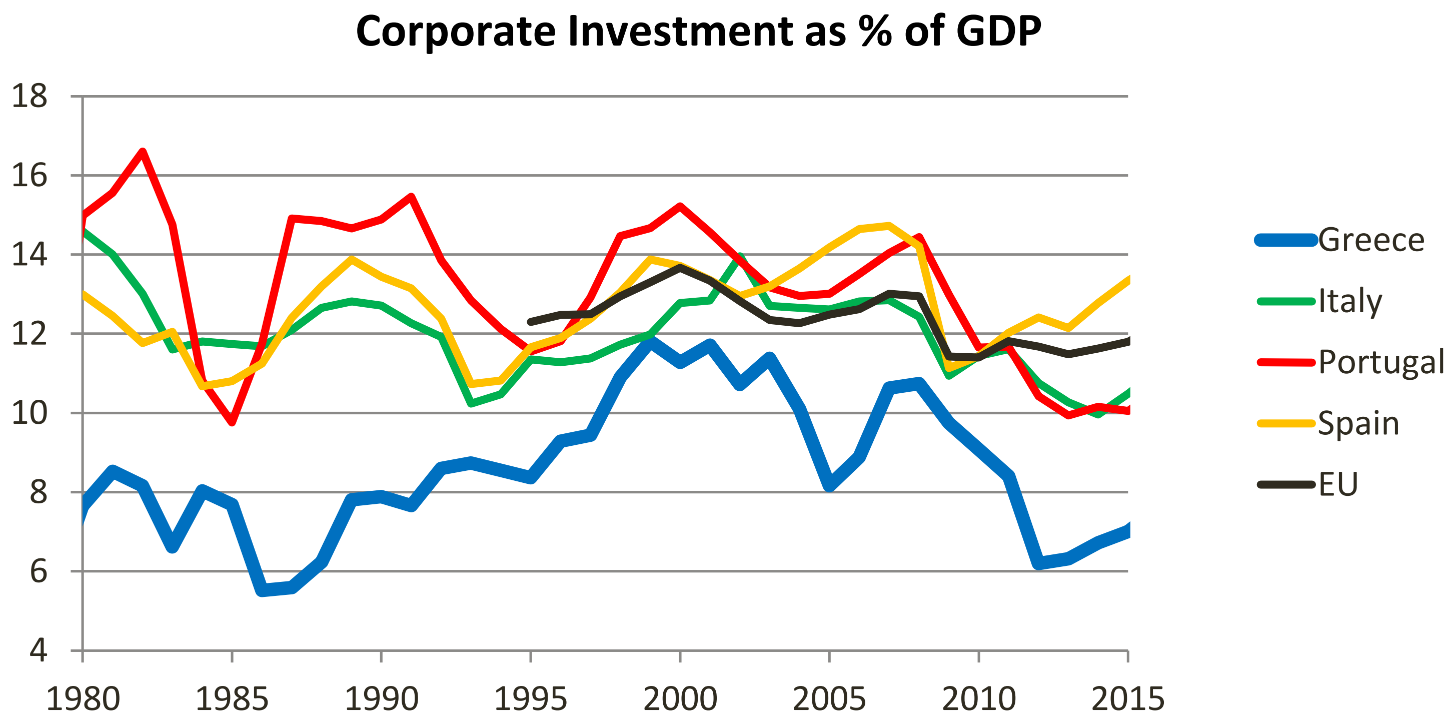
- Greece was "canary in the mine" – weaker and first to fall.
  - High current account deficit (as Portugal and Spain).
  - High government debt (as Italy) and deficit.

