

Atradius Country Report

Greece – April 2014



Greece: Atradius STAR Political Risk Rating*:

7 (Impaired) – Positive

* The STAR rating runs on a scale from 1 to 10, where 1 represents the lowest risk and 10 the highest risk.

The 10 rating steps are aggregated into five broad categories to facilitate their interpretation in terms of credit quality. Starting from the most benign part of the quality spectrum, these categories range from 'High Quality', 'Good', 'Adequate', 'Impaired' to 'Prohibitive Conditions', with a separate grade reserved for 'Off Cover.'

In addition to the 10-point scale, there are rating modifiers associated with each scale step: 'Positive', 'Stable', and 'Negative'. These rating modifiers allow further granularity and differentiate more finely between countries in terms of risk.

For further information about the Atradius STAR rating, please [click here](#):

Overview

General information

Capital:	Athens
Government type:	Parliamentary democracy
Currency:	Euro (EUR)
Population:	11.3 million

Most important sectors (2012, % of GDP)

Services:	80%
Industry:	16%
Agriculture:	4%

Main import sources (2012, % of total)

Russia:	12.6 %
Germany:	9.3 %
Italy:	7.7 %
Saudi-Arabia:	5.6 %
China:	4.8 %

Main export markets (2012, % of total)

Turkey:	11.7
Italy:	8.1 %
Germany:	6.7 %
Bulgaria:	5.9 %
Cyprus:	5.2 %

Key indicators

	2011	2012	2013	2014*	2015*
Real GDP growth (y-on-y, % change)	-7.1	-7.0	-3.8	-0.2	1.7
Consumer price index (%)	3.3	1.5	-0.9	-0.4	1.0
Real private consumption (y-on-y, % change)	-7.7	-9.3	-6.0	-0.6	0.6
Retail sales (y-on-y, % change)	-10.2	-12.3	-7.7	-0.1	0.3
Industrial production (y-on-y, % change)	-7.8	-3.4	-3.6	1.2	2.5
Unemployment rate (%)	17.7	24.3	27.1	27.3	27.1
Gross fixed capital investments (y-on-y, % change)	-19.6	-19.2	-12.8	-2.8	3.2
Real net exports (EUR billion)	-15.3	-7.6	-3.6	-1.6	-0.2
Fiscal balance (% of GDP)	-9.5	-9.0	-2.5	-2.4	-2.0
Government debt (% of GDP)	170.3	156.9	175.5	174.7	170.4

*forecast

Source: IHS Global Insight

Economic situation: still troubled despite signs of improvement

Debt reduction deal has lessened the likelihood of a Eurozone exit

In November 2012 the Eurozone member states agreed to a number of measures to reduce the Greek government's debt burden, which was seen as unsustainable. A European Financial Stability Facility (EFSF) loan was made available - and accepted - to repurchase EUR 61.8 billion nominal government debt at a price of 33.8%. The interest on EUR 53 billion of EU/ECB/IMF loans was reduced to 0.5% from 1.5%, and Eurosystem profits of around EUR 9.3 billion on Greek government bonds, bought at deep discounts and repaid at par, are scheduled to be remitted to Greece. These measures are intended to lower government debt to 120% of GDP by 2020. This has sent a strong signal of the political will to keep the Eurozone together, further lowering the probability of a Greek exit.

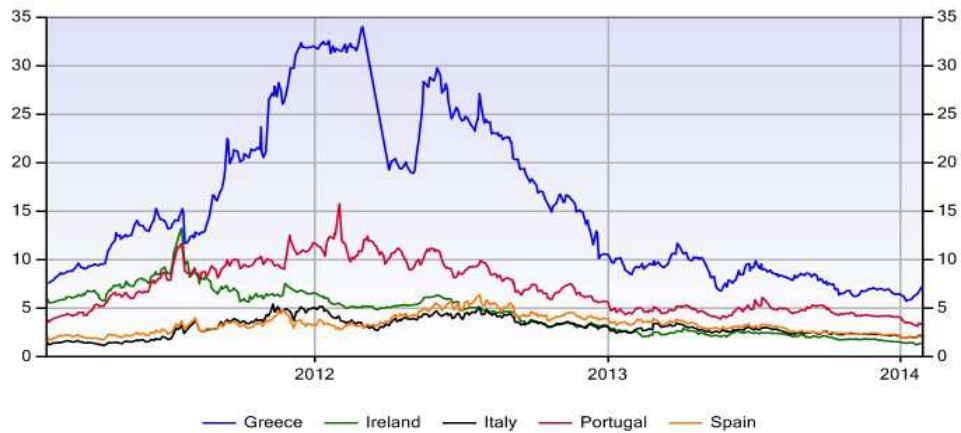
An improvement in financial market confidence

