SPECIAL ANALYSIS

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Never-ending Story: Greece

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Introduction

It is not necessary to present Greece for a long time. This cradle of European culture is a very popular tourism destination, which offers both historical heritage sites and natural wonders. General awareness has also been contributed to by the fact that this year Greece was (and for some time will remain) undoubtedly the EU state most often mentioned in the media.

Greece is going through a very stormy year, rich in events. The reason why this member state is attracting so much attention from the media and other EU states can be summarised very easily: Greece's difficult financial situation and the related threat of state bankruptcy and the risk of a Grexit, Greece's departure from the Eurozone. Some important and interesting information related to it, regarding for example Greece's macroeconomic situation, industrial sectors, tourism, instalment amounts, rescue packages and much more needs to be savoured well, because it is sometimes difficult to become oriented in the flood of news and expert discussions regarding Greece.

How time has passed with Greece

The fact that the financial system in Greece is not entirely healthy was immediately apparent this January, when two large Greek banks asked for funds from the emergency financing mechanism, which the European Central Bank then approved for them the following week. A key event for developments in Greece occurred just a few days later.

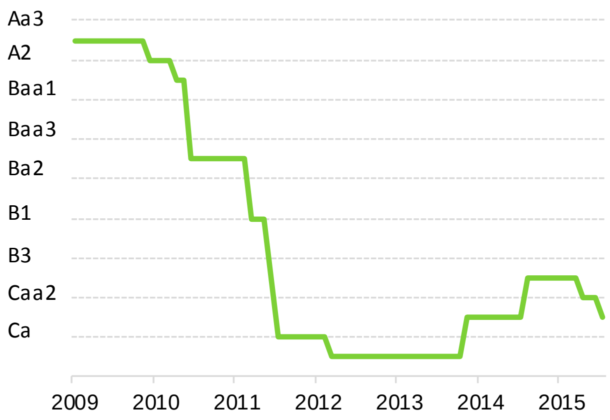
On 26 January, the country held early parliamentary elections. The winner (with 36.3% of the votes) was the left-wing Syriza party led by Alexis Tsipras, who was subsequently named Greek prime minister. Syriza gained its needed majority in parliament thanks to a deal with the Independent Greeks party. The blow for financing was the „drying up" of one of the sources that the Greek government had been relying on. At the beginning of February, the European Central Bank decided that it would not accept the Greek government's bonds as a pledge for loans to commercial banks.

However, the highly indebted country must also make arrangements with its creditors. Following an agreement with ministers from Eurozone countries, Greece managed to get the end date of the loan assistance programme moved another four months forward. However, what the country did not manage to achieve was reduction of or a halt to the outflow of capital due to the crisis affecting Greek banks. The volume of deposits also decreased rapidly to its lowest level in several years. However, even with financial problems, the Greeks managed to meet their obligations and pay several debt instalments, including EUR 310 million in March, EUR 448 million in April and EUR 775 in May to the IMF.

Together with problematic financial developments, not only did the predictions for the development of Greece's economy for subsequent periods worsen, but the outlook for the country's credit rating from agencies also worsened. The credit rating is important for investors, because it reflects the likelihood of the country's ability to pay back its loans and reflects the level of riskiness in the particular destination. At the end of July 2015, Greece's evaluation from rating agencies was in the speculative range (Moody's – Caa3, Standard & Poor's – CCC+, Fitch – CC), and if a rating is in the speculative range, a particular entity's bonds cannot be invested in by large institutional investors.

The Athens Stock Exchange and Greek banks have been closed since 29 June. The daily limit for withdrawal of cash from ATMs has been set at EUR 60 daily. Greece has become the first developed economy that has failed to pay back the IMF part if its debt from the rescue programme, in the amount of EUR 1.5 billion. Greece has asked the IMF to extent the period of time allowed for payment of the owed amount. At the end of June, the Greek parliament approved the holding of a referendum on adoption of proposals from international creditors for resolving Greece's indebtedness. The referendum itself took place on 5 July 2015.This referendum provides a certain reflection of the condition of Greek society and of how the Greek government is „negotiating" with its population.

Credit Rating of Greece by Moody's



Source: Moody's

The result of the referendum was relatively clear: 61.3% of voters rejected the international creditors' conditions and stated "No, I don't approve," on their ballots. It may be appropriate to point out how the question was presented in the referendum and what its entire wording was. It is typical for the "yes" option to be specified first. However, in the Greek referendum, the "no" option was the first listed choice. And what exactly was the question that Greeks answered?

