5. GREECE

Greece has been severely affected by the COVID-19 pandemic as the large services sector and the dependency on international tourism make it particularly vulnerable to shocks triggered by travel restrictions and social distancing measures. A swift policy response has helped cushion the impact on employment and businesses so far. Economic activity in 2021 is expected to be supported by the additional fiscal measures presented in the draft budget, while funding from the Recovery and Resilience Facility is not included in the forecast.

Economic growth collapsed in the second quarter …

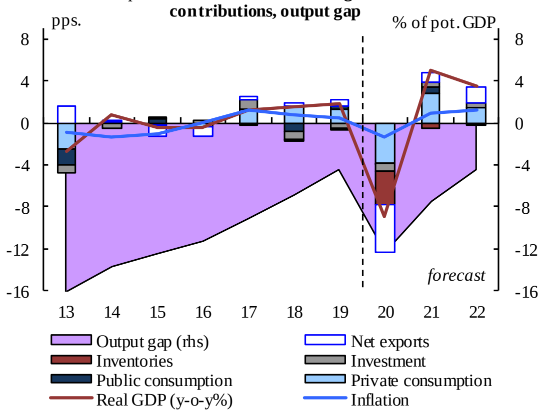
In the second quarter of 2020, real GDP declined by an unprecedented 14% quarter-on-quarter after a relatively mild decline of -0.7% quarter-on-quarter in the first quarter. The downturn was a result of the measures taken to limit the spread of the virus, which were most stringent between mid-March and mid-May. Both domestic demand and exports were severely affected. The swift policy response to safeguard employment and ensure liquidity for businesses prevented a more negative impact on the labour market in the first half of the year. Unemployment peaked at 18% in June, up from 15.6% in February, but declined to 16.8% in July.

…but is expected to recover gradually

Economic activity is expected to have recovered to some extent following the gradual lifting of restrictions in mid-May. However, with some restrictions still in place that are affecting consumer behaviour and disposable incomes and potential reintroductions of measures on account of rising numbers of infections, private consumption is expected to recover only gradually over the forecast period. High uncertainty, lower revenues and liquidity constraints took a toll on investment in the first half of 2020, but public investment and liquidity support are expected to facilitate the recovery. Overall, real GDP is forecast to decline by 9% in 2020 followed by a partial rebound in at 5% growth in 2021 and 3½% in 2022.

The external sector also registered a record decline in the second quarter of 2020, with exports of declining by 32% year-on-year. Net exports are expected to contribute negatively to GDP growth in 2020, but turn positive during the recovery in 2021 and 2022. While goods exports are expected to recover quickly, exports of services are expected to remain well below pre-crisis levels even beyond the forecast horizon. International tourism, which is particularly important for Greece's economy, was the driver of the large drop in services exports in the first half of 2020. Tourist arrivals are expected to only partially recover in 2021 and 2022.

Graph II.5.1: **Greece - Real GDP growth and contributions, output gap**



The mild reaction of the unemployment rate to the drop in economic activity so far can be partly attributed to the support measures incentivising labour hoarding; however it is also driven by workers becoming inactive after losing their jobs. Unemployment is expected to reach 18% in 2020. The recovery expected for 2021 and 2022 should help contain unemployed below 17% in 2022. Driven by low energy prices, compressed demand and VAT tax decreases, inflation is expected to be negative at -1.3% in 2020 before partially recovering in 2021 and 2022.

Uncertainty remains very large, particularly in relation to the tourism sector and travel restrictions, and the remaining size of companies' safety buffers. Additional risks are related to geopolitical tensions in the region and migration pressures. To the upside, Greece is likely to receive a substantial amount of funding under the Recovery and Resilience Facility, which could significantly support domestic demand once implemented.

Fiscal policy will support recovery

Greece's headline balance is expected to decline to close to -7% of GDP in 2020 due to the economic downturn and the cost of fiscal measures taken to address the crisis, which is estimated at 4.1% of GDP. The forecast also incorporates the payment of retroactive pensions worth 0.8% of GDP following a Council of State ruling in July 2020. The primary balance monitored under enhanced surveillance is projected to reach a deficit of 4½% of GDP in 2020.

The general government balance is expected to remain in deficit in 2021 and 2022. The forecast factors in the temporary measures announced by the government for 2021, most importantly the decrease in social security contribution rates, the abolition of the social solidarity tax for private-sector earners and a new temporary recruitment subsidy programme with an estimated fiscal cost of 1.1% of GDP. The forecast also includes the cost of a stepped-up 7-year defence programme. The expected gradual economic recovery and the expiry of the emergency measures are projected to slightly reduce the general government deficit to around 6¼% of GDP in 2021. Under a no-policy-change assumption, the general government deficit is expected to decrease further to 3½% of GDP in 2022. This forecast does not include any funding under the Recovery and Resilience Facility.

