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Preliminary Debt Sustainability Analysis for Greece

This note, produced by the staff of the European institutions, summarizes their views and those of the IMF staff. It presents a preliminary debt sustainability analysis of Greece assuming a Staff Level Agreement (SLA) and an extension of the current EFSF financial assistance programme for five months. During this period financial assistance in the form of EFSF disbursement (including redirection of the HFSF buffer), SMP profits transfer and IMF disbursement would be provided. It first recalls the parameters of the 2012 EG agreement, then looks at the current estimates of the debt/GDP level at the 2020 and 2022 horizon depending on different assumptions, and then, as a complement, examines gross financing requirements for assessing debt sustainability in light of the specificities of the structure of the Greek debt. A more detailed DSA will be presented at the full closure of the review.

1. The 2012 EG framework for debt

The 2012 EG framework agreed on a number of measures to ensure that Greece can reach a debt-to-GDP ratio of 124% in 2020, and in 2022 a debt-to GDP ratio substantially lower than 110%. It also agreed to consider further measures, if necessary, for achieving a credible and sustainable reduction of Greek debt-to-GDP ratio, when Greece reaches an annual primary surplus, as envisaged in the current MoU, conditional on full implementation of all conditions contained in the programme. The Eurogroup of 20 February 2015 reaffirmed the commitment to this framework.

Greece has already benefitted from a number of debt reducing measures. Conditions on the GLF have been revised three times (extension of the grace period and maturities, reduction in interest rates). Conditions on EFSF have been amended in 2012 (extension of maturities, cancellation of fees and deferral of interest rates payments). Moreover, the Eurogroup committed to transfer the profits of SMP and ANFA. Overall, these measures already imply a direct reduction of financing needs over the next decade and correspond to an economic debt relief, in net present value terms, from a market perspective. It should also be noted that interest payments of Greece are comparable to those of less indebted countries (Italy, Portugal for instance). Finally, the PSI operation led to a reduction of around EUR 100bn of public debt in March 2012 (52% of 2012 GDP).

2. Current situation with respect to DSA

It is clear that the policy slippages and uncertainties of the last months have made the achievement of the 2012 targets impossible under any scenario. The main factors behind the deterioration of the DSA are the worsening of economic growth, the revised primary balance path, the lower privatisation revenues and possible additional financial needs for the banking sector.

3. DSA under different scenarios

For this preliminary DSA, three scenarios are presented. The first assumes full implementation of programme reforms and corresponding growth effects; the second assumes partial reform compliance, among others regarding privatization, resulting in a 0.5% lower growth path and a higher risk premium (0.6%). The third scenario reflects the IMF's baseline. Further work is under way to reconcile the scenarios.

Under all scenarios, debt to GDP ratios are on a declining path but remain substantially above the Eurogroup November 2012 targets described as "well below 110% by 2022".

			2015	2020	2022	2030
	Debt to GDP ratio (%)	Scenario A	172.8	137.5	124.0	85.0
		Scenario B	174.3	146.5	135.0	100.9
		Scenario C	176.7	149.9	142.2	118.0
Assumptions*	**Primary surplus (%GDP)**	Scenario A	1.0	3.5	3.5	3.5
		Scenario B	1.0	3.5	3.5	3.5
		Scenario C	1.0	3.5	3.5	3.5
	Privatisation proceeds (€bn), cumulative	Scenario A	1.4	15.2	22.0	26.8
		Scenario B	0.4	9.2	16.0	20.8
		Scenario C	0.5	3.0	4.0	4.0
	Nominal GDP growth	Scenario A	-0.6	4.1	4.1	4.0
		Scenario B	-1.2	3.5	3.5	3.5
		Scenario C	-1.2	3.7	3.5	3.5
	Re-financing rates (%)	Scenario A	1.4	5.1	4.9	4.1
		Scenario B	1.4	5.4	5.2	4.7
		Scenario C	1.4	6.3	6.3	6.3

Note: All scenarios assume a new 3-year programme with concessional financing. Debt ratio would be higher if additional needs for bank recapitalisation are needed.

4. The Role of Financing Needs

Focusing on the debt-to-GDP level does not allow to capture the structure of debt and per se is not accounting entirely for the measures taken for the European financial support to make Greek debt sustainable. This aspect can better be assessed by the gross financing needs of a country, which captures its payment structure over time. Lower gross financing needs imply better market access and less financial stability risk.

This gross financing need metric points to no sustainability issues under the first two scenarios. The gross financing needs remain well below 15% threshold, a threshold mentioned in IMF guidance for this criterion. Under this scenario c), significant reprofiling of the stock of debt and concessional lending terms would improve sustainability. Reprofiling of payment flows does not imply nominal haircut or budgetary costs for creditors. This would also entail further NPV gains for Greece, and strengthen the sustainability of the Greek public debt in the long-run.