cepAdhoc

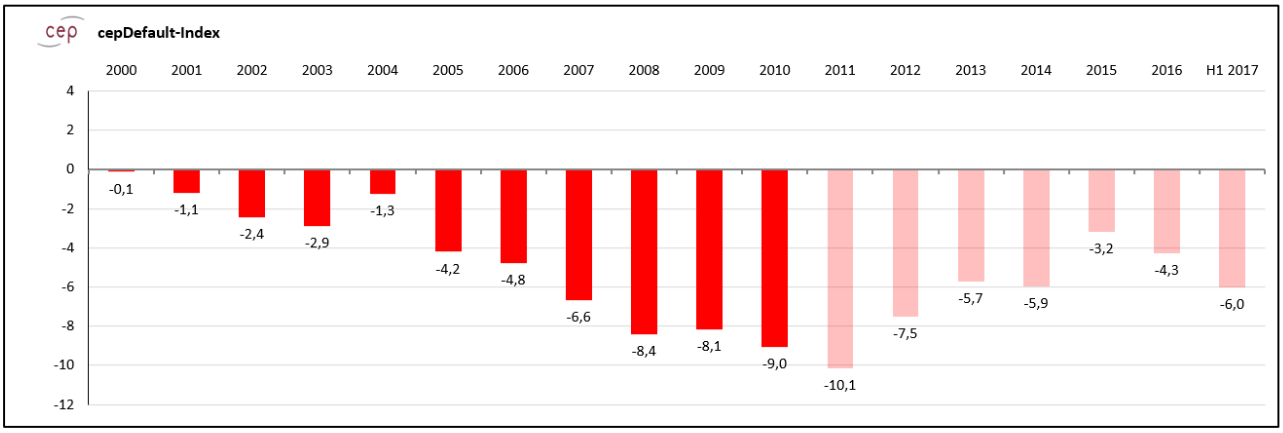
25-01-2018

cepDefault-Index Greece

Greece's Lack of Creditworthiness

Prof. Dr. Lüder Gerken, Dr. Matthias Kullas and Till Brombach

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	H1 2017
Risk category	3	3	3	4	4	4	4	4	4	4	4	4	4	4	4	4	4	4
I^c	6,5	6,9	5,8	7,0	6,0	3,8	5,4	6,8	5,8	3,4	0,6	-1,8	-5,1	-5,9	-5,8	-5,6	-5,2	-6,7
NTE	-6,6	-8,0	-8,2	-9,9	-7,3	-8,0	-10,2	-13,4	-14,2	-11,5	-9,6	-8,3	-2,4	0,2	-0,1	2,4	0,9	0,7
I^c + NTE	-0,1	-1,1	-2,4	-2,9	-1,3	-4,2	-4,8	-6,6	-8,4	-8,1	-9,0	-10,1	-7,5	-5,7	-5,9	-3,2	-4,3	-6,0



The third aid programme for Greece is due to expire in August. By then, at the latest, the Greek state should once again be able to fully refinance itself on the capital market. With this in mind, cep has been examining the trend in Greece's creditworthiness.

- Greece is still not creditworthy. The three rescue packages undertaken since 2010 have done nothing to change that. Greece will not manage without a fourth rescue package.
- This is firstly due to the fact that the country's capital stock has been continuously shrinking since 2011 and, in the first half of 2017, to an even greater extent than ever before. The country is becoming more and more impoverished.
- Another reason is the excessive consumption ratio which is by far the highest of all the EU states. At 112% of available income, it is significantly higher than the critical 100% threshold.

1 Layout and Informative Value of the cepDefault-Index

The cepDefault-Index measures the trend in creditworthiness for the overall economy – i.e. not only that of the state-sector. In addition to the state-sector, it also looks at credit behaviour in the financial sector and the credit behaviour of companies and consumers. The Index assesses (1) net lending or net borrowing of the total economy (NTE), reflecting the foreign credit needs of an economy, and (2) the resources used to increase the physical capital stock, i.e. capacity enhancing capital formation (C) over a certain period. The Index is formed from the sum of NTE and C; both values are indicated as a percentage of the gross domestic product (GDP): cepDefault-Index = NTE + C. [1]

