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GREECE Outlook 2021E: Patience is necessary

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2021E:
In a nutshell

- The economy is suffering deeply from the protracted disruptions in the tourism industry, but it is benefiting increasingly from FDI inflows and improvements in the manufacturing sector.
- Third-quarter GDP was marginally above our expectations, thanks to household consumption moving back to positive yoy growth. However, monthly surveys show that consumption fell back in 4Q and will most likely stay weak in 1Q. As a result, we expect to see a deep contraction in real GDP until 2Q, when the base effects should at least bring GDP, on a yoy basis, back to positive territory.
- In our view, a realistic expectation on the number of tourists reaching Greece in 2021E is one-third of 2019; alas, this keeps a lid on consumption and the aggregate profits for small companies. That said, we are beginning to see evidence of a pick-up in EU-related funds in the BoP, there is growing evidence of a strengthening and broadening FDI pipeline, and there are encouraging signs in the manufacturing sector.

2021E: In a nutshell

Also, importantly, as the unemployment rate appears to be at its peak and there is a modest wage increase trend, real aggregate incomes are rising rather briskly – around 3% – which supports consumption even in these unfavourable circumstances.

- Prices reached 2% deflationary levels, with core inflation below -1% in the past few months; we do not expect any inflationary risk in the medium- to long-term, as the economy faces a negative output gap. House price inflation slowed down from its peak to levels around 4% yoy; we believe the moratoria extension (until December 2021E) should help house prices avoid moving into negative territory.

- This year, Greece is eligible for approximately 4% of GDP in SURE and EU Recovery Funds. We assume that EU sources and FDI will lead investment spending going forward, while we stress that, in the aggregate, non-financial corporate balance sheets remain very weak.

- Structurally, Greece is lagging its Eastern EU peers in terms of digital infrastructure and human capital. This does not preclude a rise in FDI-related investment in services, but suggests to us that the wage level is likely to remain very contained in the next few years – lagging the CE3.

Note: this is an extract of our Greece 2021 outlook, if you would like to discuss Greece in detail please contact us.

Key points

- We expect the unemployment rate to drop slowly, going forward, even under modest tourism revenues assumptions, as the effects of EU funds and FDI reveal themselves, going forward.

- The twin deficits are wide and will remain wide: the budget and current account deficit are significant relative to GDP, and we caution that we may not see much consolidation in 2021E nor 2022E. However, funding is likely to be more than comfortable, given the EU support.

- We expect inflation to be non-existent over the full forecast horizon, which is somewhat troubling for the public finance outlook, in our view . That said, evidence signals a genuine improvement in trend growth going forward, in line with what was expected pre-COVID-19.

Cyclical momentum

- January's economic sentiment index fell mildly, but reported improvements everywhere, bar in industry
- We forecast 2021E real GDP at 3.6%, accelerating to 5.3% in 2022E, assuming that tourism remains heavily impaired this year, but investment is robust, thanks to external funding
- NFC lending moving towards positive levels in yoy terms, while lending costs are close to the 2009 lows. Households' lending remains low
- Deflation in the core component: we do not expect any inflationary risks in the next two years
- Housing market: prices in positive territory and moratoria (until December 2021E) should equal the avoidance of deflationary risk

