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Greece: Mapping a Path Forward

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Greece has, for the first time, completed its obligations promptly, thus paving a path for a successful completion of its third, ESM (European Stability Mechanism) - backed programme in August 2018. Although the conclusion of the third review still requires the timely implementation of a difficult set of prior actions, both the Greek government and the Institutions are working under the assumption that these will be completed within schedule, at the next Eurogroup meeting in January. A lot is at stake. Greece wants to finally shake off the tough guardianship, effectively the loss of national sovereignty in a number of economic and other policy sectors, which its home-made fiscal delinquency brought about. After all, it has restored a number of macroeconomic imbalances, the excessive deficit procedure brought against it in 2009 has been closed and its primary fiscal surplus is projected to reach 3.57 percent of GDP in 2018 – albeit on the back of a socially unjust and largely unsustainable policy mix. Obviously, in case there is a need of a reminder, membership of the monetary union continues to come with significant governance constraints and Greece will be subjected to the same, if not stricter post-programme surveillance as Portugal, Ireland, Spain and Cyprus, considering the size of the financial envelope it received.

The Institutions, on the other hand, no longer wish to risk their reputation and their credibility on the ‘Greek case’. Although the form of support to be offered to Greece after the end of the programme is still on the table, there is simply no appetite for financing a fourth programme and no political capital to be invested in it. The Institutions know that the key to Greece’s return to normalcy lies both in the continuation of structural adjustment reform, where progress has been patchy, and sticking to a path of fiscal prudence where historical experience shows that the medium-term primary fiscal surpluses demanded for a country with Greece’s economy are unattainable and socially disastrous. For the Institutions, Greece remains caught between its history of reform ‘ownership’ and still low projected levels of GDP growth. No one likes to admit it but, in spite of all the aid and policy conditionality thrown at Greece, its economic model remains primarily based on private consumption, the much heralded shift to export-led, tradable sectors in limbo. Worse, the country remains a laggard in every single indicator measuring competitiveness, economic freedom and quality of institutions and governance.

Realistically, for sustainable GDP growth to take hold under these conditions and for confidence in the country’s prospects to return, the IMF, the EU institutions, and some creditor countries should finally agree on the debt relief that Greece needs post-programme. The European Stability Mechanism has implemented, throughout 2017, a package of short-term debt measures, including the smoothing of Greece’s repayment profile and reducing interest rate risk. It has estimated that these will reduce the country’s debt-to-GDP ratio by about 25 percentage points by 2060, and the gross financing needs-to-GDP ratio by around six percentage points. It has however failed to make public the assumptions on which it bases its analysis or the specific path of the debt indicators. The official European position remains that additional measures will only be provided at the end of the ESM programme (August 2018), and on the basis of a debt sustainability analysis. The Fund, on the other hand, argues that without meaningful debt reduction, Greece’s stock of debt will continue to hold back investment and capital inflows. A principled compromise is due if only to avoid further reputation damage or worse the implementation of *another* Greek programme. Additional debt relief should come with strings attached, should be vested interests-proof and should be subjected to the right conditionality. While the Greeks cry reform fatigue and the Institutions place limited trust in Greece, a significant, last effort to tie the targeted opening up of the economy with debt sustainability, fiscal prudence, strengthening of productive capacity and improved social protection for the vulnerable should be made.