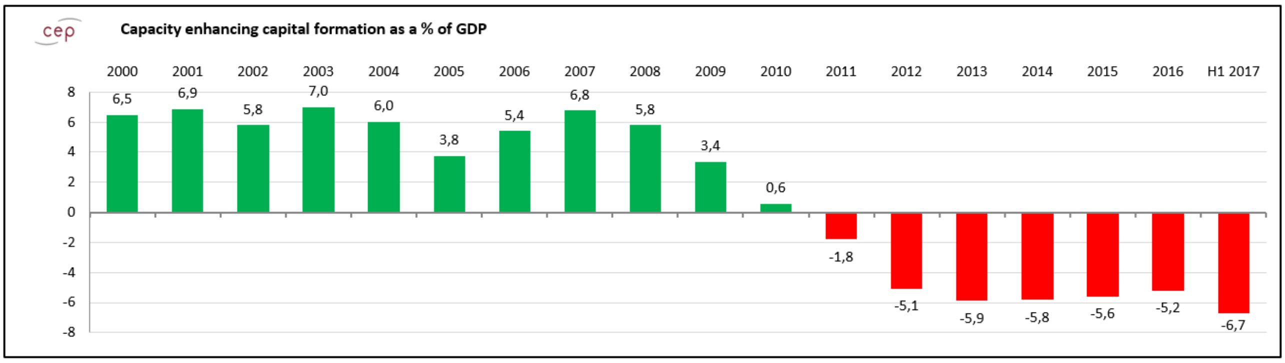
Risk Category 1 (green light) means: creditworthiness is increasing. Risk Category 2 (amber light) means: the trend in creditworthiness is unclear. Risk Category 3 (red-amber light) means: creditworthiness is declining. Risk Category 4 (red light) means: creditworthiness has been declining continuously for three or more years; the erosion of creditworthiness is not a temporary but a structural problem; the risk of a complete loss of creditworthiness has intensified or has actually occurred (Risk Category 4).

2 cepDefault-Index for Greece

Summary: Greece's creditworthiness continues to deteriorate. The financial aid, which began in 2010, has done nothing to change that. Greece is still not creditworthy.

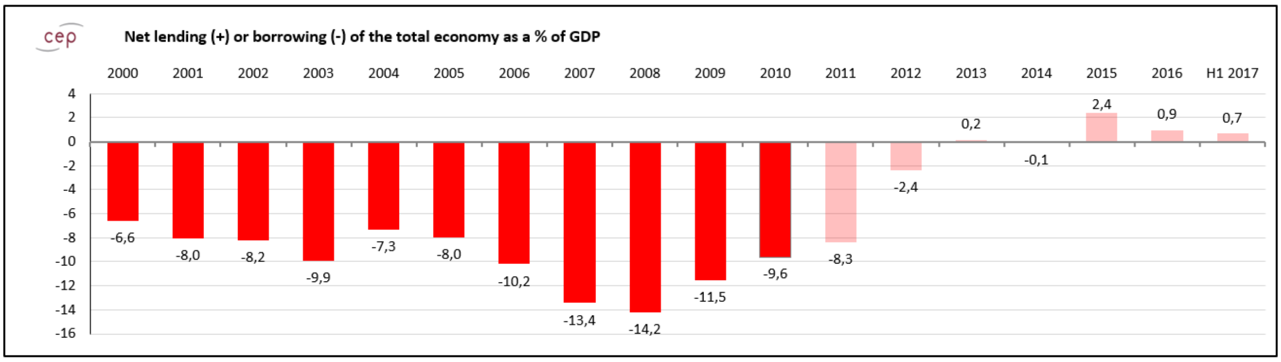
	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	H1 2017
Risk category	3	3	3	4	4	4	4	4	4	4	4	4	4	4	4	4	4	4
I^c	6,5	6,9	5,8	7,0	6,0	3,8	5,4	6,8	5,8	3,4	0,6	-1,8	-5,1	-5,9	-5,8	-5,6	-5,2	-6,7
NTE	-6,6	-8,0	-8,2	-9,9	-7,3	-8,0	-10,2	-13,4	-14,2	-11,5	-9,6	-8,3	-2,4	0,2	-0,1	2,4	0,9	0,7
I^c + NTE	-0,1	-1,1	-2,4	-2,9	-1,3	-4,2	-4,8	-6,6	-8,4	-8,1	-9,0	-10,1	-7,5	-5,7	-5,9	-3,2	-4,3	-6,0

Capacity Enhancing Capital Formation (C): Greek capital stock has now been falling for six and a half years. In the first half of 2017 alone, it fell by 6.7% of GDP. This is not only by far the highest level of all EU Member States but also the biggest fall yet measured in the country. The falling capital stock is due to a lack of both public and private investment, with the latter being the most significant factor.[2] All in all, this shows that the conditions for foreign and domestic investment in Greece remain unattractive.