Following the June 2012 election and the resolve shown by Eurozone members in November that year, Greece's yield spread over the German bund followed a decreasing trend, which continued in 2013 (see chart overleaf), reaching less than 7% by end of March 2014: a fall of more than 25% since early 2012.

Additional proof of improved market confidence is provided by the rebound of the Greek stock market, which has increased by more than 20% since June 2013 as Greek assets win investors back. The corporate bond market was also fairly active, with 15 companies issuing bonds worth a total of EUR 4 billion in 2013. Among the issuers were local groups such as Hellenic Petroleum and OTE (telecom).

Long bond yield divergence within the Eurozone

(10-year government bond yield spreads over the German Bund)



Source: IHS Global Insight

Current sovereign risk ratings

	March 2014		February 2013	
S&P	B-	Stable	CCC	Stable
Fitch	B-	Stable	CCC	Negative
Moody's	Caa3	Stable	B-	Stable

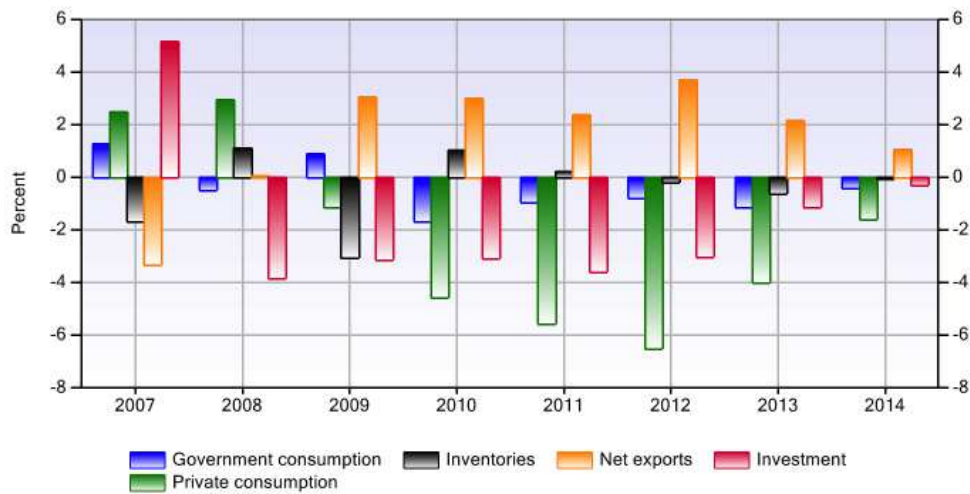
Lower GDP contraction in 2013 than expected a year ago

Greek GDP is expected to have contracted 3.8% in 2013, better than the 5% fall expected a year ago. The reasons are the rise in tourism and less of a dip in internal demand, helped by a stabilising of household incomes and lower consumer prices. Additionally net exports benefited from improved competitiveness, contributing positively to GDP last year (see chart overleaf). Compared to 2010, unit labour costs decreased by 20% in the business sector and 33% in the public sector, helped by wage reforms stipulated in the IMF programme. Exports of goods increased 3.3% year-on-year between January and November 2013 while imports declined 5.4%.

However, the government sector still contributed negatively to GDP, as fiscal consolidation still weighed on the outcome. Similarly, the investment contribution was still negative, though there is an improving trend.

Contribution to GDP growth: Greece

(Chain-weighted basis; forecast data edge 2009)



Source: IHS Global Insight

Unemployment improved slightly in Q2 of 2013 (27.1%) and Q3 (27.0), but grew to 27.5% in Q4. The youth unemployment rate (i.e. for those aged 15-24 years) is still high at 57%.