GDP



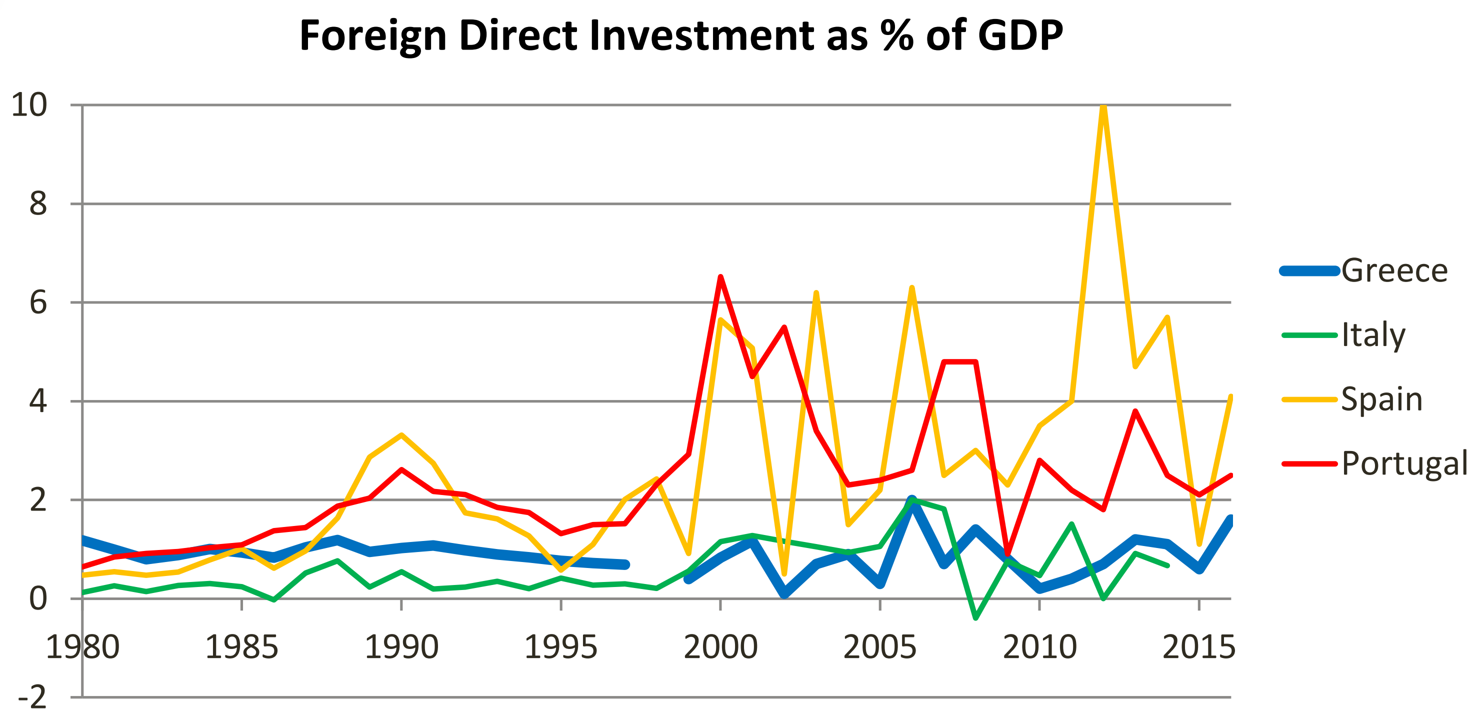
- Greece experienced a large growth and subsequent decline of GDP after Euro entry.
- Its growth over the long term (1980-2017) has been relatively small.
  - Similar to Italy.
  - Similar before and after Euro entry.

Corporate investment



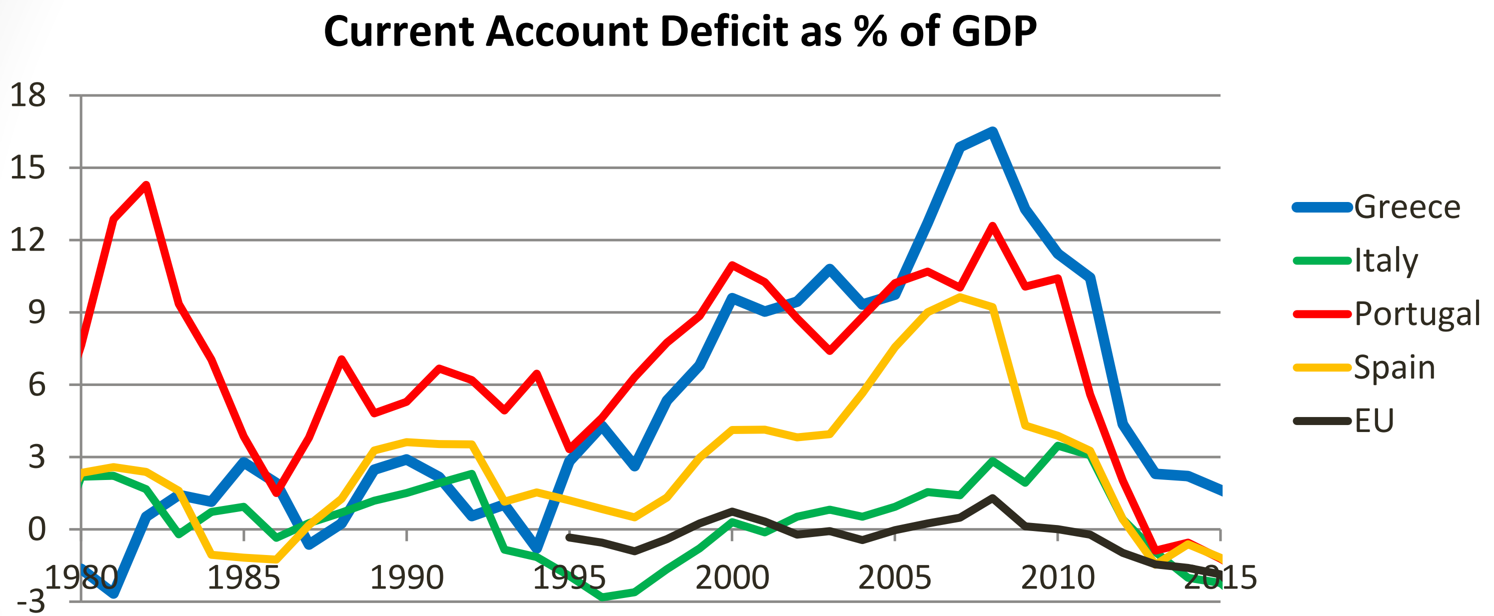
- Corporate investment in Greece has been relatively low.
  - But total investment (incl. housing) is comparable to EU average!
- It rose significantly in the run-up to Euro entry, but dropped again during the crisis.