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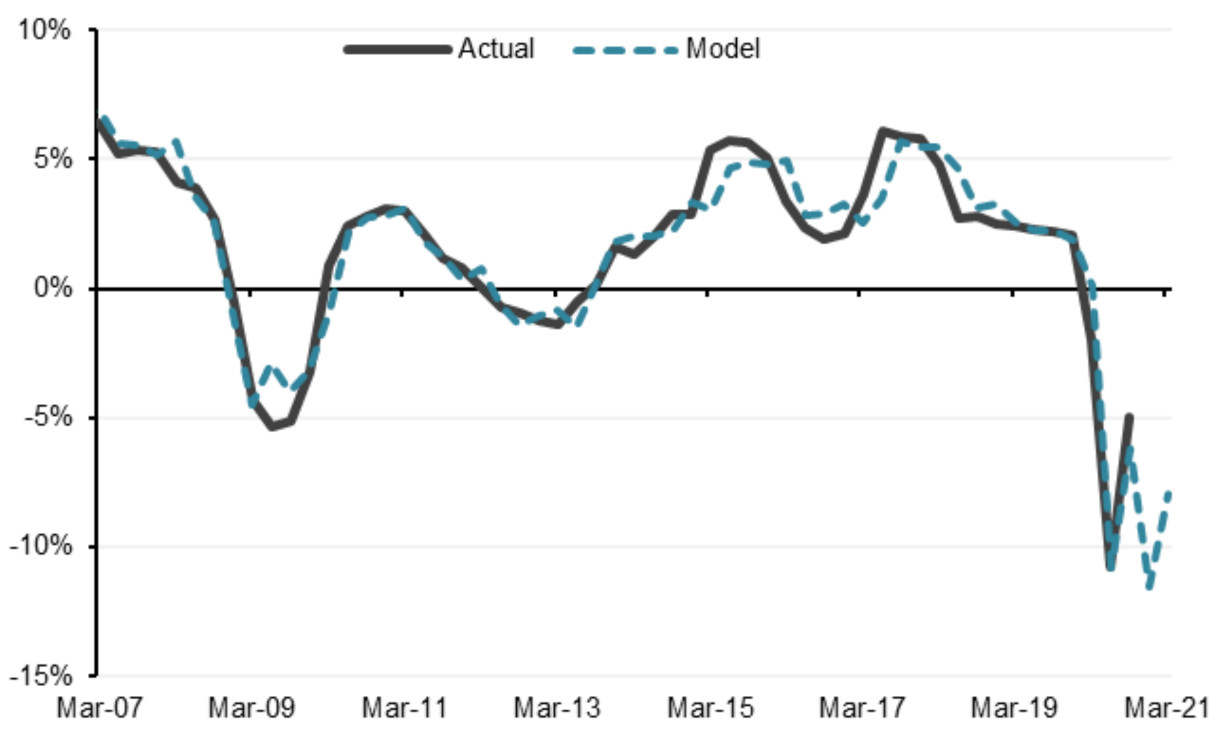
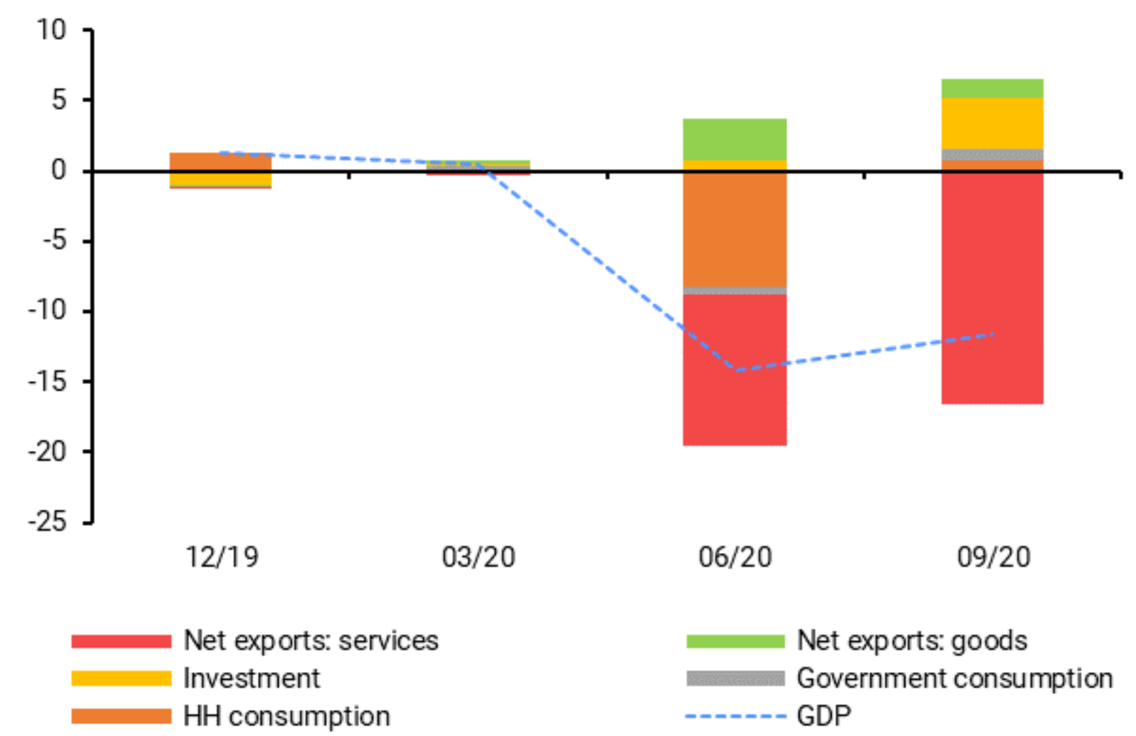
GDP prospects in the near term: the worst is not over yet