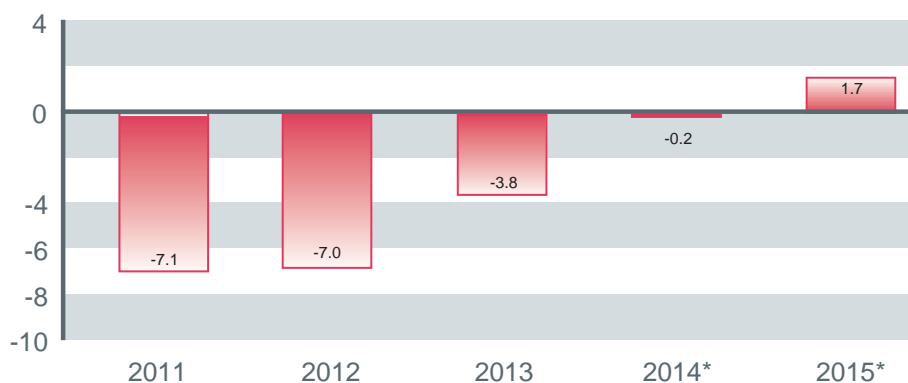
Economic growth expected to return in 2015

The forecast for 2014 shows progress in the economic rebound, with GDP expected to contract only 0.2%, compared to the 2% forecast of a year ago. Tourism revenues are expected to reach a new plateau, with 18.5 million arrivals compared to 12.6 million in 2013. While fiscal consolidation slowly fades, exports are expected to grow by 2.4% as global demand strengthens.

The outlook for 2015 is for positive GDP growth of 1.7%, sustained by an increase in private consumption, industrial production and investments.

GDP growth

(% change on previous year)



*forecast

Source: IHS Global Insight

Consumer price deflation in 2013 and 2014

In 2013 consumer prices contracted 0.9% due to partial product and service market reforms. This deflation is expected to continue in 2014 (down 0.4%). Last year, Greek consumer prices were well below the Eurozone average (see chart below) reflecting extremely weak demand and lower wages in both the public and private sectors.



Source: IHS Global
Insight

Vulnerability in the banking system has been addressed

The four major Greek banks have been recapitalised, costing the Hellenic Stabilisation Fund EUR 38.4 billion of the EUR 50 billion available, but non-performing loans are still increasing. Banks' profitability is improving, and though it is still substantial: EUR 70 billion at the end of 2013, dependence on funding by the European Central Bank is gradually decreasing. Private sector bank lending to both business and consumers decreased 4% in 2013, while loans to businesses alone declined 4.9%.

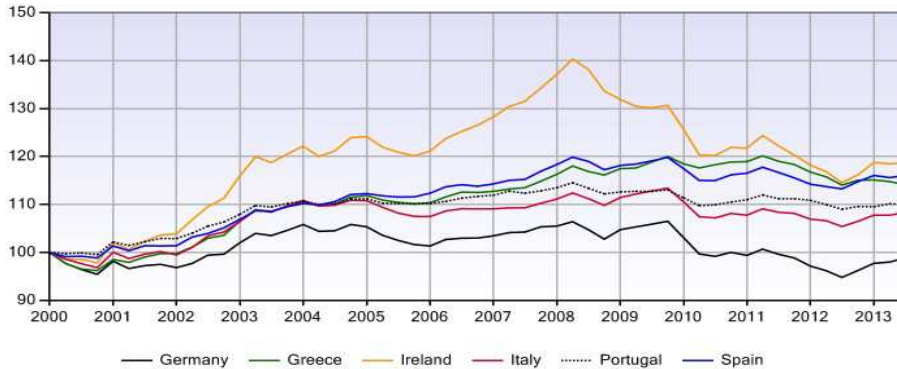
In early March the Greek Central Bank estimated that the country's main banks require an additional EUR 6.4 billion in capital. However, the troika has stated that banks may need more capital in the event that the authorities and banks do not address the high level of non-performing loans urgently and efficiently.

International competitiveness has improved...

The improvement in Greece's competitiveness, already evident in 2012, continued in 2013. Greece's Real Effective Exchange Rate (REER), which measures its international competitiveness as costs and prices change, has improved compared to other countries (see chart below), due mainly to lower wages and prices.

Real Effective Exchange Rate (REER)

(Trade weighted currency baskets adjusted for relative inflation, Index January 2000 = 100)



Sources: IHS Global Insight; IMF.

