Executive Summary

The Greek economy is recovering rapidly

After a dramatic recession of 9.0% (according to the revised data of ELSTAT) in 2020, the Greek economy shows a “V-type” significant recovery. Essentially what we see is a verification of the “spring theory”. And it is not just the data of the last quarter that verifies this estimate. The estimates of foreign and domestic investors and banks raise the growth rate of 2021 to around 8%, much higher than the revised 6.1% of the government: at 7.5% the National Bank of Greece; at 7.8% UBS, Oxford Analytics and Moody’s Analytics; at 7.9% KEPE (see section 1.3); at 8% IOBE; at 8.5% Capital Economics and at 8.6% Scope Ratings. It is now clear that state support of about 40 billion euros saved the economy’s productive base, significantly increased deposits and kept unemployment at 13.9% in August 2021, which is the lowest level in 11 years.[1]

What are the main drivers of growth?

The main drivers of growth (during the first half of the year), are fixed capital investments (11.8%), public consumption (7.0%), exports of goods & services (5.8%) and private consumption (4.7%) (see section 1.1).

Investments

Recently, there has been an increase in various business agreements and investments, such as that of Digital Realty (the largest manufacturer of Data Centers in the world), Pfizer in Thessaloniki, CISCO and the shipbuilding group Fincantieri (Elefsina Shipyards, following the successful completion of the tender for the Scaramanga Shipyards with the bidder, Mr. Prokopiou). Essentially, what is observed is that the investment funds are looking for a place in the Greek market, precisely because they see that the next period is very positive. This is also confirmed by the successful processes of selling 100% of DEPA Infrastructure to Itaglas for 733 million euros, the concession of Egnatia Odos to the GEK-TERNA-Egis Projects consortium for 35 years, for a total benefit of 2.8 billion euros, and the acquisition of 49% of HEDNO by Macquarie, for 2.1 billion euros.

Exports

In Greece, the effects of the pandemic on exports were manifested in the second quarter of 2020, with a relatively mild negative rate of change, while in the third and even more so in the fourth quarter of the year, the country recorded a significant recovery in exports. By contrast, the EU has seen an average drop in exports of goods since the first quarter, with the situation deteriorating rapidly in the second quarter, but with some first signs of a marginal recovery emerging towards the end of the year. In relation to the prospects of the Greek export sector for the year 2021, the developments in the international environment are expected to create more favorable conditions for the development of Greek exports of goods. Based on the evidence so far, the European and global economies are recovering this year, boosting international trade. At the same time, the needs for pharmaceutical products are expected to remain increased, while oil prices are higher than last year, which, combined with increased demand, is expected to significantly enhance the value of Greek exports.

Inflation: the biggest risk for the recovery of the Greek economy

In recent months, we have seen an increase in the prices of almost all goods (see section 1.2). The increases are particularly noticeable in energy (gas, electricity, oil) as well as in transport and raw materials. For example, the price of oil rose to about $84 per barrel, more than four times higher than that recorded in the midst of the pandemic (about $20 per barrel in April 2020). The prices of electrical items have increased by 60% since the beginning of the year. The cost of a container has skyrocketed from €1,500 last year to €12,000 this year. The rise in the price level in commodities, and especially in energy, that has taken place in recent months may significantly burden family budgets, ultimately squeezing the purchasing power of households. The Greek government, in an effort to curb the effects of price increases on households, has already taken measures to support society against the nega-

1. <https://www.statistics.gr/el/home>

tive effects of the energy crisis, such as increasing the heating allowance (from 36% for households without children, up to 68% for households with three children) and in broadening the eligibility criteria to cover a larger percentage of households (over one million, compared to about 707 thousand households in 2020). At the same time, as the government had announced at the Thessaloniki International Fair, a subsidy will be given for household electricity bills, while a similar policy is expected to be applied to gas consumption bills. The budgetary cost of the subsidies of electricity bills is expected to amount to €326 million, and the cost of the heating allowance to €168 million. In addition, the prime minister announced during the Thessaloniki International Fair policies that lower the tax burden and support incomes and business (e.g., the extension of the exemption from the special solidarity contribution in 2022, the reduction of insurance contributions in the private sector, the reduction of corporate tax from 24% to 22%, the extension of the application of reduced VAT rates on transport, coffee and non-alcoholic beverages, cinemas and the tourist package by June 2022, etc.).

Inflation creates uncertainty for businesses and households as well as a big question mark: Is ***the return of inflation a temporary phenomenon*** *due to the faster adjustment of demand relative to supply to a post-pandemic normality,* ***or a structural change with more permanent characteristics*** *linked to the pursuing expansionary fiscal and monetary policy at the international level?*

A careful analysis of the global data leads to the conclusion that the inflationary pressures observed internationally ***are due to many different cyclical factors, all of which, however, appeared in the current situation, which will gradually decline***. E.g., the sharp drop in the price level last year due to the pandemic, combined with the rise in prices this year; the dynamic warming of economies after the lifting of restrictive measures, combined with the creation of stocks by companies to avoid future shortages; the imbalance between supply and demand in some sectors due to disruption in the global supply chain as well as to climate change (e.g., very hot summer and no winds in Europe, fires in Siberia, increased demand for air conditioners in Asia). Added to this is the (hasty?) change in the energy mix in the European Union, combined with the intention to move to a production model based more on renewables and less on traditional energy sources (e.g., lignite, coal and oil), which led to an increase in the price of carbon dioxide emission allowances paid by energy producers. This resulted in an increase in production costs, which is then passed on to both the wholesale and retail markets.

