Centrum für
Europäische Politik

CEP Default Index

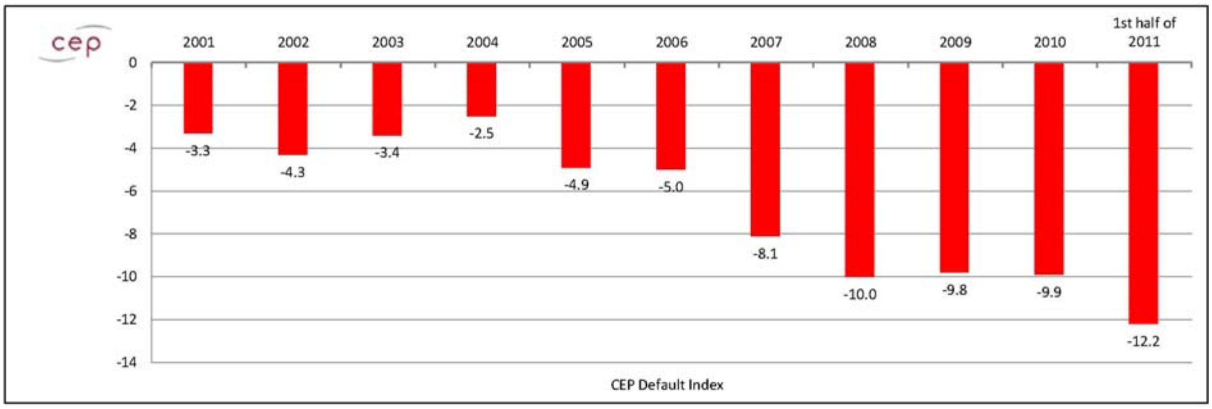
Country Report Greece – 1st half of 2011

Creditworthiness Trends, Causes and Reform Prospects

– Abstract[1] –

Prof. Dr. Lüder Gerken Dr. Matthias Kullas Dr. Jan S. Voßwinkel

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	1st Half of 2011
NTE	-10.2	-11.7	-10.7	-9.0	-9.5	-10.8	-14.7	-16.2	-13.3	-10.6	-9.0
I^C	6.9	7.4	7.3	6.5	4.6	5.8	6.6	6.2	3.5	0.7	-3.2
CEP Default Index	**-3.3**	**-4.3**	**-3.4**	**-2.5**	**-4.9**	**-5.0**	**-8.1**	**-10.0**	**-9.8**	**-9.9**	**-12.2**
Risk category	3	3	4	4	4	4	4	4	4	4	4



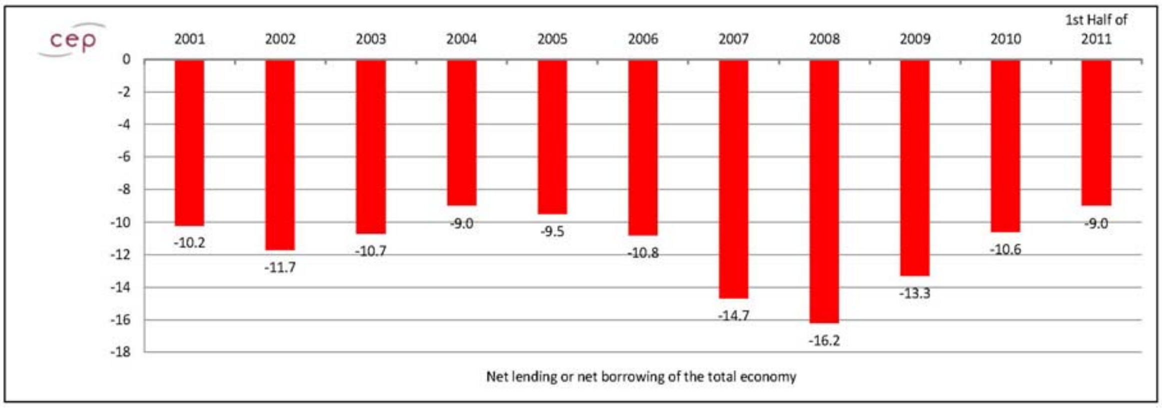
[1] The long version can be found under http://www.cep.eu/fileadmin/user_upload/CEP-Default-Index/Griechenland_2011.pdf.