The REER, deflated by wage costs, shows that by Q2 of 2013 Greece had recovered the competitiveness it had lost between 2000 and 2009.

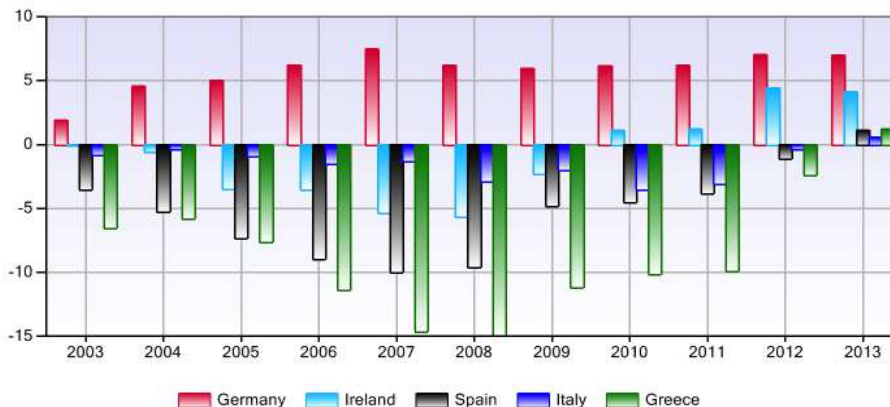
... with another current account surplus expected this year

The rebalancing of the economy continued last year, as Greece's current account benefited from its improved competitiveness and decreasing imports due to lower internal demand, while there was a significant rise in net EU transfers. This resulted in a current account surplus in 2013 (1.2% of GDP) after years of deficits. Foreign direct investment (FDI) remained subdued, although Greece has advanced on the World Bank's Ease of Doing Business index and other indices. However, portfolio investment has surged as the danger of a Eurozone exit has been fading: EUR 3 billion of corporate bonds were issued in 2013.

With internal demand likely to remain subdued in 2014 and export growth expected to accelerate to 2.4% due to Greece's improved competitiveness, the current account is expected to continue to improve: to a surplus of 2.2% of GDP this year.

Current account balance

(Current account balance as percentage of GDP)



Sources: IHS Global Insight; National Statistics offices.

Improved fiscal performance, but government debt still rising

Efforts to reduce Greece's budget deficit have been fairly successful: from 15.7 % of GDP in 2009 to an expected 2.5 % of GDP in 2013 - within the Maastricht criteria. The primary budget (government net lending excluding interest payments on debts) recorded a slight deficit of 0.1% of GDP in 2013. This was due largely to lower government investment, as the budget outlays were up just 1% against the planned 10 %, while other spending and tax receipts went broadly to plan. Indeed, there is some evidence that tax compliance is beginning to improve.

In 2014 the aim is to achieve a primary budget surplus of 1.1 % of GDP, while the budget deficit is forecast to decrease to 2.4 % of GDP. To do so, a number of austerity measures worth 2.3 % of GDP (EUR 4 billion) have been approved. However, estimates by the troika indicate that additional measures worth EUR 2-2.5 billion would be required, while the Greek government insists that, due to the 2013 over-performance, this additional figure is only EUR 1-1.5 billion and will be met by reductions in social spending. However, the troika wants to see that actions agreed in the IMF programme, such as tax cuts and social security reductions to be paid by employers, are followed through and that structural reforms are progressed more vigorously.

Is more debt relief on the horizon?

The IMF has identified a EUR 11 billion funding requirement for Greece in 2014-2015. There are a number of options to address this, including stretching the ECB credit opportunities, government deposits (EUR 17 billion) and currently unused funds in the Hellenic Financial Stabilisation Fund (EUR 10 billion). However none of these is straightforward and therefore this major issue remains to be resolved.

Despite the relatively good news concerning the budget deficit reduction, government debt increased to 176 % of GDP in 2013 and is not expected to begin to fall until 2015 at the earliest (and then only to a forecast 170 % of GDP). The government debt targets set by Greece and its Eurozone peers for 2020 (120 % of GDP) and 2022 (110 % of GDP) are not realistic without more debt relief, especially as, between now and 2020, there are a number of downside risks: for instance, that the projected economic growth averaging 3 % from 2015 to 2020 will not materialise. However, a decision on further debt relief for Greece would be highly politically sensitive in some Eurozone countries

Further reform is essential – despite strong resistance

Greece still lags well behind the average EU best practice in creating free and undistorted competition, as its product and service (regulated professions) liberalisation was put on hold during the 2012 election period. The privatisation programme stalled completely and performed below expectations in 2013, with preparations for asset sales taking far more time than anticipated. Questions remain as to the political will to implement the programme, not least as three chairmen of the privatisation programme have left since mid-2012.