Foreign Direct Investment



- FDI in Greece has been low.
  - Similar to Italy.
  - Even during the boom years after Euro entry.
- Indicative of broader problems with business environment.

Current Account Deficit



- Current account deficit rose significantly in the run-up to and after Euro entry.
  - Similar to Portugal and Spain.
  - Rise in investment, consumption, and GDP.

Key structural improvements achieved

- Labor market.
  - Significant deregulation of a formerly over-regulated labor market.
- Pensions.
  - Unification of a highly fragmented pension system.
  - Viability through significant pension cuts.
- Product markets.
  - Deregulation, privatisations, and reduction of legislated barriers to entry.
- Tax administration.
  - Establishment of independent tax collection authority.
  - Fully electronic filing.

Labor market

- Over-regulated before the crisis.
  - EPL in 2008 fifth-highest in OECD.
  - High % of long-term unemployed and of self-employed.
  - Low reallocation rate (hirings and firings).

- Key changes in regulation.
  - Severance pay has been halved, to five months of salary.
  - Collective dismissals no longer require ministerial approval.
  - Firm-level agreements have become possible, and effectively replaced collective agreements.

- EPL in Greece is now at OECD average.

Pensions

- Costly, inefficient and fragmented system before the crisis.
  - Pension expenditure in 2007 second-highest in EU (12% of GDP), and projected to double by 2060.
  - Yet, high old-age poverty.
  - Rules mapping contributions to pensions differed across professional groups.

- Key changes:
  - Single pension calculation for all.
    - Minimum pension (384 Euros).
    - Pension proportional to number of working years.
  - Single retirement age at 67.
  - ➔ Drastic cuts to some existing pensions.