"Should the draft agreement submitted on 25 June to the Eurozone by the European Commission, the European Central Bank and the IMF, consisting of two parts forming the entire proposal, be adopted? The first document is entitled "Reforms for the completion of the current programme and beyond" and the second is entitled "Preliminary debt sustainability analysis."

Although in a sociological survey more than 80% of Greek citizens voiced support for keeping the euro, the country had to hold a referendum, which was basically pointless, because the government did not act based on the referendum results anyway.

On the day after the referendum, Janis Varufakis resigned from the position of finance minister, and Euklidis Tsakalatos became the new Greek finance minister. Indebted Greece officially asked the ESM for new loan assistance on 8 July. However, under the rules of the European Stabilisation Mechanism, the assistance itself must be connected with economic reforms, which must be approved by the European Commission, the ECB and possibly also the IMF. Therefore, Greece has begun preparing a package of reforms, which in the years to come should bring significant savings of approximately EUR 10 billion. Greece presented its 13-page proposal to the Eurozone states on 10 July. The representatives of the mentioned institutions, the European Commission, the ECB and the IMF, evaluated the proposal positively and consider it a basis for further negotiations regarding provision of a third rescue package worth up to EUR 86 billion. Greece received two rescue packages already in the past.

The first package – was received in March 2010, when the Eurozone decided to provide bilateral loans shared with the Commission in the total amount of EUR 80 billion. That amount was then reduced by EUR 2.7 billion, because Slovakia, Ireland and Portugal refused to participate in the financial assistance. The financial assistance agreed upon with the Eurozone member states was part of a joint package with the IMF, which mediated another EUR 30 billion.

The second package – was received in March 2012, after which Eurozone finance ministers approved its financing. Eurozone member states together with the IMF agreed on a loan of EUR 130 billion plus unpaid amounts from initial assistance and drawing of funds between 2012 and 2014. The total assistance reached EUR 164.5 billion, of which EUR 144.7 billion was provided via the European Financial Stability Facility (EFSF), while the IMF contributed EUR 19.8 billion. Drawing was postponed or halted several times before creditors reached a deal with the newly elected government. Following negotiations between creditors and the Greek government, the drawing was extended until February and then until 30 June of this year.

The Greek government approved the reform proposals as a basis for negotiations with creditors. By adopting the financial rescue package, Greece committed to reforms related to VAT, tax collection, pensions, public sector employee wages and other measures.

Main reform points adopted by Greece

Value-added tax (VAT): VAT collection should be made more effective. Greece will continue to have three VAT rates, 23%, 13% and 6 %. Changes will be made to the division of individual services:

- restaurant and catering facilities will be moved to the 23% basic VAT bracket;
- basic food products, utilities, accommodation and water will remain in the reduced 13% bracket;
- the lowest rate will remain in effect for medicines, books and theatres;
- by the end of 2016, tax discounts on islands will be abolished, starting with the islands that are most popular among tourists.

Tax reforms: A major emphasis is being placed on strengthening the legal framework for the purpose of making tax collection more effective. Increasing checks, powers and punishments for avoiding tax obligations.

- increasing the corporate tax rate from 26% to 28%;
- a special 12% tax for companies with profit exceeding EUR 500,000;
- abolishing of subsidies for consumer taxes on diesel fuel for farmers;

- revision of individual coefficients in relation to property taxes;
- simplifying individual income tax calculation, increasing and integration of solidarity surcharges;
- introduction of a tax on TV advertising and 30% taxation of gambling slot machines;
- increasing the tax rate on luxury boats from 10% to 13%.

If Greece has a fiscal budget deficit in 2015 as well, then based on the adopted reforms it must consider further increases of individual and corporate income tax rates.

Pensions: New changes in the area of pensions relate to early departure, freezing of limits, increasing of health insurance and cancellation of special contributions for retirees.

- Limiting of early retirement and setting conditions, including sanctions, for early retirement. An exception will remain in place only for demanding professions and for mothers caring for children with medical disabilities;
- Freezing monthly nominal pension limits until 2021;
- Increasing the health insurance contribution from an average of 4% to 6% and expanding it to supplementary retirement insurance;
- Abolishing of the special contribution for retirees, which ranged from EUR 57 to 320.

Public sector employee wages and other measures:

- Reform of wage tables, harmonisation of non-wage benefits. Establishing ceilings for payments of employees in individual positions in the public sector;
- Reduction of the defence spending ceiling by EUR 100 million and EUR 200 million for 2015 and 2016 respectively;
- Privatisation of the state Independent Power Transmission Operator (ADMIE) and other state property.

