Executive Summary

Greece facing natural disasters

At the present juncture, Greece has been confronted with extreme natural phenomena, which, due to their unprecedented magnitude, will have significant economic consequences. The extent and time horizon over which the disasters, and in particular the floods in Thessaly, will affect GDP development cannot be estimated at this time. On the one hand, we do not know the initial economic footprint of the disasters and the time it will take to restore normality and productive activities to the affected areas. On the other hand, multiple domestic rehabilitation, support and solidarity mechanisms have been mobilised to assist the people affected and to repair the damage, and significant financial resources are to be made available from the European Union for the same purposes. Pending specific data on the above parameters, any assessment of the outlook for the Greek economy for the remainder of this year can only be based on the economic data currently available for the period before the disasters occurred.

The Greek economy remains on a growth path

Based on currently available data, the updated forecast of the Centre for Planning and Economic Research (KEPE) estimates the average annual rate of change of Greece's real Gross Domestic Product (GDP) for the year 2023 at 2.4% (see section 1.3), which is a slight upward revision of the corresponding previous forecast of KEPE (2.2%). While based on the latest available data incorporated in the above forecast, i.e., the data for the second quarter of 2023, the Greek economy remained firmly on track for satisfactory growth rates, and developments in key aggregates and indicators were mostly positive. The risks to the country's economic outlook are significant at the current juncture, not only because of the recent natural disasters, but also because of other factors related to the weak performance of the European economy and the economic downturn in the euro area. On the other hand, there are also several factors that can contribute to an improved outlook for Greece's GDP, such as the continued positive developments in the tourism sector, the use of the Recovery Fund and NSRF resources to strengthen productive investment, the strengthening of the resilience of the economy through the fulfilment of fiscal targets and the recent upgrade of Greek government bonds to investment grade by S&P.

Despite recent geopolitical developments, the stock market is performing impressively

The first eight months of 2023 ended with impressive returns for the Greek stock market since the beginning of the year, with increased market capitalisation and transaction value (see section 1.4).With the aim of containing inflation, the ongoing interest rate hikes by the ECB continue to put pressure on the bond market, affecting the yields of new issues and the cost of borrowing for the Greek government. A milestone for the Greek economy was the recovery of the investment grade, which is expected to have positive effects on businesses, households, the stock market and the government through lower borrowing costs, increased liquidity and the attraction of new investment capital.

Inflation is falling

Regarding price developments, the decline in energy prices since the beginning of the year, combined with the restrictive monetary policy, have led to a deceleration of inflation internationally. However, inflationary pressures remain strong with core inflation remaining high in most economies of the world. According to OECD analysts, the persistence of core inflation is due to higher production costs and high profit margins in several productive sectors. There is also a significant differentiation between the price inflation of material goods and services, with upward pressures on the prices of the latter remaining strong due to a higher share of labour costs in the total costs of service industries.

However, its long stay in the Greek economy seems to be due to 'greedflation'

The analysis we conducted at KEPE shows that during the period 2021-2022 and especially for the period 2022q1-2022q4, which is characterized by strong exogenous inflationary pressures mainly in the energy sector, *unit profits* increased their contribution to domestic price increases as reflected in the percentage increase in GDP deflator (section 1.2). Moreover, as we have seen, the drivers of the increase in unit profits (the gross operating surplus in the economy as a whole) were fuelled by increases in the (unit) net operating surplus of MFIs and unit gross income. These conditions provide evidence that firms *chose not to absorb the increases in energy costs by passing them on to product prices and, at the same time, boosted their net operating surplus*.

The results of the analysis add to a series of papers on other countries, the euro area and the USA. Various interpretations have been attributed to this phenomenon. Some firms may be increasing their prices to protect their profit margins. Given that in the initial phase of inflation there was excess demand, a price increase would not result in a loss of market share. According to another interpretation, some firms increase their profit margins in order to recover losses of previous years. Another possible reason lies in the attempt to create 'cushions' in an environment of high uncertainty. In a similar vein, some firms form expectations that inflation will continue and therefore discount increases in production costs by adjusting product prices accordingly. Finally, another interpretation focuses on 'seller inflation', i.e., the ability of some firms with a large market share to raise prices. In the current context, whatever the motivation behind the way in which firms set the prices of their products, this behaviour prolongs the monetary policy of high interest rates, risking a recession.

In any case, the challenge is to radically *tackle inflation and high price levels*. The government has from time to time announced various measures both to compensate for the losses in the living standards of citizens and to reduce the price of basic consumer goods. Indicative examples are the increases in the salaries and pensions of civil servants (but also in the minimum wage), the market pass, the compulsory shelf label for products with a 'permanent' price reduction of at least 5% for basic household products for a period of at least 6 months, the notification to the Ministry of Development of all price lists of super markets with a turnover of more than 90 million euros and the decisive strengthening of the control mechanisms.