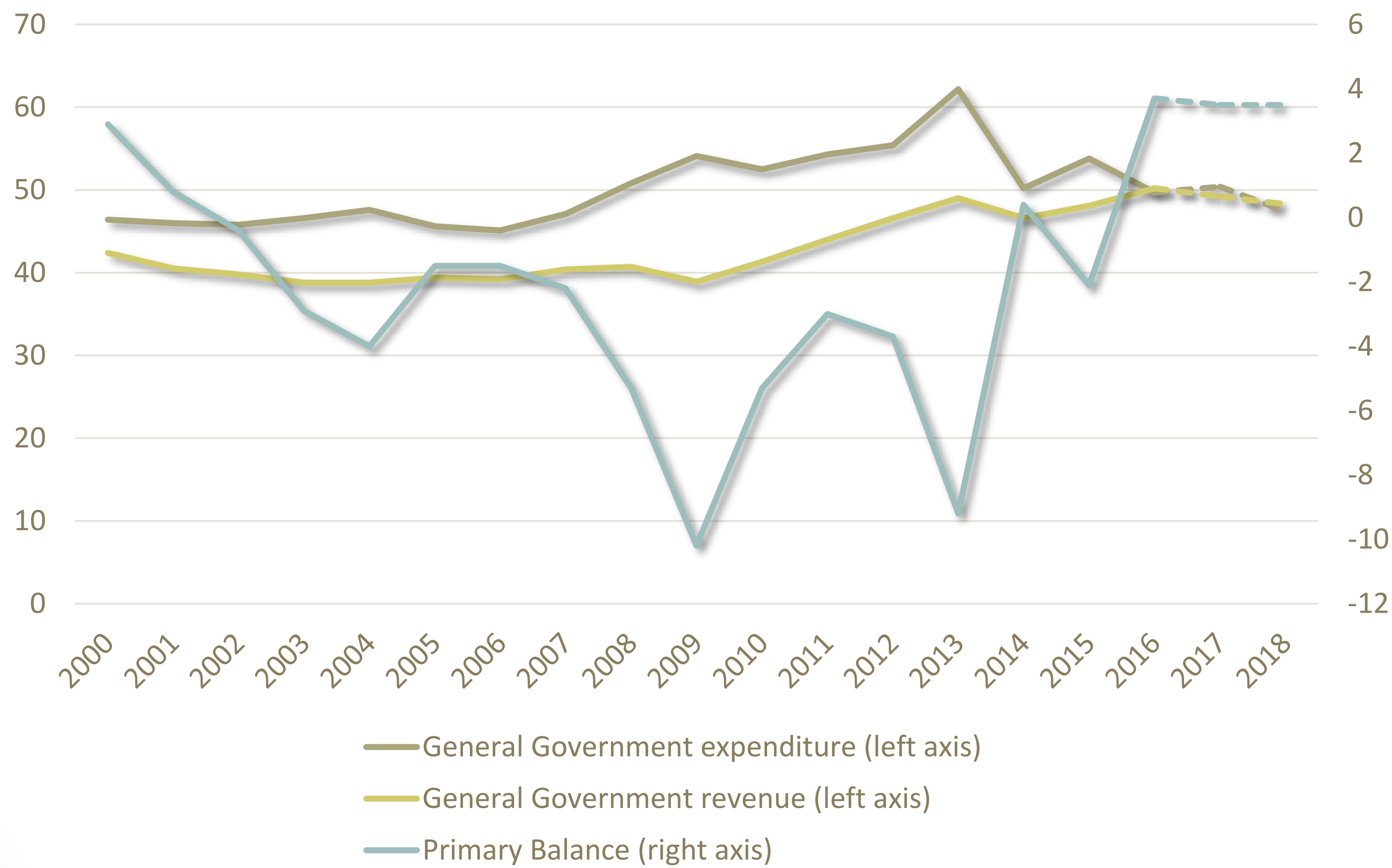
Product markets

- Over-regulated before the crisis.
  - PMR in 2008 second-highest in OECD.

- Reduction in barriers to entry and competition in a number of key sectors.