- Our model suggests that, *de facto*, the economy will contract at a double-digit pace on a yoy basis in 3Q20, 4Q20 and 1Q21. Part of the reason for the correction is a heavy drag from net exports, while investment is performing well, given the circumstances, and consumption is constrained by lower tourism revenues.

Projected 4Q21E real GDP yoy growth, sentiment induced



Real GDP growth: components



Sources: ADA Economics, CEIC

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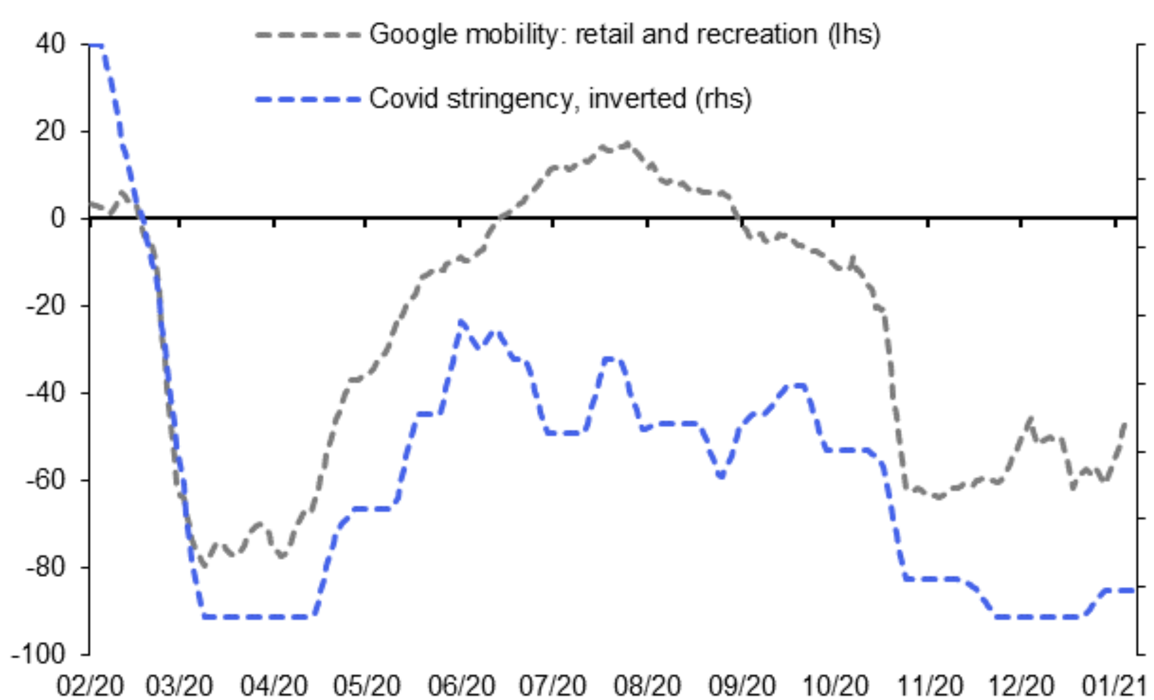
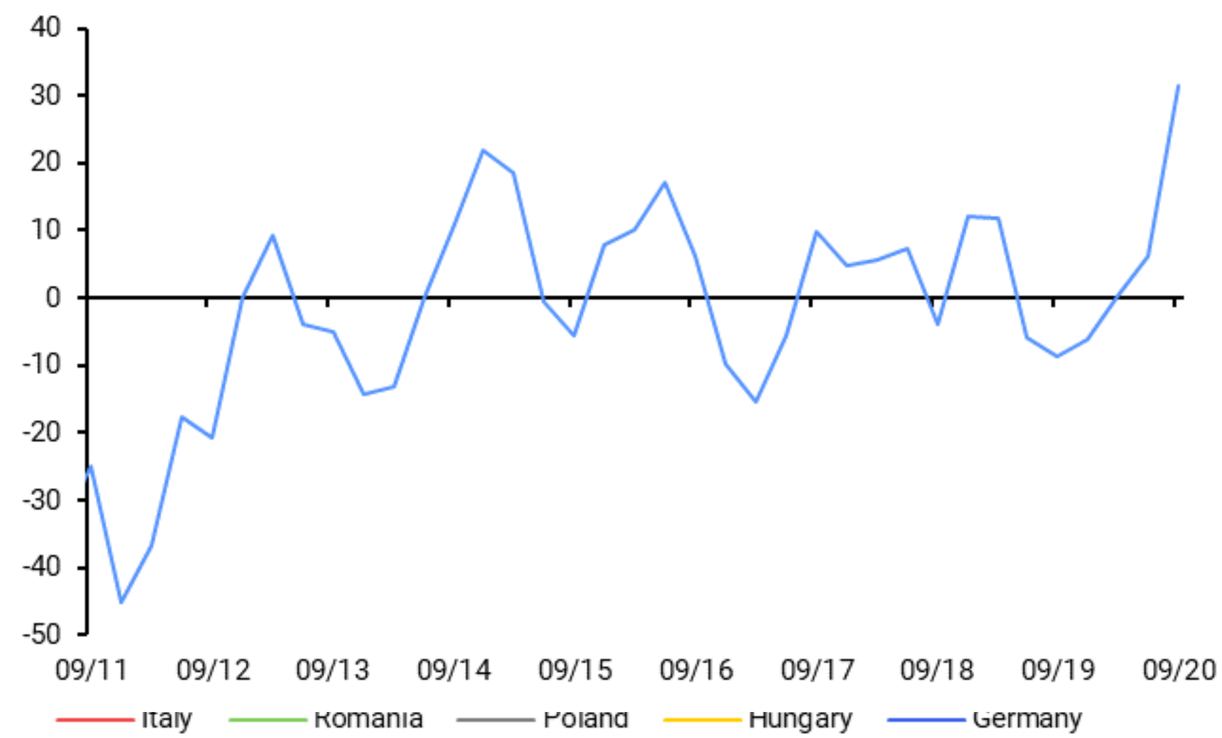
GDP prospects in the near term: the worst is not over yet

- Greece, currently, has mobility restrictions close to the April-May levels; which results directly in a strong decline in retail mobility.
- Investment levels are significantly higher than in 2019, unlike most of its European peers.