The European Commission has recommended providing Greece with a bridge loan via the European Financial Stabilisation Mechanism. That assistance should help cover Greece‘s soonest due obligations.

Greece has gained access to a three-month bridge loan in a total volume of EUR 7.16 billion from the EFSM.

According to the Finance Ministry‘s press release, the Czech Republic, following a deal with countries outside of the Eurozone, including Great Britain, Sweden and Denmark, is participating in negotiations regarding the possibility of securing a short-term loan for Greece for a period of up to 3 months. If Greece does not repay the loan, the Czech Republic and other states outside of the Eurozone will not be responsible for covering the losses, since they will be covered by the revenues from Greek bonds held by the European Central Bank (ECB). A couple of days ago, Greece paid the amounts it owed to the IMF, and therefore the IMF is prepared to continue helping the country.

Athens was visited at the end of July by representatives of international creditors (the IMF, the EC, the ECB) and the European Stabilisation Mechanism (ESM) to discuss the new rescue programme for Greece, after the Greek parliament approved what is already the second package of reform measures. The creditors conditioned the commencement of negotiations on economic reforms and austerity measures. The negotiations with creditors should end by 20 August, when Greece must pay back its debt of approximately EUR 3.4 billion to the ECB.

Tourism - still in good condition

Greece‘s poor economic situation is not only a matter of this year, since Greece has faced the risk of state bankruptcy already several times in recent years, and had to be rescued by EU institutions by their providing of rescue packages to Greece in 2010 and 2012. Tourism is very important for Greece and brings the country significant state budget income. The direct share of tourism in Greece‘s GDP in 2014 amounted to 7% of the growth expected in subsequent years.

In 2014, the total growth in tourism (including investments and corresponding sectors) even amounted to 17.3% of GDP. Tourism is also a very important source of jobs in Greece, due to its high unemployment level. In 2014, there were more than 340,000 people working in the country‘s tourism sector, which represents 9% of the total employed population.

In 2015, growth in employment in this sector by 3.8% (353,000 jobs) is expected. As far as the total benefit of tourism from corresponding sectors, the number of people working in them in 2014 even ranged at around 700,000.

The Greek Statistical Office states that according to a statistical survey of the Bank of Greece, the number of tourists in 2014 compared to the previous year increased by 23%.

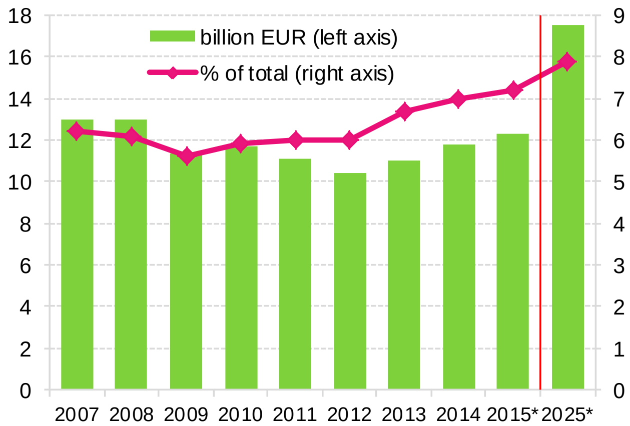
The popularity of mainland Greece and the islands has also increased among Czech citizens, by 21.1% to 350,000 in 2014. In 2014, Greece was visited by more than 22 million tourists, including 13.2 million from elsewhere in the EU.

It is recommended that tourists travelling to Greece bring with them enough cash and the medications that they use, but otherwise their stay should basically be problem-free. So far it is apparent from the most recent statistics that there has been 45.6% growth compared to the same period of 2014.

However, the number of tourists for the first quarter represents only a fraction of those who travel to Greece during the main season, but it does give a certain reflection.

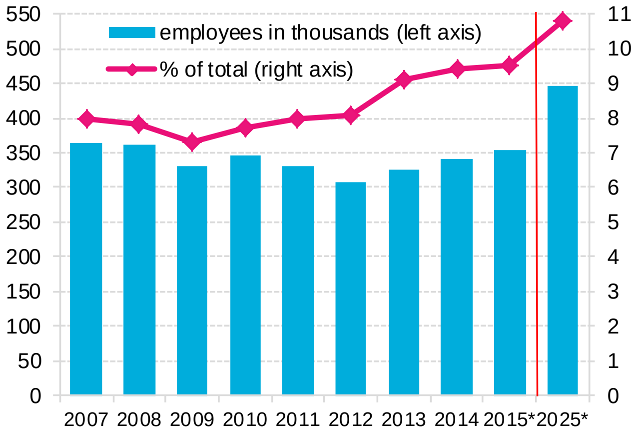
This growth will be influenced by the unfavourable situation in certain other destinations and probably only very negatively influenced by events occurring in Greece.