The CEP Default Index[2]

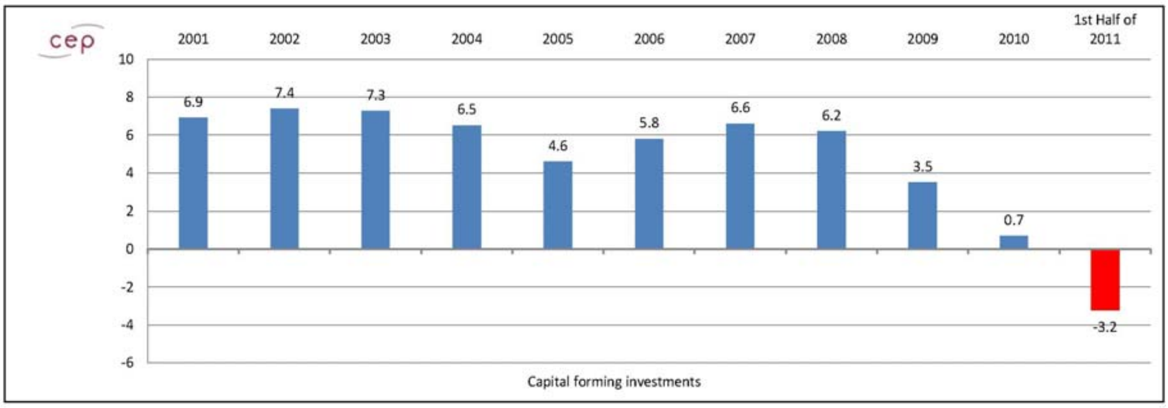
The CEP Default Index measures the development of an individual countries' capability to pay back foreign credits. The Index assesses the net lending or net borrowing of the total economy (NTE) and the resources used to increase physical capital stock, that is capacity forming investments (I^c) for a certain period. Both values are measured as a percentage of gross domestic product (GDP). Negative index values indicate an erosion of creditworthiness.

CEP Default Index for Greece: Findings

- The creditworthiness of the Greek economy has decreased every year since 2001 (see front page). Since 2007, this trend has intensified dramatically. In the first half of 2011 the CEP Default Index dropped significantly to a new low of –12.2. This negative trend is set to continue; Greece is not creditworthy.
- The key causes of this trend are:
  - In the first half of 2011, at 9.0% of GDP the net credit demand for additional foreign credits was slightly lower than in 2010.



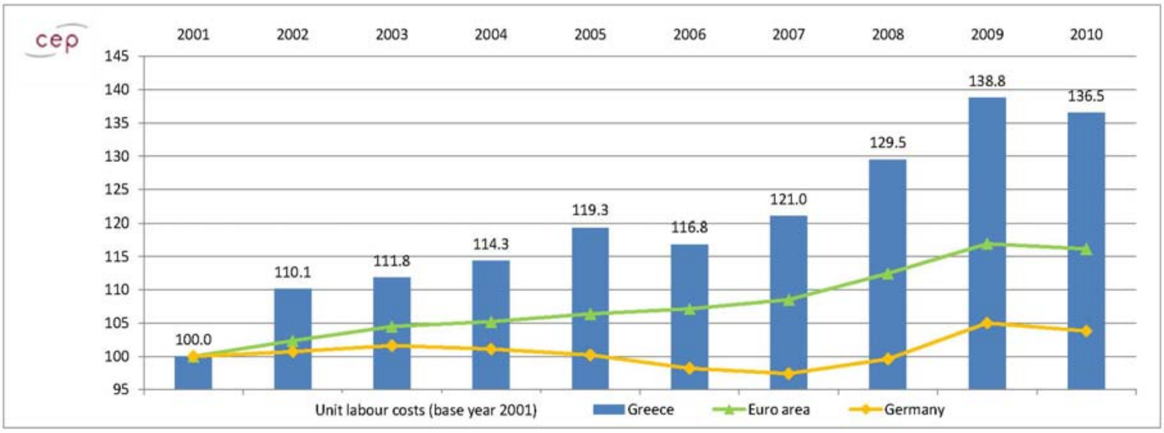
  - In the first half year the Greek economy de-invested significantly: capital stock shrank by 3.2% of GDP.