The fiscal forecast is surrounded by substantial risks. These risks relate the activation of state guarantees that have recently been recently issued as part of the emergency measures. Further risks relate to the cost of ongoing litigation cases and remaining public service obligation, which could deteriorate the balance when agreed. The uncertainty related to the full extent of the retroactive compensation for cuts in supplementary pensions and seasonal bonuses introduced by previous pension reforms remains, as the 2020 Council of State ruling has not be published yet. Further risk stems from the potential additional cost of the coverage of the people without health insurance. On the positive side, Greece is expected to greatly benefit from funding under the Recovery and Resilience Facility, which could trigger additional revenues through its expected impact on growth.

Public debt is expected to increase to around 207% of GDP in 2020 before declining to around 195% in 2022, supported by the economic recovery.

Table II.5.1:

Main features of country forecast - GREECE

		2019			Annual percentage change					
	bn EUR	Curr. prices	% GDP	01-16	2017	2018	2019	2020	2021	2022
GDP		183.4	100.0	-0.2	1.3	1.6	1.9	**-9.0**	**5.0**	**3.5**
Private Consumption		127.0	69.3	0.0	1.9	2.3	1.9	**-5.5**	**4.0**	**2.0**
Public Consumption		36.1	19.7	0.4	-0.1	-4.2	1.2	**-0.1**	**2.2**	**-0.8**
Gross fixed capital formation		18.6	10.1	-3.9	8.1	-6.6	-4.6	**-8.0**	**5.5**	**4.0**
of which: equipment		8.9	4.9	-2.1	23.3	-3.3	6.7	**-15.4**	**5.0**	**2.7**
Exports (goods and services)		73.5	40.1	2.0	8.5	9.1	4.8	**-21.6**	**10.7**	**10.1**
Imports (goods and services)		76.6	41.7	0.6	7.4	8.0	3.0	**-9.8**	**6.7**	**4.7**
GNI (GDP deflator)		183.1	99.8	-0.3	1.5	0.8	2.2	**-8.0**	**3.9**	**3.4**
Contribution to GDP growth:	Domestic demand			-0.3	1.2	4.4	1.7	**-4.6**	**3.9**	**1.7**
	Inventories			0.0	-0.1	-3.2	-0.5	**0.0**	**0.0**	**0.0**
	Net exports			0.3	0.2	0.3	0.7	**-4.6**	**0.8**	**1.6**
Employment				0.2	-0.5	1.4	1.2	**-3.6**	**1.7**	**1.6**
Unemployment rate (a)				15.3	21.5	19.3	17.3	**18.0**	**17.5**	**16.7**
Compensation of employees / head				1.3	1.5	1.8	1.0	**-1.0**	**0.3**	**0.5**
Unit labour costs whole economy				1.8	-0.3	1.6	0.4	**4.8**	**-2.9**	**-1.3**
Real unit labour cost				0.2	-0.7	1.7	0.2	**6.2**	**-3.3**	**-2.3**
Saving rate of households (b)				-	-	-	-	**-**	**-**	**-**
GDP deflator				1.5	0.4	-0.1	0.2	**-1.4**	**0.4**	**0.9**
Harmonised index of consumer prices				2.2	1.1	0.8	0.5	**-1.3**	**0.9**	**1.3**
Terms of trade goods				-0.4	1.2	-1.2	-1.4	**-1.1**	**0.5**	**0.2**
Trade balance (goods) (c)				-14.0	-11.3	-12.6	-13.1	**-12.2**	**-12.7**	**-13.0**
Current-account balance (c)				-8.4	-1.5	-3.1	-1.7	**-6.2**	**-6.4**	**-4.8**
Net lending (+) or borrowing (-) vis-a-vis ROW (c)				-6.7	-0.3	-2.1	-0.6	**-4.8**	**-4.9**	**-3.2**
General government balance (c)				-7.8	0.7	1.0	1.5	**-6.9**	**-6.3**	**-3.4**
Cyclically-adjusted budget balance (d)				-5.7	5.5	4.6	3.9	**-0.4**	**-2.4**	**-1.1**
Structural budget balance (d)				-	5.2	5.2	2.8	**-0.1**	**-2.6**	**-1.1**
General government gross debt (c)				135.5	179.2	186.2	180.5	**207.1**	**200.7**	**194.8**

(a) as % of total labour force. (b) gross saving divided by adjusted gross disposable income. (c) as a % of GDP. (d) as a % of potential GDP.