  - Implementation of “OECD tool-kit”.

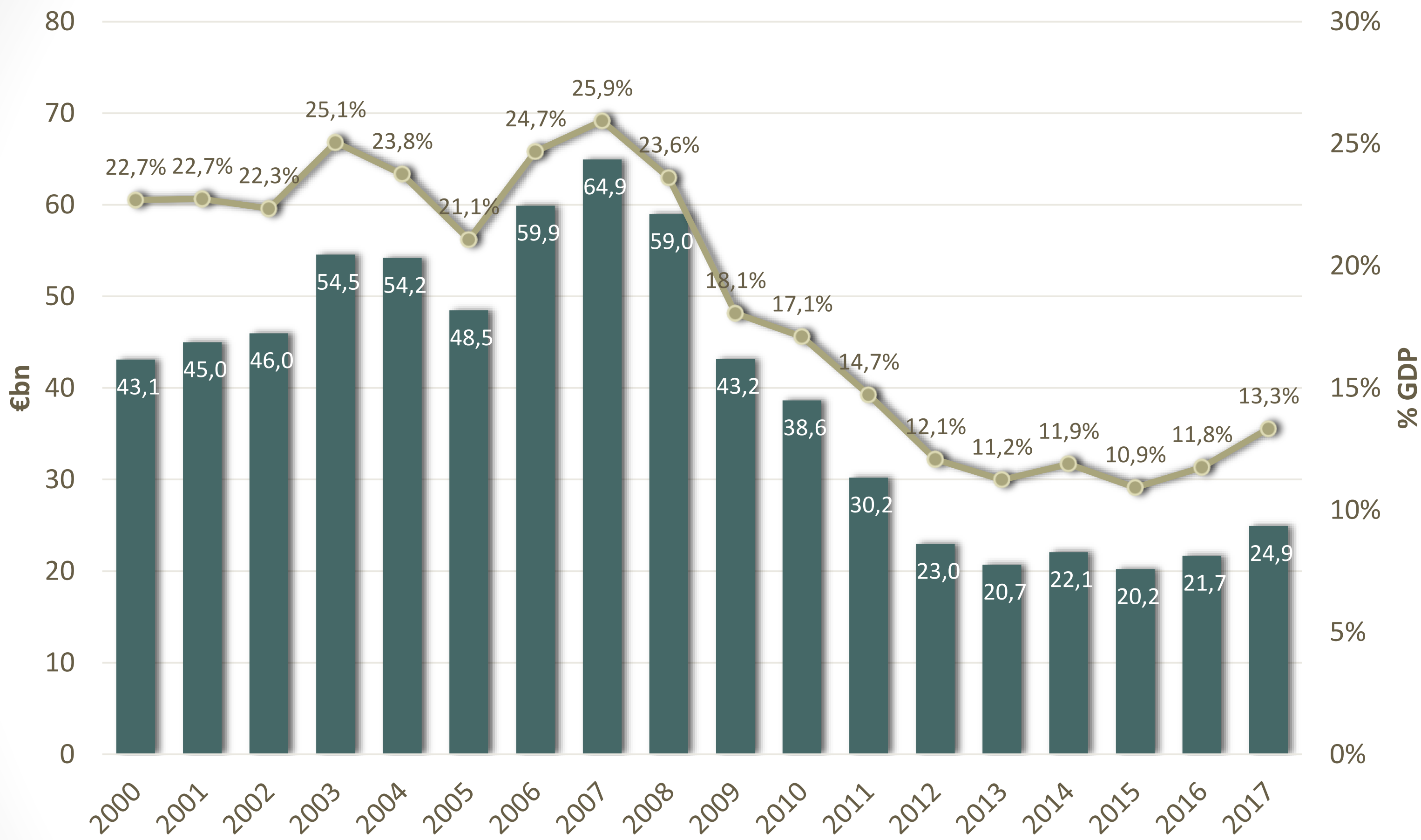
- PMR improved significantly.
  - Fourth-highest in OECD in 2013.
  - Dropped from 2.21 to 1.74. OECD average dropped from 1.59 to 1.47.

