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GREECE FOCUS NOTES

Midyear Review: an update on 2022 GDP growth forecasts

	2021, € bn	Shares in 2021 GDP (real)	2022 %YoY Real growth	2022 %YoY Real growth
			Baseline Scenario	Adverse Scenario
Private Consumption	125.7	69.7%	0.0%	-1.3%
Gov. Consumption	38.9	20.8%	0.5%	2.5%
Total Consumption	164.7	90.6%	0.1%	-0.4%
Gross Capital Formation	32.6	15.0%	7.4%	5.0%
Domestic demand	197.3	105.6%	1.0%	0.3%
Imports	88.8	42.3%	7.5%	10.8%
Exports	74.3	37.0%	13.4%	15.2%
GDP	**182.8**		**3.0%**	**1.4%**
HICP	0.6%		7.0%	8.2%
Unemployment Rate (% of l. f.)	14.7%		12.6%	13.6%

Source: ELSTAT, Eurobank Research

1. Overview

The Greek economy, after a quick recovery in 2021, which allowed to reclaim the bulk of pandemic-induced losses, had entered 2022 with leading indicators signaling prospects for dynamic growth: production in many manufacturing sectors and sales in retail trade were above pre-pandemic levels, economic sentiment was in multi-year highs and unemployment was falling. Then, the war in Ukraine erupted. This new crisis, as in the entire European economy, negatively affects short- and medium-term prospects in comparison to previous forecasts. It will likely cause a deceleration of growth in the short term and an increase in inflation, yet it will not overturn realization of the Greek economy's potential in the longer term. The size of the impact will depend on a multitude of factors, including the duration of the war, final mix and duration of EU sanctions and monetary and fiscal policy measures. The direct impact of the crisis will be limited as

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3 Ιουνίου 2022

trade, tourism and financial links with Russia and Ukraine are relatively small: exports of goods & services to Russia and Ukraine combined comprised in 2019 ca 2.1% of total, (same share for tourism revenue) and no Greek bank has a notable presence in these countries. Yet, there are notable channels of indirect impact, including (a) the disturbance caused by the war on supply chains, external demand and world trade routes, (b) the supply side shock from energy prices' increases: Greece has an exposure on Russian imports on its energy mix as 73% of its imported oil and 39% of natural gas in 2020 was coming from Russia. Although there are alternative sources to substitute Russian imports, so that energy security is not at risk, increases in energy prices are feeding into prices of goods and services. This exacerbates inflationary pressures, which were already elevated before the war as a result of ultra-accommodative monetary and fiscal policies in the aftermath of the pandemic, the opening of economies after the lockdowns and disturbances in supply chains. Inflation, in turn, erodes disposable incomes, and exercises pressures on the current account (especially given that a significant portion of imports concerns energy products); (c) increased uncertainty may cause the postponement of consumer and investment decisions in the short term and exert upward pressures on private and sovereign borrowing costs.

On the other hand, the Greek economy, has significant counterweights that support short-term prospects: (a) there are expectations of a strong tourist season (see below) upon normalization of the Ukraine situation. Also, latest information points to unabated activity in a number of other sectors, (b) Greece will benefit from RRF (largest beneficiary in the EU as a percentage of its GDP), MFF 2021-2027, and EIB funds, altogether ca €90bn available in the next 5 years. These funds, along with mobilized private and banking capital, not only provide amble liquidity, but also assist in the transformation of Greece's production model towards exports- and investments-driven sustainable growth. This can be achieved via channeling of resources in selected economic activities, green transition and digitization in particular, as well as via the structural reforms that accompany disbursement of funds; (c) the economy enjoys a very comfortable liquidity position: ca €34bn of new deposits were accumulated in the pandemic alone, the State has a cash buffer of ca €38bn as of April 2022, €38.5bn of GGBs were purchased in ECB's PEPP and will be flexibly reinvested up to end 2024, thereby supporting funding costs, and banks draw from TLTRO liquidity; (d) fiscal measures are implemented to cushion energy costs for households and businesses (ca €7,5 bn up to May 2022). These come on top of Covid-19 related support measures of €43.3bn in 2020-2022, of which €4.1bn pertain to 2022. In addition, inflation also reduces to ratio of public debt over GDP, thereby improving confidence on the sustainability of Greece's fiscal position.