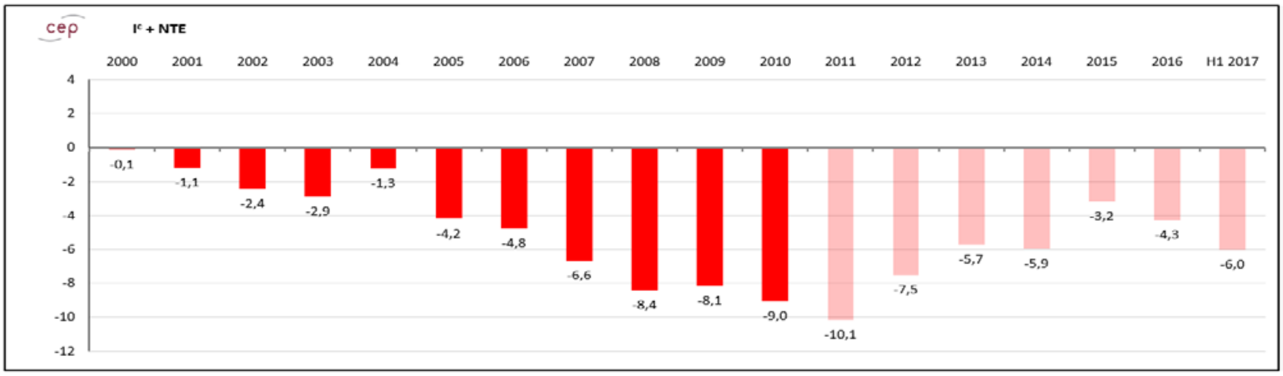


[1] For a detailed explanation see Gerken/Kullas/Brombach (2017): cepDefault-Index, Section 2.
[2] Cf. European Commission database, Ameco, online at: http://ec.europa.eu/economy_finance/ameco/user/serie/SelectSerie.cfm, accessed on 12.01.2018.

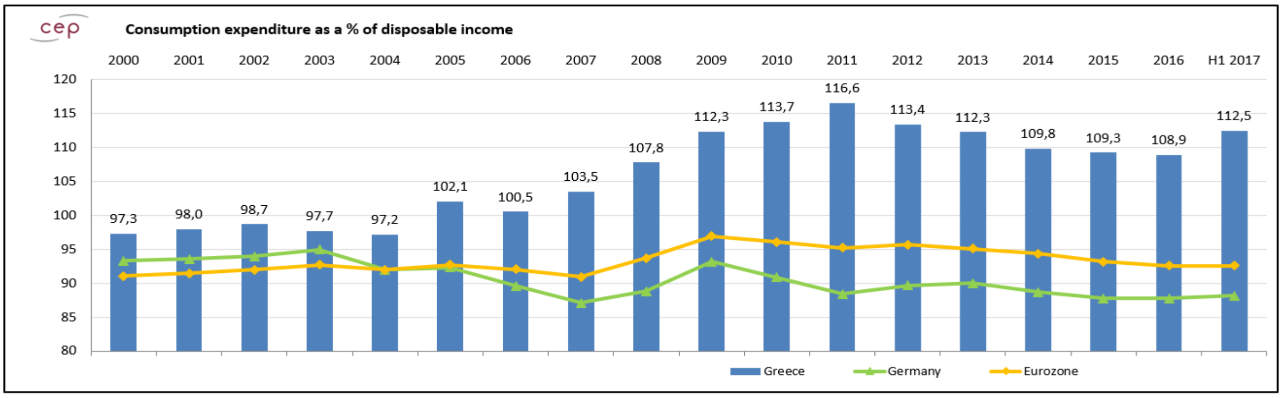
Net lending or net borrowing of the total economy (NTE): On balance, between 2000 and 2012, Greece incurred foreign debt every year although Greek net borrowings have fallen continuously since 2009. In the last two and a half years, Greece even became a net capital exporter. This capital export is problematic, however, because at the same time Greece's capital stock has diminished. Thus the capital export is not a sign of an internationally competitive economy but of capital flight. By comparison with the previous two years, though, its level has dropped.



C + NTE: The sum of C and NTE is negative for the entire reference period. To begin with, this was caused by massive borrowings. Since 2012, this situation has been due, in particular, to the fall in capital stock.



Consumption ratio: Since as long ago as 2005, the Greek consumption ratio has invariably exceeded the critical threshold of 100% of available income. The first half of 2017 saw a further significant increase to 112.5%. This value is not only significantly above the eurozone average of 92.6% but is by far the highest of all EU Member States.



Cause: Greece's lack of creditworthiness is firstly due to the fact that the country's capital stock has been falling since 2011. This is clearly indicated by the fact that Greece remains unattractive to international investors. Unless this changes, Greece will not regain its creditworthiness. The cause is, firstly the propensity of the Greek population and the Greek government to consume.

Recommended action: In order for Greece to regain its creditworthiness, the country must become more attractive to domestic and foreign investors. For this reason, investment conditions must be improved. The condition for the latter is a reduction in the consumption rate below 100% of available income so as to free up funds for investment. Public spending, in particular, must be used more for investment purposes.

Above all, the country must implement reforms and must believe in those reforms. The best medicine in the world will not help if the patient believes the doctor is trying to poison him.