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Greece must change or sink!

By Harris A. Samaras

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Pytheas Investors Service

The Athens stock market lost 1.2% per cent in early trading two days ago as investors absorbed news of the Greek government's plans to reduce the nation's budget deficit. The spread between 10-year Greek sovereign debt and German Bunds jumped also above 255 basis points, signaling traders remain concerned...

A day before the newly elected Prime Minister, George Papandreou, had announced a crackdown on corruption and the introduction of tight controls on spending but the speech – which came after markets closed – disappointed market-watchers who had expected more decisive measures to reduce the budget deficit.

The newly appointed government told trade unionists and business groups that public sector workers would receive real wage rises next year in spite of Greece's deteriorating public finances. Also a 90% tax on bonuses for senior bankers in the private sector, a ban on bonuses for executives at public sector corporations and a 10% cut in social security and government spending have been announced.

But trade unions are staging a 24-hour strike today in protest against the government's economic policies. And Mr Papandreou will face harsh criticism from two leftwing leaders over his plans to freeze civil servants' salaries above €2,000 monthly and cut their allowances by 10 per cent, although he approved real pay increases for lower-paid workers.

The economy is predicted to shrink by 1.3% this year and another 0.3% in 2010. The deficit would fall by 4 percentage points of GDP in 2010 against earlier targets of 3.6%. Mr. Papandreou repeated his pledge to European Union leaders to cut the budget deficit from 12.7% of GDP to below 3% at the end of 2013. Investors continue to sell the country's bonds and stocks… Note that the country's public debt is currently at 113.4% of GDP!

The desirability of his aim – slashing the Greek budget deficit from 12.7% of gross domestic product to below the EU's 3% limit by 2013 is clear. The problem is getting there. Since 1981, the Greek budget deficit has only been that low once, in 2006. True, over the previous decade the deficit did shrink from a ruinous 15% of GDP to within a 3%. But that took more than nine years. The Greek government now proposes tightening almost as much and in half the time. And public acceptance of these measures is key to the success of stabilizing Greece's situation over the long term. More importantly, increasing public sector pay and taxing bankers' is definitely not the solution!

Top European Union officials have repeatedly stated that Brussels would help Euro-member governments in trouble but EU solidarity does not represent a blanket guarantee. If it did, Greek government bonds would trade in line with German Bunds. Nor would any help be an act of EU charity. Other Eurozone members would rather see Greece's problems contained than have them contaminate their markets – and so increase their cost of funding.

The scale of any aid need not be prohibitive; Greece accounts for only less than 3% of the Eurozone economy. There is also a precedent. Hungary, Latvia and Romania have all won EU and IMF backing, albeit with tough conditions attached. In short, the risk of a default remains remote, although Greece will have to take pain, now. Additionally, **it is Pytheas opinion that Greece is not the next domino to default! It is unthinkable that an EU member country would default! A bankruptcy in the Eurozone could destroy the common European currency; confidence in the Euro will be shattered... If one EU member fails, speculators will test the stability of other potential bankruptcy candidates… and then what about Spain, Portugal, Italy and Ireland? What about the impact on countries such as Germany, where many banks have invested heavily in the high-yield Greek treasury bonds?**

Despite the above last statement, Pytheas predicts that any time shortly and most likely before Christmas, Greece will have its credit rating cut by at least a notch to A2 by Moody's Investors Service. The imminent downgrade will put Greece's rating five steps above noninvestment grade and two higher than the levels assigned to it by Standard & Poor's and Fitch Ratings. The ranking is the lowest among the euro-member states and the same as that of Poland and Botswana.

It is, however, the position of Pytheas that Greece is extremely unlikely to face short-term liquidity or refinancing problems unless the ECB decides to take the highly unusual step of making the sovereign debt of a member state ineligible as collateral for bank repurchase operations.

Greece needs to undergo harsh adjustments and reforms in order to regain competitiveness and credibility. **The Country has to address immediately the main causes of societal "cancer" and eliminate them from the root! Providing solutions the "Greek way" is usually the creation of another department, another level of command and supervision that is supposed to control the already infected ones. As a result, they end up getting infected themselves; Greek citizens are "forced" to "cheat" to get by; more red tape; more chaos; governments come and go; and Greeks citizens are treated and behave as "children of a lesser God"!** The vast majority, if not all, of Greek citizens believe that nothing can change because those who govern the country have made corruption a way of life.

Systemic corruption and **"clientelism"** – paying money for political favors – had created a sense of the lack of the rule of law in Greece and accentuated issues such as tax evasion – Greece has the highest corruption indices according to the charts of all international organizations (from the IMF to the World Bank); considered the most corrupted state in the 25-member bloc.

The current **tax inspectorate** cannot remove corruption and end tax evasion when most businesses regard the inspectors as all-powerful protection racketeers who threaten companies with audits and heavy fines unless they pay bribes. The vicious cycle extends to the **parallel economy** (black/shadow/underground economy) – which is one of the largest in size amongst EU countries – forcing entrepreneurs to go "underground" not to avoid official taxes, but to reduce the burden of bureaucracy and corruption.

The **health sector** is even shadier. The so-called "fakelaki" is a prime example. This cash "gift" for the doctor and/or the administrator before an operation or medical treatment is thought to guarantee less waiting, the best possible care for a patient and a descent room at public hospitals.

The **real estate industry** is also riddled with bribes and kickbacks. Most architects, builders and staff at town planning offices require "speed-up" fees to issue permits without delay. This becomes even more complicated since Greece has no central computerized system researching land titles… the only EU member country that does not yet have a "functional" **land registry**!

Stifling bureaucracy, **red tape** and legal confusion have been the cause of Greece missing EU and other grant deadlines as well as foreign direct investments of hundreds of billions of Euros during the last five years alone.

Last but not least, **Greek political parties** are so one-sided and polarized that they will more than often contradict themselves depending on whether they are in power or not.

Greece must change fundamentally or sink!

See also "Greece unlikely to escape its worst financial crisis of modern times!"