The baseline scenario approximates the supply shock caused by energy price increases under the assumptions of no escalation of the war, EU sanctions against Russia at the magnitude known as of May 2022, Greek government fiscal support measures known as of May 2022, monetary policy trajectory as seen in May 2022 (gradual normalization); all in, this leads to a real GDP growth of 3.0%YoY in 2022, and an HICP rate of change of 7%. Although the current baseline scenario foresees lower GDP growth than pre-war projections, the unemployment path is improved due to base effects (lower realized unemployment for 2021) and continued support measures.

The adverse scenario assumes a prolongation of the war and economic sanctions, which lead to a larger supply shock, manifested in higher energy prices. In turn, this means higher and more persistent inflation (and subsequent erosion of incomes), more protracted postponement of investment, lower external demand but also more fiscal support measures. All in, this leads to a real GDP growth of 1.4%YoY in 2022. The size of the difference between the baseline and the adverse scenaria ensues from the nature of the supply side shock implemented and, therefore is not attempting to approximate tail risks, i.e. a cumulative impact of a multitude of negative factors.

It is important to note that the estimate is conducted with hard data up to March 2022, leading indicators up to April 2022, and fiscal support packages announced up to May 2022. As reminder, GDP growth of 8.3%YoY was recorded in 2021, which was used as a basis for 2022 GDP forecast; also, according to AMECO, (net) national disposable income at current prices (EUR bn) at end 2021 was standing at € 149.8bn.

A. Baseline Scenario

Disposable Income drivers & Private Consumption

The following section analyzes impacts to various components of GDP and aggregates that into the headline projection. As for private consumption, impacts to disposable income are calculated along with transmission to consumption via the respective elasticity. Determinants of exports include price competitiveness and global demand.

Impacts:

(a) Primary fiscal deficit of €4bn in 2022 (assuming energy bill support up to June inclusive) vs €9.1bn in 2021 (according to 21.4.2022 El.Stat. announcements); assuming measures are reflected equiproportionally in disposable incomes, a fiscal drag of -€4bn or -2.7% decrease in nominal net disposable income

(b) increase in capital profits: +8 % increase (vs +6.8% in EC due to, inter alia, a robust tourism season expected despite Ukraine), times 50% share of capital on GDP, i.e. €7.1bn or 4.7% increase in nominal net disposable income

(c) Decline in unemployment: 12.6% of labor force from 14.8% in 2021,[1] i.e. ca 98,000 less persons unemployed compared to 2021. Assuming a per person loss in disposable incomes from unemployment approximately equal to €13k (difference between the per capita gross income and the unemployment benefit), decrease of unemployment will increase total net nominal disposable income by ca €1.3billion or 0.9%.

(d) Wages: +4.5% increase (partial carry from minimum wage increase, given slack in labour market), times 50% share of labour on GDP, i.e. €4bn or 2.7% increase in nominal net disposable income

In total, net nominal disposable income is projected to increase by ca € 8.4billion or 5.6%. In addition, we pencil consumption of €2.2bn of deposits by households accumulated during the pandemic in an effort of

[1] The estimation of unemployment is based on projections of an increase of the labour force and a decrease of non-active population in 2022, and employment growth peaking in 2022 (decelerates afterwards to a rate ower compared to its pre-pandemic trend).

households to intertemporally smooth their consumption (although total deposits will continue to grow due to credit expansion and tourism, inter alia).

Eurobank Research projects an HICP change of 7% (period average), due to 4.8ppts carry from energy prices and an estimate of core inflation of 1.8%, a bit under ECB's 2% target due to labour &product market reforms.2 Hence real disposable incomes (plus wealth) should be flat (0% change, vs 1.5% in EC's 2022 Spring forecasts).

Note that according to the historical experience, which is consistent with intertemporal consumption smoothing, income elasticity of consumption is 0.9, yet flat incomes mean no change.