Tax collection reforms and measures to combat tax evasion are still behind schedule. Political and public resistance to reforms remains strong and social tensions will limit the government's room to manoeuvre, especially as an economic rebound is not expected before 2015.

This means that Greece will continue to struggle to meet the reform/liberalisation and fiscal targets set by the EU/ECB/IMF troika, which are a precondition for the release of additional tranches under the bail-out agreement.

Business insolvency increase expected to moderate

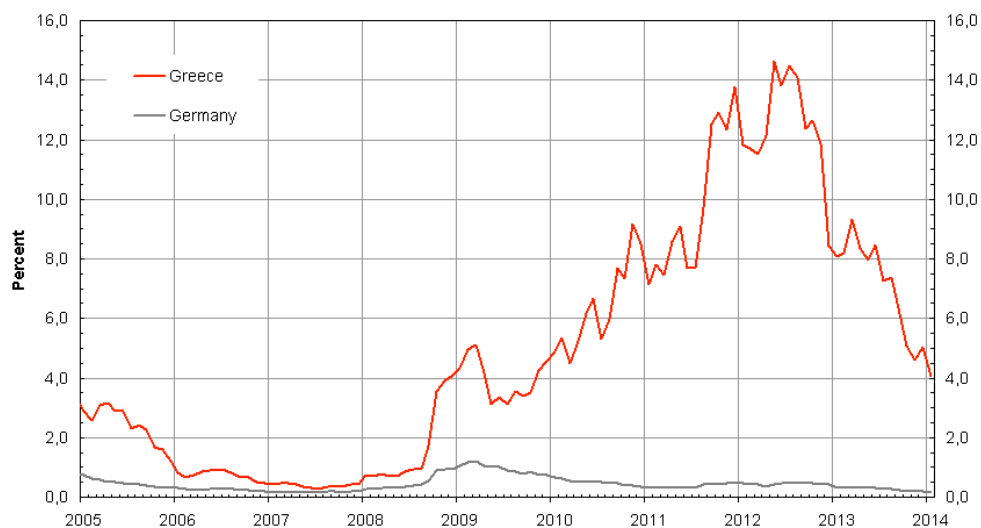
Greek business insolvencies recorded sharp year-on-year increases of 30 % and more in 2008-2012. However, since 2012 (up 30 %) there seems to be a decreasing trend at last. After a 10 % increase in 2013 we expect business failure to increase 5 % in 2014.

Expected default frequency for Greek listed businesses: decreasing but still very high

The monthly median expected default frequency (EDF) for Greek listed companies rose sharply in the second half of 2011. There was a slight improvement in early 2012, but growing political uncertainty before and in the wake of the May and June 2012 general elections and heightened fears of a Greek Eurozone exit took their toll. The EDF subsequently increased to unprecedented levels reaching 14.48 % in July 2012.

Since then, Greece's EDF has improved, with January 2014's figure down more than 1,000 basis points to 4.07%. This improvement reflects the debt reduction deal agreed with Eurozone members, which has lessened the likelihood of a Greek Eurozone exit, and also the better than expected economic performance in 2013. However, the EDF remains very high, so that listed companies in Greece are still facing a comparatively high default risk (see chart below).

Median EDF evolution by country*



Source: KMV Credit Monitor and Atradius Economic Research

*The Expected Default Frequency (EDF) chart above is based on listed companies in the markets referred to, and the likelihood of default across all sectors within the next year. In this context, default is defined as a failure to make a scheduled payment, or the initiation of bankruptcy proceedings. Probability of default is calculated from three factors: market value of a company's assets, its volatility and its current capital structure. As a guide, the probability of one firm in a hundred defaulting on payment is shown as 1%.

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Atradius Credit Insurance N.V.

Postbus 8982
1006 JD Amsterdam
David Ricardostraat 1
1066 JS
Amsterdam m