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Quantitative assessment of relief strategies reportedly discussed at this week's Eurogroup

This brief note attempts a preliminary assessment of a range of strategies reportedly discussed at the last Eurogroup on how to deal with Greece's sovereign liquidity and solvency problems, especially in view of the deeper-than-expected domestic recession and the recent extension of the country's fiscal adjustment programme by two years. Relying on a number of media reports as to the content of official discussions, the analysis presented herein evaluates the potential impact of some of these measures on the evolution of Greece's public debt ratio and the general government borrowing need and sources of funding. Without necessarily taking a firm view on the feasibility of proposed initiatives (*from a political, constitutional or other perspective)*, our analysis suggests that some of the measures discussed at this week's Eurogroup could be adequate to bridge the projected borrowing gap in 2013-2016 and bring the country's debt to GDP ratio to sub-120% levels by FY-2020. Heading into the extraordinary November 26 Eurogroup, financial markets expect EU partners and the IMF to resolve any lingering differences on how to deal with the Greek fiscal sustainability problem and agree on sound and brave strategies to support Greece and safeguard the stability of the euro area. Greece has already fulfilled all key prerequisites for the release of the next EU-IMF loan tranche and the ball is now in the official lenders' court to: (i) give the green light to next loan disbursement; and (ii) provide certain concessions to repair Greece's sovereign solvency outlook.

Table 1.1 below adjusts the *baseline* debt sustainability analysis (DSA) for Greece we presented in our November 16, 2012 *Greece Macro Monitor*[1], so as to broadly incorporate the underlying assumptions of the new troika DSA reportedly discussed at this week's Eurogroup.[2] Note that the new baseline scenario reveals a dramatic deterioration in public debt dynamics (relative to the troika's March 2012 assessment), purportedly as a result of the deeper-than-expected domestic recession, a 2-year lengthening of the agreed fiscal consolidation programme and past implementation slippages ensuing from a prolonged pre-election period.[3]

[1] See Eurobank Research "Now, more than ever, fiscal sustainability requires stabilization of domestic output dynamics", November 16, 2012.
http://www.eurobank.gr/Uploads/Reports/GREECE%20MACRO%20FOCUS%20November%2016%202012.pdf

[2] According to press reports, the new troika DSA now sees Greece's public debt-to-GDP ratio declining to 144% at the end of FY-2020 (and to 133% in FY-2022) after peaking at ca 190% in 2013-2014.

[3] The baseline scenario of the March 2012 troika assessment envisaged a terminal debt ratio of 116.5%-of-GDP in FY-2020.

Table 1.1 – Greece: debt sustainability analysis (revised "baseline" scenario)

		Projections										
	2011	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**	**2019**	**2020**	**2021**	**2022**
Nominal GDP growth (%)	-6.1	-6.5	-5.4	0.2	3.2	4.9	4.9	5.0	4.9	4.7	4.4	4.1
Primary balance (% GDP)	-2.3	-1.5	0.0	1.5	3.0	4.5	4.5	4.5	4.5	4.5	4.5	4.5
Avrg interest rate on debt (%)	4.5	3.0	2.8	3.1	3.7	3.7	3.7	3.7	3.7	3.7	3.8	3.8
Stock flow adjustment (% GDP)	3.6	-12.6	-2.7	-3.2	-3.4	-2.6	-1.6	-1.6	-1.6	-1.7	-0.6	-0.1
Gross public debt (% of GDP)	**170.6**	**176.8**	**189.4**	**190.1**	**184.7**	**175.7**	**167.5**	**159.4**	**151.6**	**144.0**	**138.0**	**133.0**

Source: EC,ECB, IMF, Eurobank Research

Table 2 on page 4 presents a quantitative assessment of the impact of a number of potential relief strategies *reportedly* discussed at the November 20, 2012 Eurogroup. The strategies discussed aimed to re-instate fiscal sustainability[4] and bridge the government financing gap ensuing from a 2-year extension in the country's fiscal adjustment programme. According to a number of reports circulated in the foreign press and newswires, these include a broad set of proposals, ranging from lower interest rates on loans disbursed under the 1st programme (Greek Loan Facility) and debt buybacks to a deferral of interest payments on new EFSF loans, return of future profits accruing to Greek Government Bond (GGB) holdings of Eurosystem central banks as well as other measures.