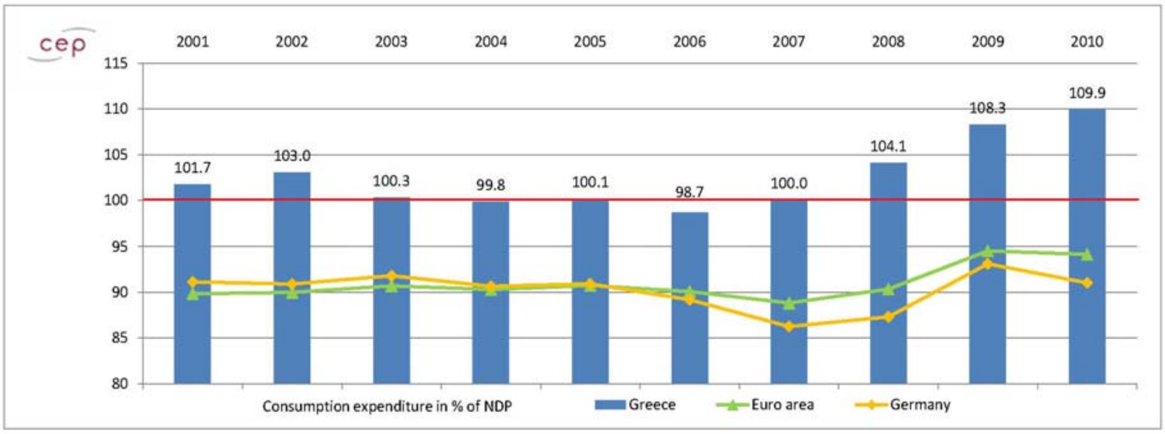
[2] For a detailed presentation, see cepAnalysis "CEP Default Index" under http://www.cep.eu/en/analyses-of-eu-policy/economic-stability-policy/cep-default-index.

Causes of Greece's Credit Unworthiness

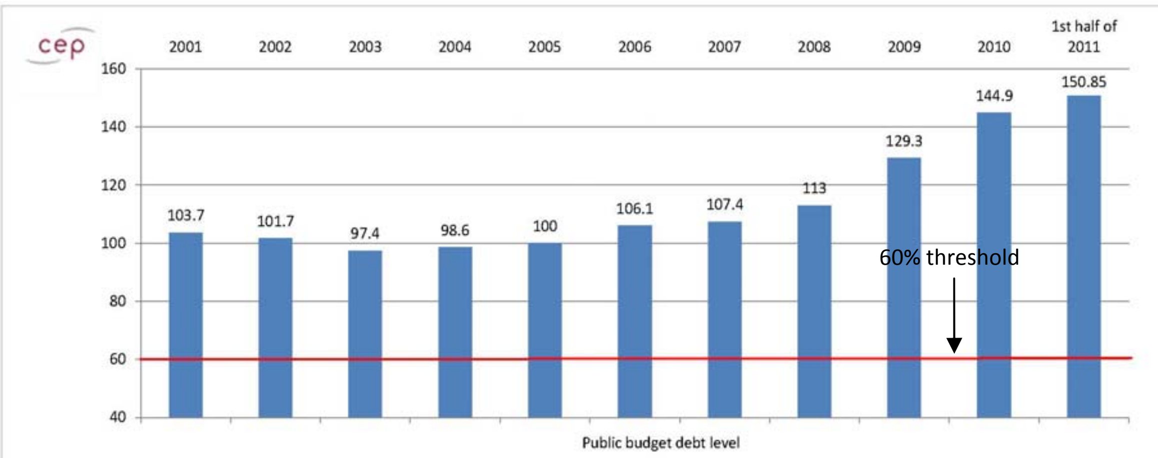
- The main cause is that Greece has lost its competitiveness against other Euro countries: Greece's unit labour costs have increased by 36.5% since 2001, German's by 4%. The difference of 32.5 percentage points indicates a gap in competition.