High frequency indicators, COVID-19 related restrictions



Investment (GFC) growth, yoy



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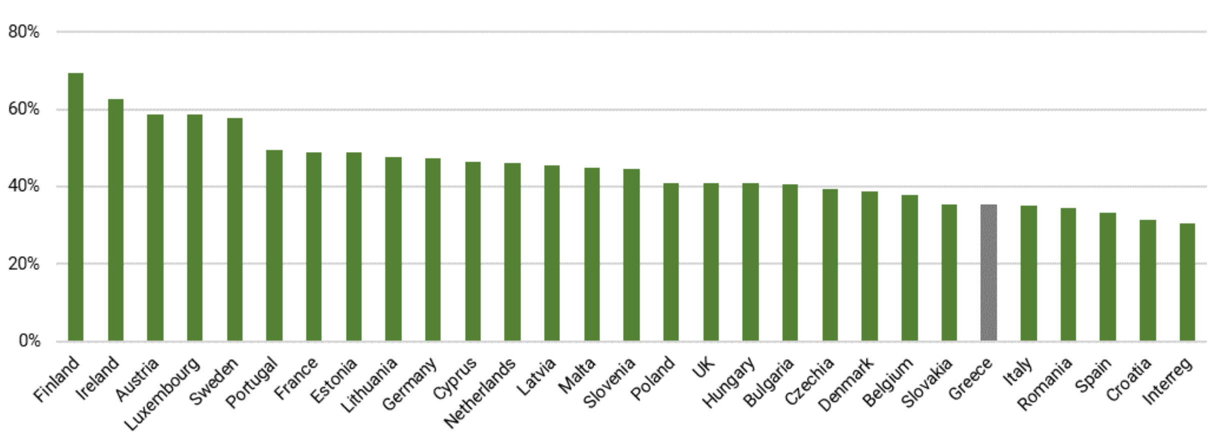
EU Fund support: historically weak, but beginning to improve

Funds spent, % of planned (2019)