Total Contribution of Tourism to GDP



*Source: World Travel & Tourism; Economic Impact 2015 Greece; *estimates*

Total Contribution of Tourism to Employment



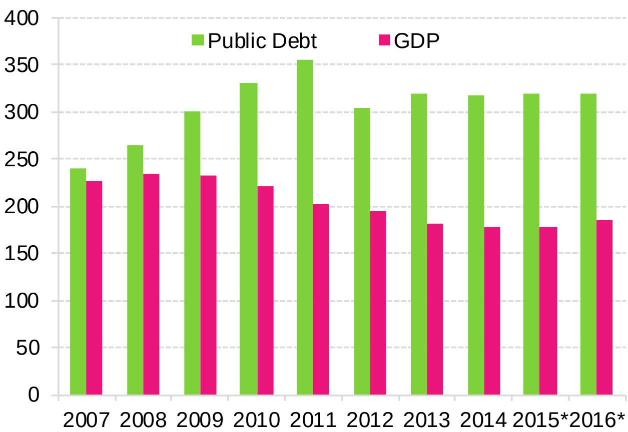
*Source: World Travel & Tourism; Economic Impact 2015 Greece; *estimates*

Economic burden of prior years

The unfavourable macroeconomic situation in Greece is not only a matter of the last few months. This southern state has been suffering from high public debt and declining GDP for a few years already. The absolute amount of Greek public debt (EUR 317 billion in 2014) is not so serious compared to other member states (it represents approximately a seventh of the debt of Italy, Germany or even the UK, whose debt hovers around EUR 2.1 trillion), but in relation to GDP Greece's debt is the highest in the EU.

With its public debt at 177.1% of GDP, Greece's debt greatly exceeds that of the second place country Italy (132.1% of GDP) and third place Portugal (130.2% of GDP). The unhealthy economic environment and low competitiveness also bring with themselves a high unemployment level of more than 25%. The major social problems are reflected mainly in the youth unemployment level, which hovers at around 50%.

Gross Public Debt and GDP in bln EUR



*Source: AMECO, EC; *estimates*

Production in Greece

According to Eurostat, work productivity in Greece is not at all at a favourable level, but some members of the Eurozone are much worse off. While in Greece for an hour of work EUR 20 is generated in permanent prices based on 2005 statistics, in Latvia and Lithuania the figure is approximately EUR 10, half Greece's amount. Of the 19 members of the Eurozone, Lithuania, Latvia, Slovakia and Portugal have lower work productivity than Greece.

Eurostat's statistics about the number of reported worked hours show another interesting phenomenon: Greeks work more hours per week than anyone else in the EU. The average Greek employed full-time works 44 hours per week (compared to the EU average of 41.5 hours).

Let's examine the Greek economy in greater detail. It is true that Greece traditionally has a low share of industry. It accounts for 16% of GDP and employs 14% of the population. A very strong sector in Greece is the service sector, which accounts for nearly 80% of Greek GDP. The Structural Business Statistics (SBS) are an indicator of the actual productive output in the economy.

In four sectors – industry, construction, trade and services – it monitors detailed information at the level of very detailed sub-sectors.

It is important that these statistics focus on companies and ignore the role of the state and of the financial services sector. The most important indicator is the total volume of production (measured by added value), and in Greece it is a third lower than in the Czech Republic. The most important sector at the level of NACE2 in Greece is wholesale and retail, which creates 15% and 11% of added value respectively, 50% more than in the Czech Republic.

Accommodation and the higher representation of the energy and telecommunications sectors are also worthy of attention. That may be due to the fact that energy and telecommunications are essential – at lower production, the energy and telecommunications sectors will always yield the same production.

It can be stated in general that Greece produces much less than the Czech Republic, not only in terms of volume, but also in terms of the number of industries that the Greeks are involved in. That is not good news for Greeks.