Government Expenditure, Spending, Primary Balance (% GDP)



Sources: Eurostat/European Economic Forecast, autumn 2017, European Commission

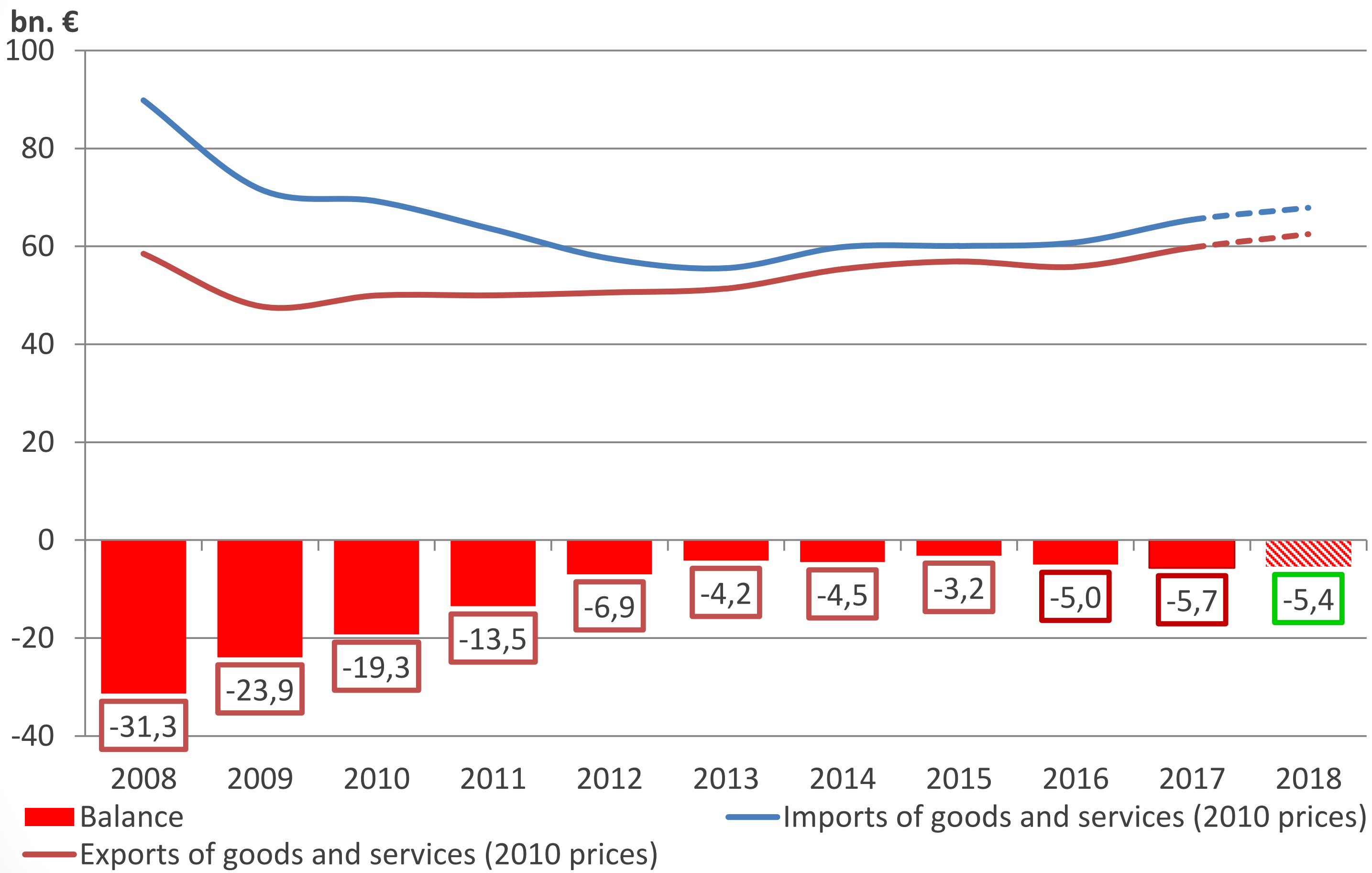
Investment collapses



Sources: Eurostat/ELSTAT

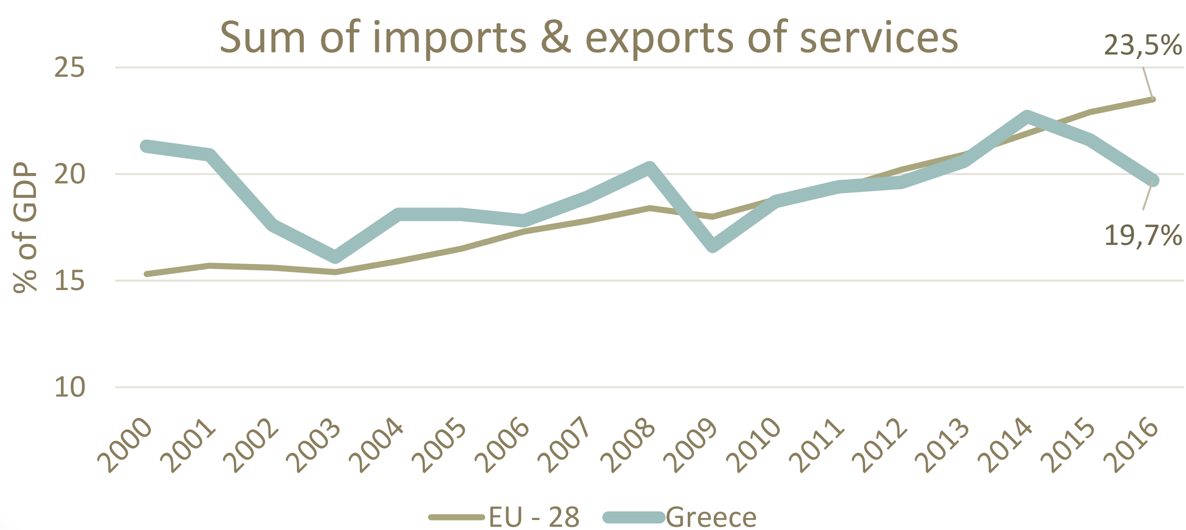
- Highest investment level in 2007 (€64.9 bn)
  - Highest level of investment as a % of GDP in the same year (25.9%)
- Significantly lower investment in 2017 (€24.9 bn, 13.3% of GDP)

Trade balance (goods and services)