Although useful, these measures are not enough to deliver a significant and lasting blow to inflation and increased price levels. This is probably because recent inflation is linked to business behaviour. Inevitably, the question arises whether competition in Greece is functioning effectively and fulfilling its task of self-regulation in a market often dominated by a small group of single digit players. In many respects, the concentration of an industry in the hands of a very small number of companies is not positive for consumers. The few, very large firms that form an oligopoly are more likely to set higher prices, earn higher margins and pay lower wages. In addition, consumers have fewer choices. For example, how easy is it today for a small firm with a new brand to enter the market, find a place in the distribution network, compete for consumer preferences and use its presence to drive competition? 'Greedflation' is fuelled by oligopolies, whose inherent characteristics include limited competition, barriers to entry, price rigidity and 'strategic' behaviour by their members to maintain higher prices and profits.

In this respect, effective measures to radically tackle inflation and high price levels in Greece are those that strengthen the functioning of competition. In the past (2012, 2014, 2016), strengthening the competitive functioning of markets was promoted through the OECD's "toolkit". The OECD Toolkit examined the competitive conditions in 13 sectors of the Greek economy that accounted for 30.7% of the country's gross value added and 35.2% of employment, from tourism to trade, food and specific manufacturing sectors. As a result, 2,312 laws and regulations were assessed, 1,276 of which were found to restrict competition, and 775 proposals were made. Is it time today to create a new 'Greek toolkit' by extending its application to other sectors of the economy where there are serious indications that competition is not working and healthy entrepreneurship is being hampered? KEPE and other research centres could contribute to such a national objective by studying and formulating proposals to enhance competition in individual sectors of the Greek economy.

The labour market is improving

In the first two quarters of 2023, the labour market picture improved further, according to the Labour Force Survey (section 3.1). The number of employed persons continued its upward trend and the number of unemployed persons decreased. Although the employment rate reached an all-time high, the number of people employed is still below the 2008 figure due to the decline in the population, an issue that may need to be brought into the labour market debate. The increase in employment seems to have mainly benefited women, young people and foreigners. Central Macedonia and Central Greece are the two regions with the largest increases in the number of people employed, while Western Greece also recorded a significant increase. The three sectors that have led the increase in employment over the last year are *transport and storage*, *human health and social work activities, and financial and insurance activities.* These are small sectors in terms of employment. Furthermore, part-time employment has declined both in absolute terms and as a share of total employment, while underemployment has also been significantly reduced over the last year. However, it continues to be primarily a 'women's issue'.

Wage employment, which accounts for almost two-thirds of the employed, continued its upward trend in the first seven months of 2023, while positive data include the reduction in the conversion of full-time contracts into flexible employment contracts, and especially the restriction of conversions to rotational employment without the employee's consent. Finally, the unemployment rate, although still higher for women and young people, is decreasing and the differences between groups are narrowing. The North and South Aegean Islands, Central Greece, Thessaly, West Macedonia and Central Macedonia show a consistent decline in unemployment. Recent legislative interventions are expected to affect the labour market. The direction of influence will depend on the size of the reaction they provoke and the degree of effectiveness of the control mechanisms.

Reducing economic inequalities as a priority

Addressing economic inequalities by promoting the level of productivity and inclusive growth in Greece remains a priority (section 3.2). In this direction, policy initiatives are faced with the double challenge of pursuing a wide range of policies that reduce inequalities and, at the same time, support productivity. Products of higher quality and complexity are essential. Among others:

- Measures focusing on improving access to training to acquire relevant skills are needed to boost productivity and potentially reduce inequalities.
- Labour market reforms should aim to promote fair and inclusive employment by strengthening a framework of continuous social dialogue between employers and workers to ensure that workers receive decent wages (key principle - 6 - of the European Pillar of Social Rights).
- Strong social protection is essential to provide adequate coverage of social security and the services necessary to promote social cohesion by targeting small business.
- As long as repayment conditions are met, facilitating access to affordable finance and supporting small-scale entrepreneurship should be priorities. Financial inclusion through specific programmes can enable small businesses to invest in new technologies and innovative techniques.
- Specific initiatives to facilitate technology transfer and partnerships with other firms, including abroad, can expand the network and create links to promote exports.

Professor PANAGIOTIS LIARGOVAS
Chairman of the Board and Scientific Director,
Centre of Planning and Economic Research (KEPE)