We next proceed with a preliminary assessment of the potential impact of some of the measures presented in Table 2 on the evolution of Greece's public debt ratio and the general government borrowing need and sources of funding. **Table 1.2** shows the projected *decline* in the general government *net* borrowing requirement over the period 2013-2022, under two distinct theoretical scenarios envisaging implementation of different combination of strategies depicted in Table 2.

Specifically, **Scenario I** of Table 1.2 assumes:

— **A1.1** (*savings from a reduction of the interest rate currently charged on GLF loans to an all-inclusive rate close to current 3M euribor*);
— **A2** (*savings from a return to Greece of future income accruing to GGB holdings of Eurosystem central banks*);
— **A3.1** (*savings from a reduction in coupon payments due to debt buyback; debt buyback facility assumed to be financed at EFSF funding cost*);
— **A4** (*savings from abolishment of EFSF fee cost*);
— **B1** (*temporary savings from assumed deferral i.e., by 10-years of interest payments on EFSF loans disbursed under the 2nd programme*); and
— **B2** (*abolishment/postponement of certain cash buffers envisaged in the 2nd bailout programme*).

Similarly, **Scenario II** of Table 1.2 assumes implementation of strategies **A1**, **A2**, **A3.1**, **A4**, **B1** and **B2**..
In the baseline scenario we presented in our November 16, 2012 *Greece Macro Monitor*[5], we estimated the cumulative borrowing gap ensuing from a 2-year extension in the fiscal programme (and past implementation slippages) to be ca €15bn in 2013-2014; ca €32.6bn in 2013-2016 and close to €60bn over the period 2013-2020. [6] As attested by Table 1.2, the measures reportedly discussed at the Nov 20 Eurogroup, if implemented, appear to be adequate to broadly cover the cumulative borrowing need in 2013-2016 and beyond (probably, with some additional financing from increased T-bill issuance vs. what was projected in the troika's March 2012 baseline *i.e.*, close to zero from FY-2014 onwards).

[4] "Fiscal sustainability" is broadly defined here as the ability of reaching a debt-to-GDP ratio no higher than 120% over the relevant forecasting horizon (2020 or 2022).

[5] See Eurobank Research "Now, more than ever, fiscal sustainability requires stabilization of domestic output dynamics", November 16, 2012.
http://www.eurobank.gr/Uploads/Reports/GREECE%20MACRO%20FOCUS%20November%2016%202012.pdf

[6] The figures quoted assume broadly zero market financing via the issuance of medium- and long-term government paper.

Table 1.2 – Projected reduction in government net borrowing need due to cash relief measures

	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Senario I	**-6.52**	**-9.86**	**-4.47**	**-4.30**	**-8.55**	**-8.71**	**-9.95**	**-8.83**	**-7.69**	**-7.74**
cumulative	-6.52	-16.38	-20.86	-25.16	-33.71	-42.42	-52.37	-61.20	-68.89	-76.63
Scenario II	**-4.54**	**-7.81**	**-2.81**	**-3.31**	**-5.50**	**-5.85**	**-6.20**	**-6.20**	**-6.29**	**-6.39**
cumulative	-4.54	-12.35	-15.17	-18.47	-23.97	-29.83	-36.03	-42.23	-48.52	-54.91

Source: EC,ECB, IMF, Eurobank Research

From a fiscal sustainability stand-point, certain combinations of the range of strategies reportedly discussed at the Nov. 20 Eurogroup appear to be broadly adequate to bring the debt ratio to sub-120%-of-GDP levels in FY-2020 and beyond (see **Table 1.3**).