- This is exacerbated by the high propensity of the Greek population to consume: since joining the monetary union, they have consumed almost every year more than 100% of net domestic product (NDP). In the first half of 2011 the consumption rate of 110% even exceeded that of Italy, Portugal and Spain. In other words, the country with the biggest problems lives most beyond its means.

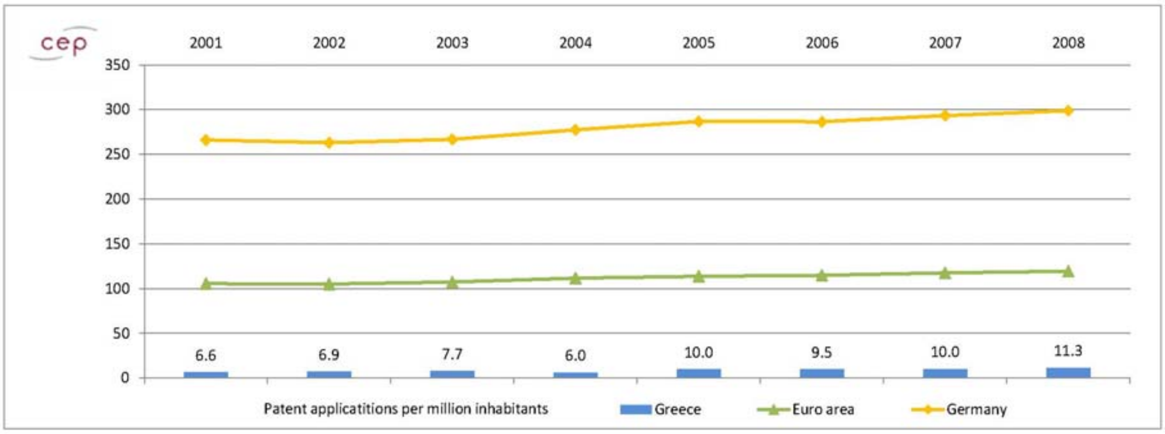


- Moreover, in the first half of 2011 alone, the state debt level grew by 6 percentage points from 145% to 151% of GDP.



Reform Prospects

- It is quite impossible that as of 2015 Greece will be able to get by without the financial support of other states, as specified in the second aid package.
- In particular, the Greek economy will not be able to restore its competitiveness, not even in the medium term, which would be a precondition for the elimination of current account deficits and in turn for foreign net credit needs.
- For productivity in Greece will almost certainly not increase faster than for instance in Germany. In fact, the opposite is likely, as currently the country has a negative investment rate. Moreover, the country has no modern research and innovation culture. For instance, the number of Greek patents registered with the European Patent Office is less than a twenty-fifth of those registered by Germany.



- Hence, competitiveness can be restored in the short term only through a drastic cut in workers' salaries. However, this will be extremely difficult to enforce in view of the people's resistance to the already existing reform measures. This is further aggravated by the factor that the state's impact on the wage formation process is limited in a private economy.
- The planned and the already adopted measures to make the labour market more flexible and to liberalise the goods market as well as the reforms of the pension scheme will not suffice to compensate for the aforementioned deficits.
- There is no sign of a substantial cut in consumption expenditure, which is urgently needed in order to reduce foreign credit demands and to release funds for investments.
- Greece will not be able to remain a member of the Eurozone without an institutionalised system of transfer payments providing a permanent transfer union.