Commentary

Going to Nowhere...

By Elias Karavolias, 8/11/2012

Yesterday the Greek parliament approved the medium-term fiscal adjustment program(MFAP) which provides measures for the period 2013-2016 .These measures have a size of 18.9 billion of which approximately 9.4 billion euro will be taken in 2013, and the vast majority of them (6.1 billion) will be related to new pay cuts, pensions and welfare benefits. According to this program, in 2014 new measures of 4.9 billion have to be adopted for the years 2015-16.

As we have seen in the previous programs the assumptions are particularly optimistic about the stabilization of the Greek economy by 2016 (i.e talking about growth of 3.5% in 2016). Without explaining convincingly the results that will come from this fiscal adjustment, it is almost obvious that the new measures will hit violently the depressed Greek economy something that we are witnessing the last three years: collapse of expectations, deepening the crisis, expansion of uncertainty, increased depression in society.

According to data from this new MFAP and as a result of the ongoing fiscal adjustment, public consumption is projected to continue to decline until 2016 (-3.8% on average for the period 2013-2016), while private consumption is forecast to remain limited levels (from -7.0% in 2013 and -1.6% in 2014 to 1.3% in 2015 and 2.3% in 2016). It is difficult to justify the provision for private consumption growth in this period when we still apply the fiscal adjustment until 2016 that actually mean absorption of funds from income circuit.

Gross fixed capital formation is expected to recover gradually (an increase of 2014 and accelerating to 10.0% in 2016). It's a prediction that unfortunately is not based on any evidence. But the development of this size is more crucial for any future GDP growth. The contribution of the external sector to growth is expected to remain positive throughout the period of the medium term plan, with exports of goods and services to increase significantly (4.6% on average per year for the period 2013-2016) and imports to record decline in 2013 (-5.2%) and 2014 (-0.4%), but increased 2.6% on average over the years 2015-16.Even if we accept that this prediction is common knowledge, that it is so small the size of exports relative to the size of GDP is impossible to lift the burden of restarting the economy.

Employment is projected to decline by 2.1% in 2013, recovering gradually from 2014. The unemployment rate is projected to increase further in 2013 (23.7%), before starting to decline steadily to 17.9% in 2016. The labor market is expected to be favorably influenced by such structural reforms already implemented or planned, but also by wage moderation. We believe there are provisions that have nothing to do with reality. Unemployment will continue to rise throughout the period of MFAP and will even generate a state of collapse of the labor market.

The general government deficit is planned to amount to 7% of GDP in 2013, to 5.5% of GDP in 2014, to 3.8% of GDP in 2014, to 4.4% in 2015 and 3.2 % of GDP in 2016. For 2013, the medium-term targets to be zero primary surplus, while the budget tabled in Parliament just a little while earlier, provides primary surplus of 0.4% of GDP!

By taking additional measures, the public debt will reach 176% of GDP this year, at 189% of GDP in 2013, to 192% of GDP in 2014, 190 % of GDP in 2015 and to 185% of GDP in 2016. The Greek National Debt is not sustainable- even not manageable- and therefore requires a

new haircut, which is already widely discussed in the international markets. According the Greek Debt sustainability baseline scenario from the IMF Staff Report (March 2012) the 'target gap' is crucial for the effectiveness of the austerity measures.
Another failure must be noticed today, according to the MFAP: just 9.5 billion are the targeted revenues from privatization in the period 2013 - 2016, while a target of 50 billion is referred to be implemented after 2020.

All reported estimates and projections MFAP held under the shadow of extreme risks and uncertainties that are able to lead the program to complete failure. The crucial factors are:

- The degree of political uncertainty that dominates the political scene in the country would supply the macroeconomic uncertainty, with negative effects on production. Great as is the budgetary effort, the existence of a high degree of uncertainty and low confidence, combined with a fragile financial system, resulting in a deeper recession.

- A further deterioration of the crisis in the Eurozone, due to lack of or delayed approach, in a dynamic way, the debt crisis. This would send the wrong signals about the commitment for stronger integration and restructuring of the Eurozone, and create an environment for serious hazards in southern countries for potential social unrest or willingness to tolerate prolonged fiscal consolidation.

- The differences between the IMF's reports and the MFAP. The IMF admitted that the fiscal multipliers used (0.5) do not respond to current economic realities and that recent studies show a significant increase in fiscal multipliers in the post-crisis period, to a level of 0.9 to 1.7 .Which means that the calculations of macroeconomic scenarios made with old multipliers. Therefore there is a high probability of deviation for the actual macroeconomic performance of the economy for the period 2013-2016 in relation to the macroeconomic scenario.

- There are financial risks associated with the assumptions adopted for the projection of revenues and expenditures. This is a consequence of not reaching the targets for GDP growth. Additionally, it has been assumed unit elasticity of revenue, which may not be true, because of the complex calculations required. and the fact that the cyclical effects of the crisis period is very difficult to estimate as it includes the degree of tax compliance of citizens, the effect of broadening the tax base, the impact of structural changes in the revenue-raising mechanism and policy to combat tax evasion.

- The planned and expected supply liquidity to the real economy, in particular middle sized companies, through the payment of outstanding obligations of the State to the third and restarting lending by banks after the recapitalization, are expected to have a positive effect on financial stability production and create jobs. Providing liquidity is planned for three years). With no funding to start the economy if there are not corrected expectations, the problem will be almost terrified.

- Finally, despite the strong commitment of the Government for the timely and rigorous implementation of the program, the global economy and the international market conditions can be causes of delay in the execution of the MFAP. We strongly believe that the sustainability of debt is highly connected to the privatization program which is highly connected to the global investment environment and more specific to the eurozone crisis environment. We know that the target of the privatization revenues has already dropped to 9.5 billion from 50 billion by 2016...