The most important sectors of the Greek economy based on value added and employment in mln EUR

NACE2	Value Added		Number of Employees	
	Greece	CR	Greece	CR
Wholesale trade, except of motor vehicles and motorcycles	15%	9%	15%	8%
Retail trade, except of motor vehicles and motorcycles	11%	6%	15%	9%
Manufacture of food products	5%	2%	5%	3%
Electricity	5%	7%	2%	1%
Construction of buildings	4%	2%	3%	3%
Land transport and transport via pipelines	4%	5%	2%	6%
Telecommunications	4%	3%	2%	1%
Accommodation	3%	1%	4%	1%
Warehousing and support activities for transportation	3%	2%	2%	1%
Total	54.4 bln EUR	82.4 bln EUR		

Source: Eurostat – SBS; sectors participating in more than 5% of total value added. The latest available information is from 2012.

It has been shown that the more products countries are able to produce, the more successful they are on the international market (Hidalgo; the Product Space Conditions of the Development of Nations).

Conclusion

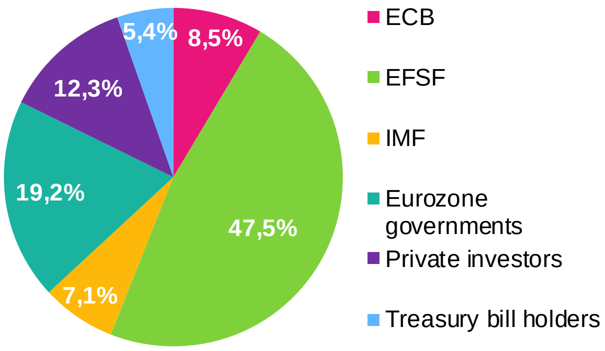
Greece's participation in the Eurozone seems rescued for a certain period of time. However, Greece and the Greek population are awaiting fulfilment of the reforms that they should not avoid.

Now they should be willing to reduce government spending, which is not sustainable in the long-term, and if possible to jumpstart the economy as soon as possible and mainly to improve the situation on the labour market.

The unemployment figures in Greece are truly dreadful. So is the amount of Greece's debt.

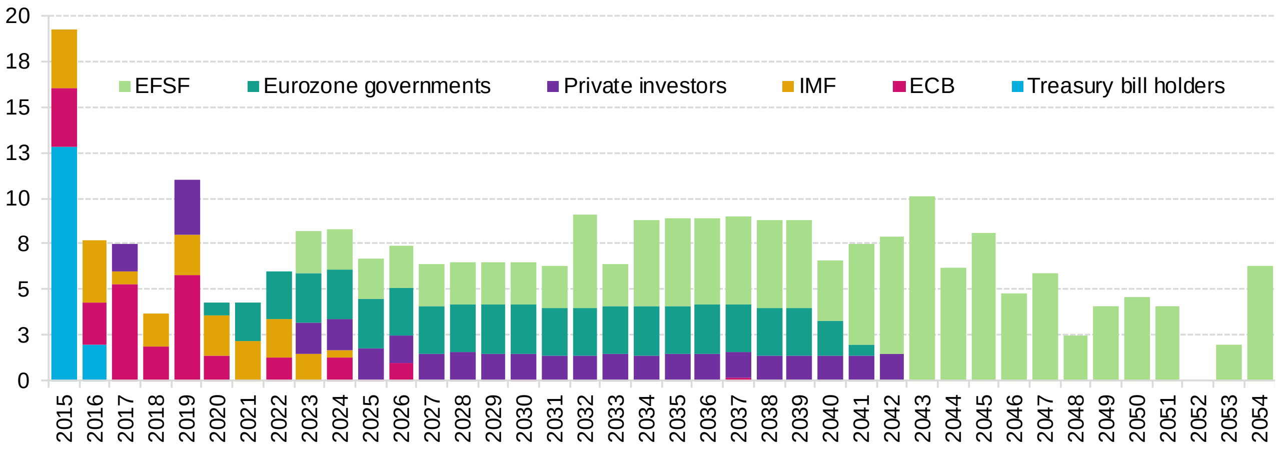
Greece's largest creditor is the European Financial Stability Facility (EUR 130.9 billion), followed by other Eurozone states, which Greece owes EUR 52.9 billion, and the ECB, which is demanding EUR 23.6 billion.

Greece's creditors



Source: WSJ

Planned debt payments to the creditors in bln EUR (since August 2015)



Source: WSJ; EFSF - European Financial Stability Facility, EIB - European Investment Bank, IMF - International Monetary Fund, ECB - European Central Bank (note: debt to EIB is just 0.02% of total)

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