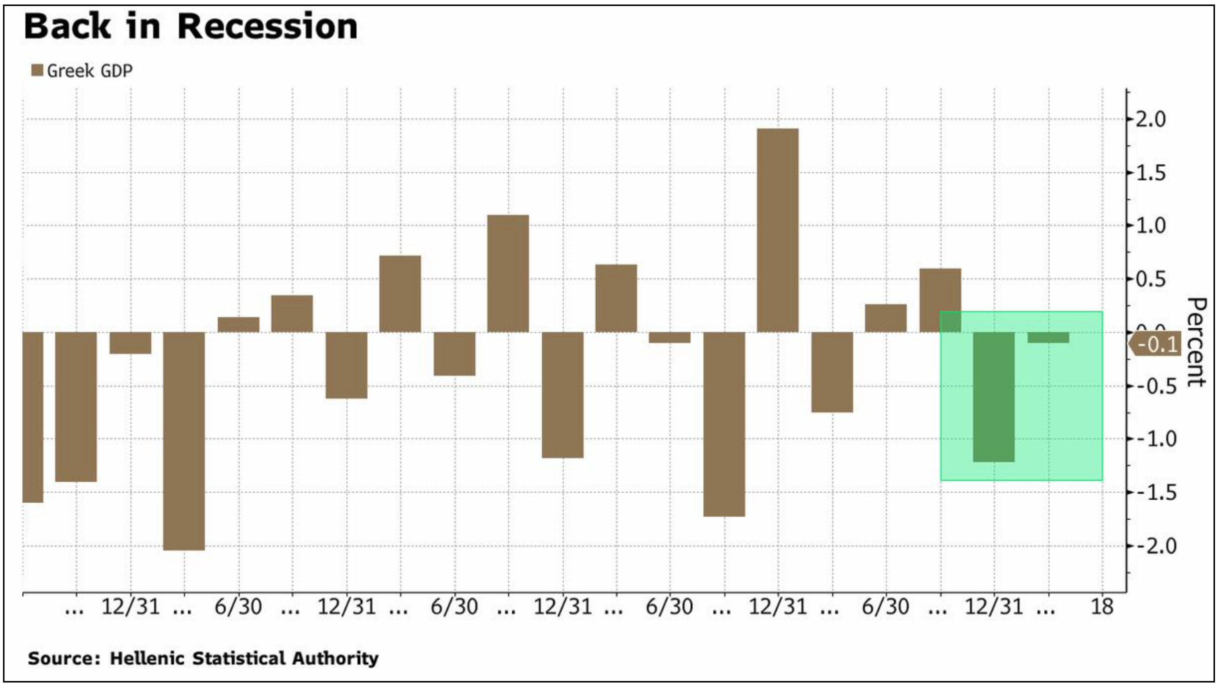
[Greek Economy Limps Onto Launchpad After Late-Night Vote]

Marcus Bensasson and Sotiris Nikas, *Bloomberg*, 19 may 2017

Greece's latest economic reforms will be key to winning debt relief that unleashes years of pent-up investment and finally ends its economic crisis. Or the austerity will crush the economy and send the government cap-in-hand for another bailout.

We'll soon find out.



After data this week showed the economy slipped back into recession in the first quarter, lawmakers on Thursday approved the latest economic measures demanded by creditors to keep the bailout loans flowing. The danger is that if efforts to hit ambitious budget goals choke the economy so much the target is missed next year, pension cuts and tax hikes will tighten the noose further.

"The Greek economy finds itself at a crucial crossroads," said Nikos Vettas, head of the Foundation for Economic and Industrial Research in Athens. "It's roughly at the same level as three years ago, and while many forces that built a negative dynamic since the start of the crisis are now weaker, there is no guarantee it will enter a sustainable growth phase."

If Greece gets a substantial enough commitment on debt relief from euro-area creditors, that in turn could restore confidence and allow investment to flow into the real economy. A deal of this kind will be discussed at Monday's meeting of euro-area finance ministers in Brussels.

With the result of the vote, "the ball is now in the lenders' court" and "it's their turn to keep their commitments as we did," Greek Prime Minister Alexis Tsipras said early Friday after he got lawmakers' approval for the economic measures. "We expect, and are entitled to, from next Monday's Eurogroup meeting, a decision on Greek public debt," he said.

Greek markets rallied this month following the conclusion of a preliminary agreement with euro-area creditors and the International Monetary Fund. Uncertainty in the run up to that deal is blamed for putting the country back in recession and causing the government to cut its 2017 growth forecast to 1.8 percent from 2.7 percent.

Turning Point

Under the optimistic scenario, a debt agreement that satisfies the IMF makes it easier for the European Central Bank to include Greek government paper in its asset-purchase program and the public debt agency to resume bond issuance this year. That triggers a stream of foreign investment chasing returns in a the country where the central bank says gross domestic product is almost 10 percent below potential.

“The agreement with the creditors entails some recessionary measures, including the requirement to deliver rising primary surpluses” in the next few years, said Nikolaos Karamouzis, chairman of Eurobank Ergasias, the country’s third-biggest lender, and of the Hellenic Bankers Association. “This negative impact would be more than offset by a better market and economic climate, QE participation and viable public debt restructuring.”

In exchange, Greece is going to have to sustain its budget surpluses for longer than the government had hoped. Dutch Finance Minister Jeroen Dijsselbloem, who chairs the group of euro-area finance ministers, on Thursday proposed the primary budget surplus should be at least 3.5 percent of GDP for five years from 2018, something the IMF has said will exact a huge price on the Greek economy, if it can be achieved at all.

Thursday’s budget package included 5.4 billion euros ($6 billion) of stimulus measures for 2019 and 2020 to offset the pension cuts and tax hikes demanded by creditors. But the catch is that this stimulus will only kick in if Greece beats budget goals.

The government says it will meet its target, pointing to a 4.2 percent primary surplus last year compared with a target of 0.5 percent as evidence that the IMF is too pessimistic.

Ilias Lekkos, chief economist at Piraeus Bank SA in Athens, isn’t convinced.

“There’s no precedent for a non-oil exporting country achieving a 3.5 percent primary surplus systematically for a period of many years,” he said. “It either can’t be achieved, or it will be achieved at the cost of a huge recession.”