Government consumption: +0.5% change (vs -1.7% in EC's 2022 Spring forecasts) given continued support measures.

Gross capital formation: +7.4% change (vs EC's 2022 Spring forecasts of +14.7%) on the back of Ukraine-imposed increase in uncertainty and energy costs, increasing (albeit still favorable due to monetary laxity) cost of capital, recovery of real estate and modestly increasing (external and domestic) demand.

Exports of g&s: a 35% increase is expected in tourism (ca 80% of 2019 revenues; conservative estimate, leading indicators point to upside risks) and 10% in transportation (IMF foresees a 5% increase in global trade, fares expected to increase by ca 5-10%), which comprise 14% and 25% of 2021 total exports of goods & services respectively; 25% in fuel exports (due to ca 25% increase in average oil prices), which are ca 14% of g&s exports. For the rest, a 5.2% average increase in external demand is expected from equiproportional recovery in trading markets (+4.2%) and improvement in relative prices (+1%), assuming unitary elasticity of demand for Greek g&s with respect to both prices and income. Overall, an 13.4% increase in exports is expected (vs EC's 2022 Spring forecasts of +11.6%)

Imports of g&s: a 7.5% real increase of imports (vs EC's 2022 Spring forecasts of +7.9%), with 5.3ppts coming from increase in fuel imports' prices and the rest from remaining goods (modest as private consumption does not rise).

B. Adverse Scenario

Disposable Income drivers & Private Consumption

Impacts:

(a) Primary fiscal deficit of €6bn in 2022 (augmented energy bill support) vs €9.1bn in 2021; assuming not all measures are reflected equiproportionally in disposable incomes, a fiscal drag of -€2.5bn or -1.7% decrease in nominal net disposable income

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[2] The estimation of the inflation rate is based, inter alia, on projections of the unemployment rate and oil prices (consistent with market expectations). Hence, the persistence of higher than earlier foreseen oil prices poses *upside risks to the projection.*

(b) Increase in capital profits: +6% increase, times 50% share of capital on GDP, i.e. €5.3bn or 3.6% increase in nominal net disposable income

(c) Decline in unemployment: 13.5% of labor force from 14.8% in 2021 ca 60,000 less persons unemployed compared to 2021. Assuming a per person loss in disposable incomes from unemployment approximately equal to €13k (difference between the per capita gross income and the unemployment benefit), decrease of unemployment will increase total net nominal disposable income by ca €0.8billion or 0.5%.

(d) Wages: +4% increase (smaller carry from minimum wage increase, given higher slack in labour market compared to baseline scenario), times 50% share of labour on GDP, i.e. €3.5bn or 2.3% increase in nominal net disposable income

In total, net nominal disposable income is projected to increase by ca €7.1bn or 4.7%. In addition, we pencil consumption of €3bn of deposits by households accumulated during the pandemic in an effort of households to intertemporally smooth their consumption (although total deposits will continue to grow due to credit expansion and tourism, inter alia).

An HICP change of 8.2% is projected, higher than in the baseline scenario given higher expected oil prices (a yearly average of $140/bl vs a historic average of $72/bl). Hence real disposable incomes (plus wealth) should decrease by -1.5%.

According to the historical experience, which is consistent with intertemporal consumption smoothing, an income elasticity of consumption of 0.9 was used. Hence, real private consumption would decrease in 2022 by -1.3%.

Government consumption: +2.5% change vs given more durable support measures.

Gross capital formation: +5% change on the back of larger Ukraine-imposed increase in uncertainty and energy costs.

Exports of g&s: a 19% increase is projected in tourism (ca 70% of 2019 revenues) and 5% in transports, which comprise 14% and 25% of 2021 total exports of goods & services respectively; 70% in fuel exports (due to ca 90% increase in average oil prices), which are ca 14% of g&s exports. For the rest, a 3% average increase in external demand is expected. Overall, an 15.2% increase in exports is expected.

Imports of g&s: a 10.8% real increase of imports: +12.4ppts from fuel price increases minus -1.6ppts from imports decrease (import elasticity of income 1.2).

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