Table 1.3 - Greece: debt sustainability analysis (after implementation of new debt relief measures)*

		Projections										
	2011	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**	**2019**	**2020**	**2021**	**2022**
Nominal GDP growth (%)	-6.1	-6.5	-5.4	0.2	3.2	4.9	4.9	5.0	4.9	4.7	4.4	4.1
Primary balance (% GDP)	-2.3	-1.5	0.0	1.5	3.0	4.5	4.5	4.5	4.5	4.5	4.5	4.5
Avrg interest rate on debt (%)	4.5	3.0	2.0	1.8	1.9	2.6	2.2	2.0	2.1	2.3	2.3	2.4
Gross public debt (% of GDP)	**170.6**	**176.8**	**182.0**	**179.5**	**170.4**	**159.6**	**148.7**	**138.1**	**127.5**	**117.9**	**110.4**	**104.0**

Source: EC,ECB, IMF, Eurobank Research

(*) Table 1.3 assumes implementation of strategies A1, A2, A3, A4, A5, B1 and B2 depicted in Table 2

Bottom line

Greece has already fulfilled all key prerequisites for the release of the next EU-IMF loan tranche and the ball is now in the official lenders' court to: (i) give the green light to the next loan disbursement; and (ii) provide certain concessions to repair the sustainability of Greece's fiscal position.

From a *pure* technical standpoint, the measures reportedly discussed at the November 20, 2012 Eurogroup appear to be adequate to bridge the projected borrowing in 2013-2016 and bring the country's debt to GDP ratio towards sub-120% levels in FY-2020 and beyond.

Heading into the extraordinary November 26 Eurogroup, financial markets expect EU partners and the IMF to resolve any lingering differences on how to deal with the Greek fiscal sustainability problem and agree on sound and brave strategies to support Greece and safeguard the stability of the euro area.

Table 2 – Projected impact of debt-relief and financing support measures reportedly discussed at Nov. 20 Eurogroup (amounts in euro billions)

	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
	Debt relief measures									
A1. Savings from reduction by 70bps of the interest rate currently charged on EU bilateral loans disbursed under the 1st programme (GLF)	0.37	0.37	0.37	0.37	0.37	0.37	0.37	0.37	0.37	0.37
A1.1 Saving from more drastic reduction of interest rate currently charged on GLF loans (to an all-inclusive rate close to current 3M euribor)	0.82	0.90	1.06	1.19	1.45	1.59	1.72	1.72	1.63	1.59
A2. Savings from return to Greece of future income accruing to (SMP-related) GGB holdings of Eurosystem central banks (40% disbursed during programme period)	1.53	1.52	0.97	0.17	1.96	1.65	2.40	1.28	0.14	0.14
A3. Upfront (net) debt reduction of €15bn voluntary buyback of new GGBs		10								
A3.1 Savings from reduction in coupon payments due to debt buyback (financing of debt buyback facility assumed to be at EFSF funding cost)	0.18	0.17	0.16	0.29	0.26	0.25	0.24	0.24	0.33	0.42
A4. Savings from abolishment of EFSF fee cost	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
A5. Temporary reduction in loan amortization payments due to the lengthening (reprofiling) of maturitites and grace period (from 10 to 20 years) of GLF and EFSF loans								2.80	3.53	13.18
	Measures to cover additional financing needs									
B1. Temporary savings from *assumed* deferral (by 10-years) of interest payments on EFSF loans disbursed under the 2nd programme	2.39	2.67	3.69	4.05	4.77	5.13	5.49	5.49	5.49	5.49
B2. Abolishment/postponment of certain cash buffers envisaged in 2nd bailout programme - net reduction (positive sign) or increase (negative sign) in government borrowing requirement	1.50	4.50	-1.50	-1.50						

Source: Eurobank Research, press report

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