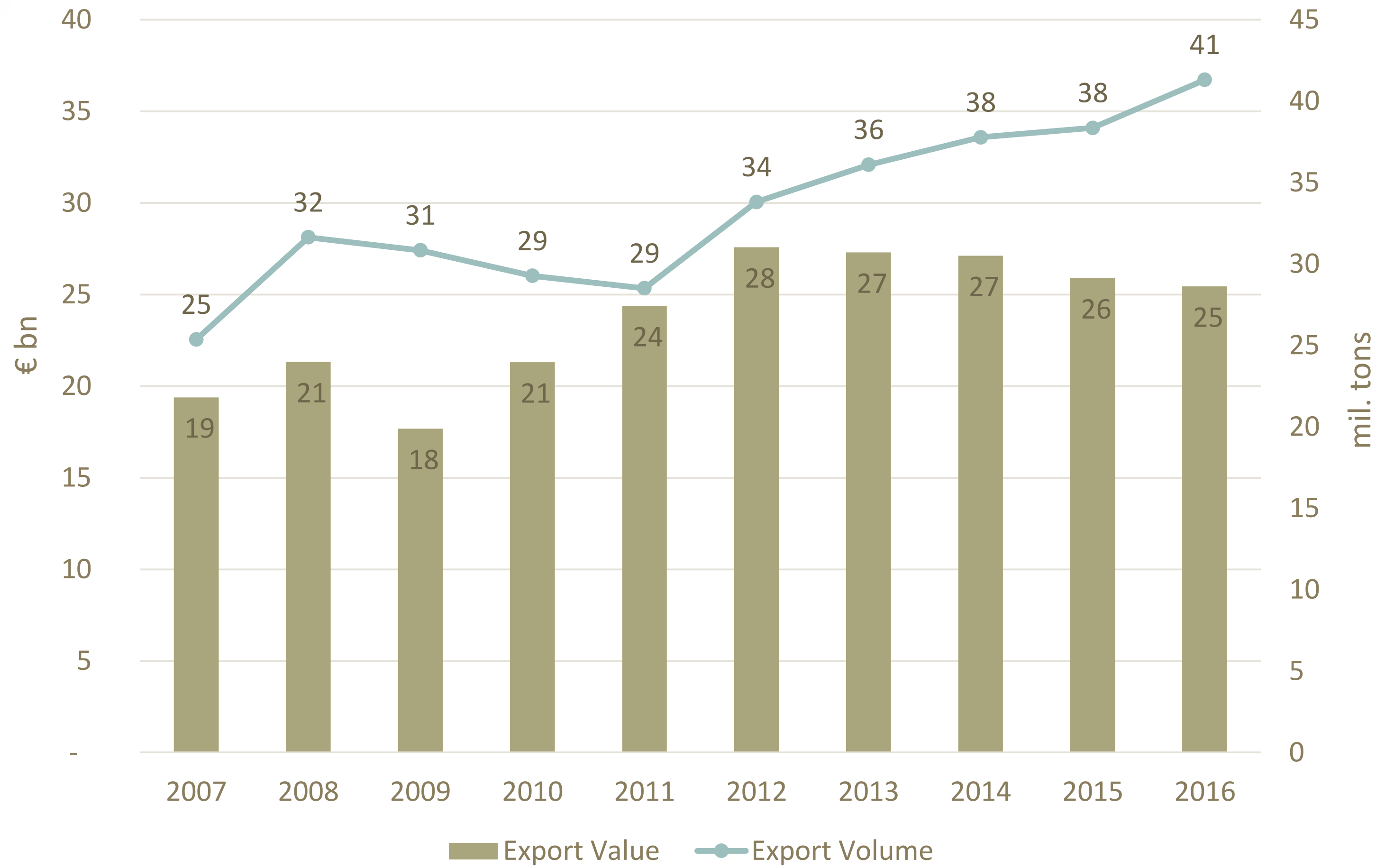
Source: AMECO

Openness



Source: Eurostat

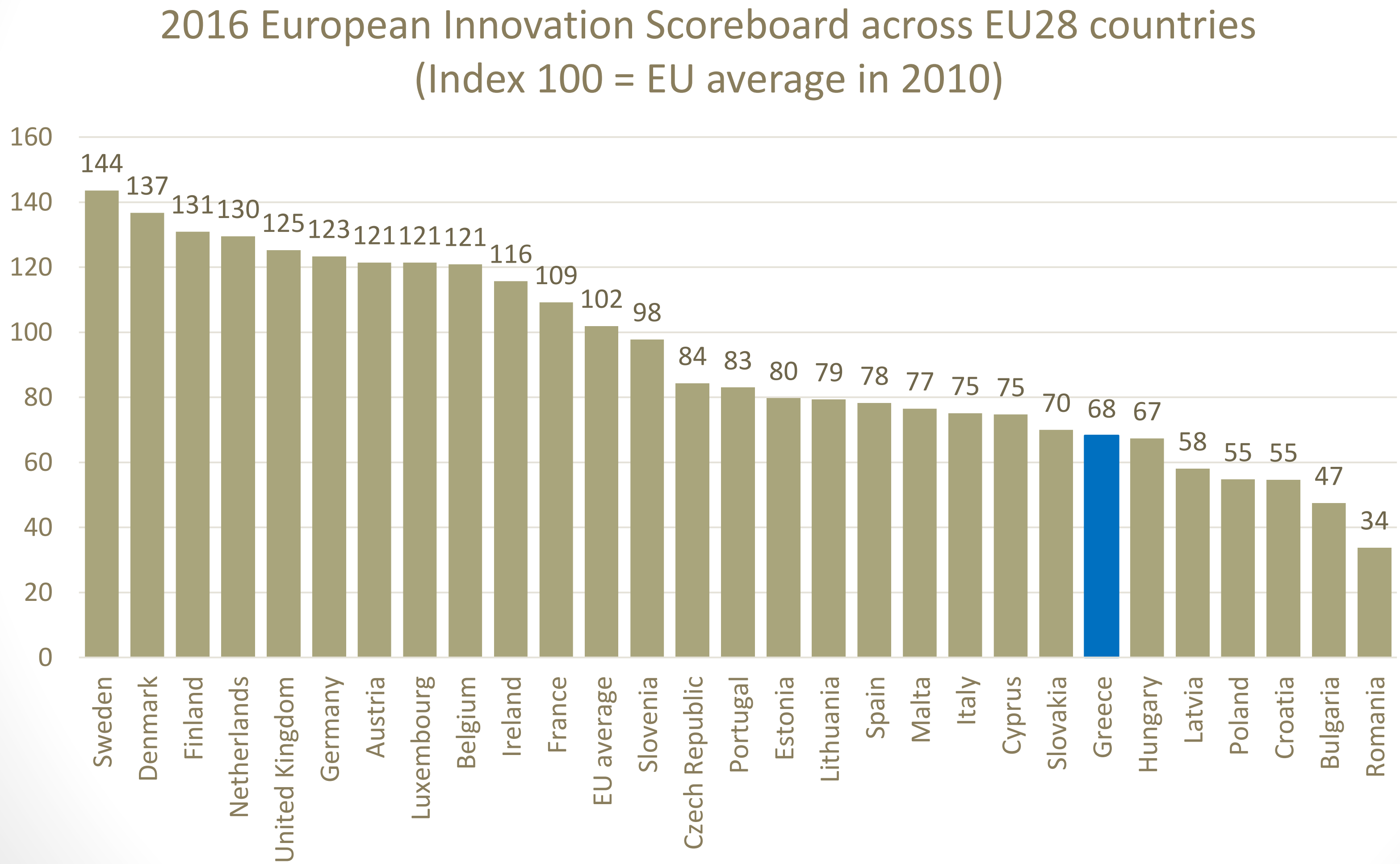
Exports of goods



Source: Eurostat

- ➢ Change in the value of exports, 2007-2016: +31.2%
- ➢ Change in the volume of exports, 2007-2016: +62.9%

Innovation



Source: European Commission

Current picture

- Economy has been stabilized; current growth prospects are weak.
- Economy does not generate new fiscal deficits; but mix of tax revenue and expenditure neither contributes to growth nor serves social protection.
- Trade deficit has been fixed; but exports growth is weak and uneven. External risks.
- Public debt has been stabilized; but level of public and private debt hinders growth, access to finance is problematic.

A ‘growth agenda’

1. Open markets, improve institutions that facilitate long-term productive investment.

2. Education and Health Care systems.

3. Allow the economy to shift towards local comparative advantages: geography and technology.

Details: conditions for growth

- Education system: governance needs modernization, extremely heavy control by state.
- Health care: significant reduction of public expenditure but structure should provide incentives.
- Health care and education also provide important opportunities for investment and growth with Greece becoming a local hub.
- Public administration: fine-tuning the level of autonomy of units from central control.
- Justice: remains very slow.

Looking a bit deeper

- Shift to a new growth model implies investment and exports will be a larger part of the economy.
- Uncertainty keeps investment out: it depresses growth directly, but it also weakens incentives and effectiveness related to structural reforms.
