Questioning Greece’s future from the other side of the Atlantic

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By Eleni Louri-Dendrinou

In the last month (20 Sept-18 Oct 2015) I visited a number of universities and think tanks in Canada and the US to give a series of lectures supported by the Onassis Foundation lectureships program. Visiting six cities and many more institutions in four weeks was a demanding but rewarding experience.

The subject was the adjustment of the Greek economy and in particular of the banking sector within the changing governance of the Eurozone. And there was an impressive amount of interest in progress in Europe and Greece even in places as geographically remote from the old continent as Vancouver, San Francisco or Sacramento. Interest was also strong in New York, New Haven as well as Washington. Fifty participants attended the last lecture given at the World Bank mostly staff of the Bank and the IMF but their interest was more or less expected given their knowledge of and involvement in Greece.

The most common question after each lecture had to do with the survival chances of the Eurozone and Greece as a full member. Eurozone’s incomplete architecture, in spite of the improvements adopted since the peak of the crisis such as the Banking Union, was commented upon as inadequate. Eurozone’s obsession with more austerity in order to fix fiscal problems was described as self-defeating, in the sense that it created a deeper recession than forecast and hence fiscal problems remained unsurpassable.

Look at the cumulative loss of GDP in Greece since 2008, they said. You’ve lost a quarter of your GDP and your debt is still increasing. It is now close to 200% while it was 120% in 2008, they pointed at my diagrams! So your adjustment seems to create more problems than it solves and where does it lead? And the banking sector has such a limited time and resources to get recapitalized until the end of 2015! Such questions full of doubt about Greece’s progress were equally expressed by academics, students, bankers and ‘think-tankers’.

So to all these similar-type questions my answer was conditionally optimistic. Yes, Greece is more likely to make it than you expect, in the sense that conditions are there for economic growth to recover. An enormous amount of adjustment has already taken place in the last five years which has created the recovery conditions of 2014 and early 2015. With political stability reinstalled and a new funding agreement in place as the basic arguments of my positive answer, here are some facts and numbers which can be more convincing.

The economy is likely to fall back into recession in 2015 in spite of a (small) positive growth performance in 2014 and in the first two quarters of 2015. It’s the imposition of capital controls (end of June) and the fiscal burden which is quite heavy in the last quarter of 2015 that will affect the economy negatively. The banking sector lost more than €40 bn (or 25%) of deposits since December 2014 due to the protracted negotiations and the political instability. And non-performing loans have become a huge challenge for Greek banks exceeding 35%. So banks are in bad shape to provide funding for growth.

But the new adjustment program which was agreed upon by the vast majority of the Greek Parliament in August, and which can mobilize up to €86 bn in financial assistance to Greece until 2018 has already started to be implemented. The program contains policies for sustainable public finances less demanding than in former programs, for instance fiscal surplus of -0.25% in 2015 and 0.5% in 2016, showing that Greece’s creditors have developed more realistic expectations. On top, competitiveness enhancing policies, such as opening product markets, easing investment procedures and scaling up a privatization program have been included.

Financial stability can be maintained starting with the Single Supervisory Mechanism (SSM) capital needs assessment with a strict timeline: disclosure of capital needs by end of October and recapitalization by the end of December 2015. No haircut for depositors is discussed. A financial envelope of €25 bn (out of the €86 bn) is allocated exclusively to the banking sector and will be used for recapitalizing banks along with private sources. The question of bank managements which may have to change in favor of clientelistic preferences (I was also asked that question) is not valid, since any management will have to be approved by the European supervisor, the SSM. The European Banking Union is mostly in place now and the new financial governance in the Eurozone is responsible for the supervision, the resolution and the deposit guarantee schemes covering banks, offering a much wider and inclusive safety net.

With political stability in place, this adjustment framework looks quite capable of pushing Greece back into positive growth, especially if a first positive assessment of the program implementation leads to opening up negotiations on debt sustainability and restructuring. A virtuous circle can then start provided there is no hesitation, delay or endless and aimless discussions. If focus, clarity and decisiveness prevail, Greece has the potential to recover within the Eurozone faster than many people in the other side of the Atlantic think possible.

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