

Greece Business Forecast Report Q3 2014

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Date: June 2014

Pages: 45

Price: US\$ 1,195.00 (Single User License)

ID: G68CBBD48ABEN

Abstracts

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Core Views

We expect a return to positive economic growth in 2014 following six years of depression. Thereafter we expect growth to remain well below the pre-crisis range.

Underpinning positive economic growth will be a stabilisation in domestic demand as well as a positive contribution from the current account. The prospect of further spending cuts and tax hikes will ensure that demonstrations and national strikes remain a key feature of the political landscape over the medium term.

Major Forecast Changes There are no **Major Forecast Changes** this quarter.

Contents

CHAPTER 1: POLITICAL OUTLOOK

SWOT Analysis

BMI Political Risk Ratings

Domestic Politics

Additional Debt Restructuring Still On The Cards

With Greece now running a primary budget surplus a year earlier than expected, another round of debt restructuring is on the cards.

We stress, however, that the presence of a funding gap in 2014 and 2015 in the headline fiscal data could reduce the government's bargaining power with its international creditors. Moreover, we would expect some form of soft restructuring such as maturity extensions or reductions in interest costs in the first instance, before outright debt forgiveness is eventually pursued.

Table: Political Overview

Long-Term Political Outlook

A Decade Of Austerity And Instability

Greece's political landscape is likely to become more tumultuous in the coming years.

The legacy of fiscal profligacy and economic distortions will leave an indelible mark on the Greek economy and society, with political voices potentially becoming more fragmented.

We therefore expect a prolonged bout of austerity and instability in the decade ahead.

CHAPTER 2: ECONOMIC OUTLOOK

SWOT Analysis

BMI Economic Risk Ratings

Economic Activity I

Return To Growth In 2014 Key For Investor Sentiment

The Greek economy is set to return to positive growth in 2014, aided by a stabilisation in household expenditure and an improving trade balance. Despite paying a high cost for economic adjustment during the last six years of depression, the economy will not be returning to the sort of growth rates enjoyed during the pre-crisis years. Instead, the loss of productive capacity, an impaired labour market and still lack of cost competitiveness will translate into a very weak longer-term potential growth rate.

Table: ECONOMIC ACTIVITY

Balance Of Payments

Strong Euro Risks Eroding Export Gains

Having gone through a difficult multi-year correction, Greece's current account has returned to surplus. We expect a further surplus in 2014, with the current account being close to balance over the medium term. We continue to stress that given that this has been predicated more on a collapse in imports than a marked improvement in foreign market export share, Greece's longer-term growth potential remains weak. Furthermore, the lingering strength of the euro threatens to undermine the progress that has been made in recent years to improve cost competitiveness.

Table: CURRENT ACCOUNT

Debt Policy

Demand For Greek Bonds Masks Credit Risk

Greece's first sovereign debt issue since entering its first bailout programme has attracted substantial interest from investors hunting for yield in an environment in which developed market policy rates are still at record lows. Despite the enthusiasm for the issue, we warn that the longer term outlook for Greek sovereign debt remains precarious, with additional restructuring involving the official sector likely in the coming years.

Economic Activity II

Deflation Persists

Consumer price deflation continues to run its course in Greece, underpinned by still weak domestic demand, insufficient credit supply and a strong euro. We expect deflation to continue through 2014 before edging back into inflation territory the following year as the economy gradually returns to positive growth.

Banking Sector

Banking Sector: Further Deleveraging Ahead

The Greek banking sector is still stuck in deleveraging mode and is likely to record another year of asset contraction in 2014. Our core forecasts see a return to positive asset growth in 2015 alongside the economy's emergence from its six-year depression. However, there are significant risks to this forecast, not least the European Central Bank's Asset Quality Review which could deter banks from taking on more risk in the form of lending to the private sector.

CHAPTER 3: 10-YEAR FORECAST

The Greek Economy To 2023

Lower Growth Path To Emerge Over The Long Term

With international credit conditions unlikely to return to pre-2008 levels over the foreseeable future, we expect both consumer and investment spending to be more subdued over the longer term, anchoring the Greek economy onto a lower growth path than that seen leading up to the global credit crisis. Moreover, while trade rebalancing has closed the current account gap, the adjustment process has been driven more import compression rather than substantial competitiveness gains in the export sector, which suggests that Greece's longer-term growth trajectory will be adversely affected.

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