- Diminish burden of State on economy: allow dynamic part of the economy to grow faster. Shift economic activity away from non-tradables and state-based rent seeking.

Growth prospects

- Growth prospects are high. Significant unrealized potential.
- But only as long as reform efforts continue. ‘Reform’ does not refer to ‘level’ but to ‘dynamics’.
- Functioning of an efficient and non-partisan State.
- Reduction of uncertainty is essential to facilitate investment inflow and management of public and private debt.
- Medium-term vs longer term growth (“the crisis is too good an opportunity to waste”)

Transition and perspective

- Adjustment programs operated as an implicit contract between Greece and its debtors: managing old debt versus fixing structure and eliminate deficits.
- Inertia from current dynamic is **not** enough. A lot more is required, a more ambitious approach.
- Investment?
- Public debt is high - a credible mechanism to (a) prevent debt from generating excessive tax burden and (b) provide systematic incentives for reform.
- Insurance as Greece gradually gains access to capital markets. Cash buffer vs credit line. Frankfurt and banks.
- Investment programs: Brussels. EU responsibility.
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Evolving views in politics and public opinion

1. Greece is immune to the world financial crisis.
2. Greek public debt is sustainable + no bail out.
3. Greece is ‘unreformable’ + there is ‘another way’
4. The (only) solution is for Greece to leave the EZ.
5. Greece needs and deserves a massive nominal debt reduction.
6. ‘Clean exit’.

Some more clarity (and credibility)!