Will the current recovery course take on the characteristics of sustainable development?

Once the risk of inflation is overcome, the current recovery must take on the characteristics of lasting sustainable development, especially in light of the country's exit from enhanced supervision in 2023, and the country must return to investment grade as quickly as possible. The conditions for this to happen are the following:

First, the effective absorption of Recovery Fund resources and the continuation of reforms

The effective absorption of the resources of the Recovery Fund and the NSRF will help to fill the huge investment gap of the last decades in the country. It is a necessary, but insufficient condition. It is the reforms that are the sufficient condition for the current recovery to have the characteristics of sustainable development. Greece has made significant progress in recent years, implementing structural reforms that can strengthen the medium-term growth prospects of the economy. However, there are still some significant obstacles to achieving sustainable and strong growth.

The intensification of reforms, especially in the fields of **Education, Justice and Public Administration**, will increase the productivity of capital, making investments more efficient. The government is not alone in this effort: a large section of society is calling for change, and the government is called upon not to deny their expectations. Millions of parents are interested in the school results of their children, and thousands of teachers, despite the demands of their union leaders, would like to know the preferences of parents and children, the consumers of the service they provide. Millions of citizens and hundreds of investors are interested in doing their business quickly without unnecessary travel and wasteful spending. A universal application of evaluation is necessary in the State as well as a fundamental change of the evaluation system of judges that will be based solely on their performance.

Second, the restoration of fiscal balance

Despite the strong recovery, Greece's budget deficit and debt increased through the crisis and remain high (see sections 2.1 and 2.2). The sharp rise in the public debt ratio makes the economy vulnerable to new negative external shocks. Interim measures should be extended for as long as necessary in order to avoid the effects of their abrupt withdrawal. However, there is no room for easing the longer-term targets for primary surpluses, which are a prerequisite for financing needs for the next decade to remain manageable. If Greece quickly "covers" its deficit, and given its high cash flow, the loss of access to the ECB's quantitative easing after the end of the PEPP, if decided, will not necessarily be a concern for the markets.

Related to the above issue is the ***fight against tax evasion***. A recent report by the European Parliament reveals the great scourge of tax evasion in European countries, with Greece unfortunately emerging as a "champion" in the Eurozone.[2] The report estimates that **Greece loses 6 billion euros a year in tax evasion.** This amount brings it first in losses among the Eurozone countries and second overall in the EU, behind Romania. According to the report, the VAT revenues that our country could have received in 2020 were 21 billion euros. The amounts that ended up in the state coffers were about 15 billion euros, i.e., there is a huge loss in VAT revenues of 6 billion euros or 28.5%. This amount corresponds almost 2.5 times the income from ENFIA. This is the so-called "VAT gap", which reflects the difference between the expected and the actual receipts from VAT; and as the data show, almost 1 in 3 euros is not collected, with tax compliance at 68%. According to the report, none of the EU states collects 100% of VAT receipts. However, Greece could achieve higher rates; when it entered the EMU and until the Olympic Games, the tax compliance rates on the VAT front reached 81%. ***If, from the 6 billion euros that the country loses from the VAT receipts, it received 4 billion euros, then the way would be opened for brave tax relief measures as well as for the abolition of the taxes imposed in the years of the memoranda.*** Tax evasion in Greece has always been great, as has the informal economy. However, in recent years, its level, especially in the field of VAT, has increased. Probably this is due to the high tax rates and the reduction of incomes that push the market and its citizens to "black" transactions.

Finally, ensuring the liquidity of banks

Recently, the financial indicators of banks have improved significantly, as compared to March 2016. The stock of non-performing loans (NPLs) has decreased by 50% and more, mainly through securitizations utilizing the Asset Protection Program ("Hercules"). Banks were able to eliminate their reliance on the Liquid Assistance Facility (ELA) and regain access to wholesale financing markets by issuing unpaid high repayment bonds and capital instruments. Two systemic banks have also resorted to capital markets and successfully carried out share capital increases in 2021. At present, banks have sufficient liquidity and security capital reserves to allow them to lend to the real economy. ***However, the percentage of Non-Performing Loans in total loans remains the highest in the euro area*** and is a deterrent to credit expansion, especially to small businesses, which are characterized by a higher credit risk.

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2. <https://www.europarl.europa.eu/RegData/etudes/STUD/2021/694215/EPRS_STU(2021)694215_EN.pdf>