Greece makes up its mind on debt goals

For the first time since Yanis Varoufakis went to his first Eurogroup meeting in February last year armed with a polemical speech and a Burberry scarf, we now have a relatively clear idea of what the Greek government would be satisfied with in terms of debt relief.

Speaking to a parliamentary subcommittee on Thursday, Alternate Finance Minister Giorgos Houliarakis set out in the most detail seen so far the type of measures that Athens would seemingly be content with. Never before has an official from this coalition set out clearly the parameters of what is acceptable to Athens.

The last few weeks have seen almost every member of the coalition from Prime Minister Alexis Tsipras down discuss debt relief. This created a cacophony from which it was difficult to extract any useful conclusions, especially as most of the statements were rather vague generalizations about how necessary a reduction in Greece's public debt is, or how positive its effect could be.

The government seemed as confused as those trying to decipher its messages. When Deputy Prime Minister Yiannis Dragasakis appeared before the same subcommittee as Houliarakis in September and played down expectations of something significant happening on the debt front in the coming months – explaining that it is a process that will largely kick in from 2018 onwards – the coalition's immediate reaction was to try to revive hopes of something big being achieved in the short term.

Houliarakis, though, appears to have dispelled the doubts and cleared up any confusion. Speaking to parliamentary deputies last week, he said that the government accepts the benchmark for debt sustainability set by the May 24 Eurogroup.

The eurozone finance ministers set out gross financing needs (the sum of budget deficits and funds required to roll over or pay debt that matures during the year) as the yardstick for judging whether Greek could meet its debt commitments. They agreed that Greece's gross financing needs should remain below 15 percent of gross domestic product until 2030 and not exceed 20 percent after that.

The alternate minister's clarification seems to have laid to rest the recent debate over how to judge whether Greece's debt is sustainable or not. In previous years, the total debt stock as a percentage of GDP and debt servicing costs against GDP were used as methods to measure sustainability.

Working on the gross financing needs principle, Houliarakis then proceeded to propose a couple of methods by which the Greek debt could be made sustainable in the medium term. Using calculations made by the Council of Economic Advisers (SOE) and the Public Debt Management Agency (PDMA) he suggested that one option to ensure that Greece's gross financing needs remain below 15 percent of GDP until at least 2030 is to fix the interest rates on the loans Greece has received at lower levels.

Apart from tweaking the interest rates, the other path proposed by the Greek official is to also extend the maturity of the loans Greece received from the European Financial Stability Facility (EFSF), which have a weighted average maturity of around 31 years and amount to almost 131 billion euros. This is just under half of the total lending Athens has received so far through the three bailout programs.

According to Houliarakis, this approach would have the advantage of reducing Greek debt, in net present value terms, to 80 percent of GDP over a 40-year-period from the current level of close to 180 percent of GDP.

In perhaps the most important part of his explanation in Parliament, Houliarakis stressed the need for the debt relief measures to translate into lower primary surplus targets in the future. He argued this would allow the government the necessary fiscal space to reduce personal and corporate tax; moves which should have a positive multiplier effect for the local economy.

Under a scenario put together by the European Stability Mechanism (ESM) that does not include any relief, Greece would have to reach a 3.5 percent of GDP primary surplus in 2018 and then maintain it for 10 years. To do this, it would also need an average annual growth rate of 3.3 percent. Given the economic devastation Greece has been through during the crisis, it is little wonder that hardly anybody thinks this is anywhere near feasible.

Houliarakis argued that aiming for a 3.5 percent primary surplus for any more than one year would be too much of a risk. Debt relief would allow these targets to be lowered without any danger of Greece's gross financing needs exceeding the comfort zone established by May's Eurogroup decision.

In its own analysis, the Bank of Greece recently suggested that Greece could aim for primary surpluses of 2 percent after 2018 and maintain its debt at sustainable levels if loan maturities are extended by 20 years and there is a smoothing out of deferred interest payments over a 20-year period.

The significance in all this is that the Greek side – which has been largely a bystander in the debt discussion even though it is the party that will be most affected by the outcome of the talks – has finally set out some proposals and cleared up in its own mind on what it wants to achieve.

It appears to have abandoned any thoughts of walking away from negotiations with the prize package of an all-encompassing deal. Short-term measures are a given as all sides have agreed that the European Stability Mechanism should put them together, but it is significant that Athens now seems to accept that what it would like to achieve on top of that is the defining of the medium-term measures so they can be applied when the time comes.

There is still no guarantee this will happen, as some eurozone players do not want to have this discussion now, but at least the parameters of the discussion are now clearer.

What remains is for Greece and the institutions to conclude the second review within the next few weeks to allow time for the discussion to take place before attention in Europe shifts to a series of national and presidential elections next year and the matter is put on ice. Athens took a great deal of time to make up its mind about debt relief; it must now move quickly to have a chance of securing a deal that meets its goals.