Net capital inflows, EUR bn, showing some acceleration recently

Sources: Bank of Greece, EU Commission

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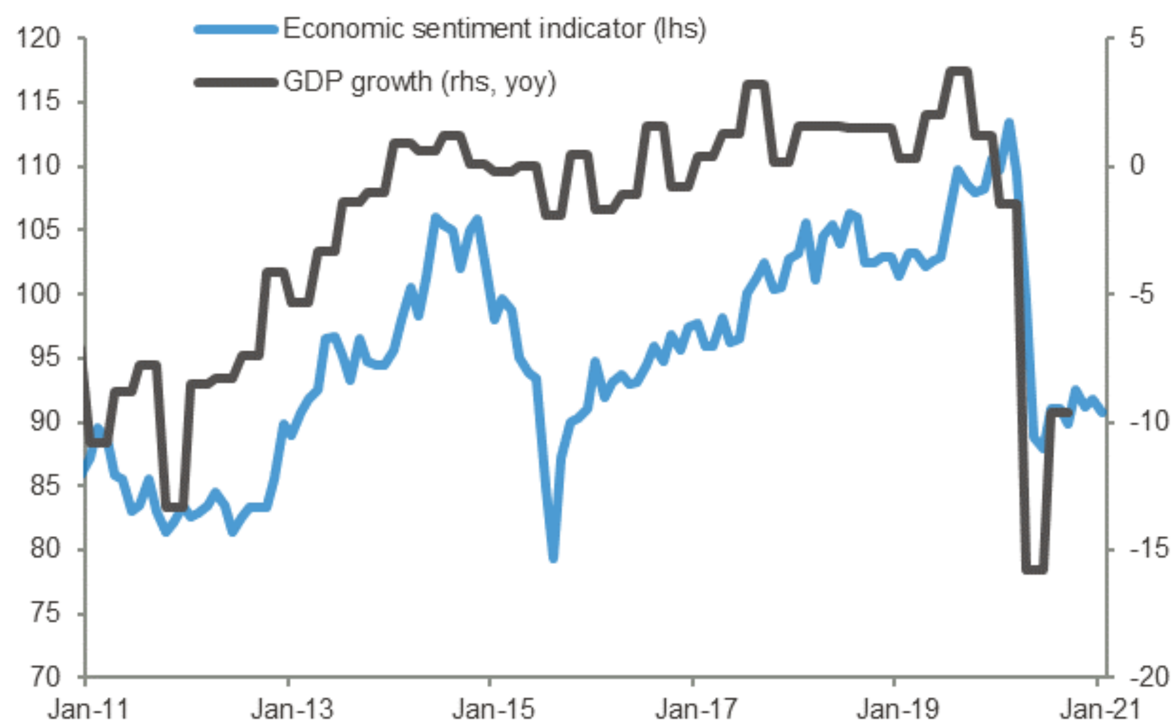
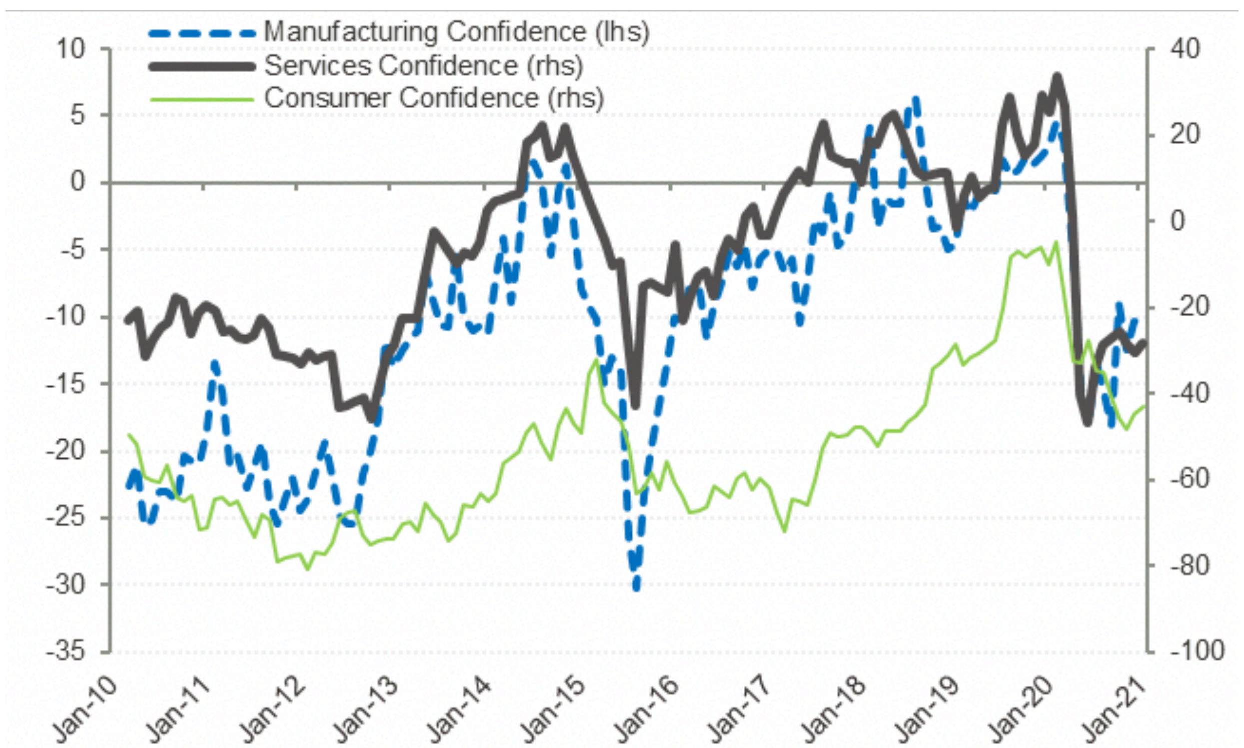
GDP prospects in the near term: the worst is not over yet

- The ESI softened in January 2021, after having moved on a frail sideways trend since September last year.
- Among the components, construction confidence registered the highest gain of +18.5pts, supported mainly by a sharp pick-up in order books, followed by services confidence (+3.2pts), which was helped by better demand related expectations and an abrupt pick- up in hiring intentions. Consumer confidence also posted a gain in January, but at a weaker pace than was seen in December 2020 (+1.5pts vs. +3.6pts), buoyed mainly by a firm recovery in spending appetite and the assessment of better saving buffers at present.

Economic sentiment indicator



ESI: components



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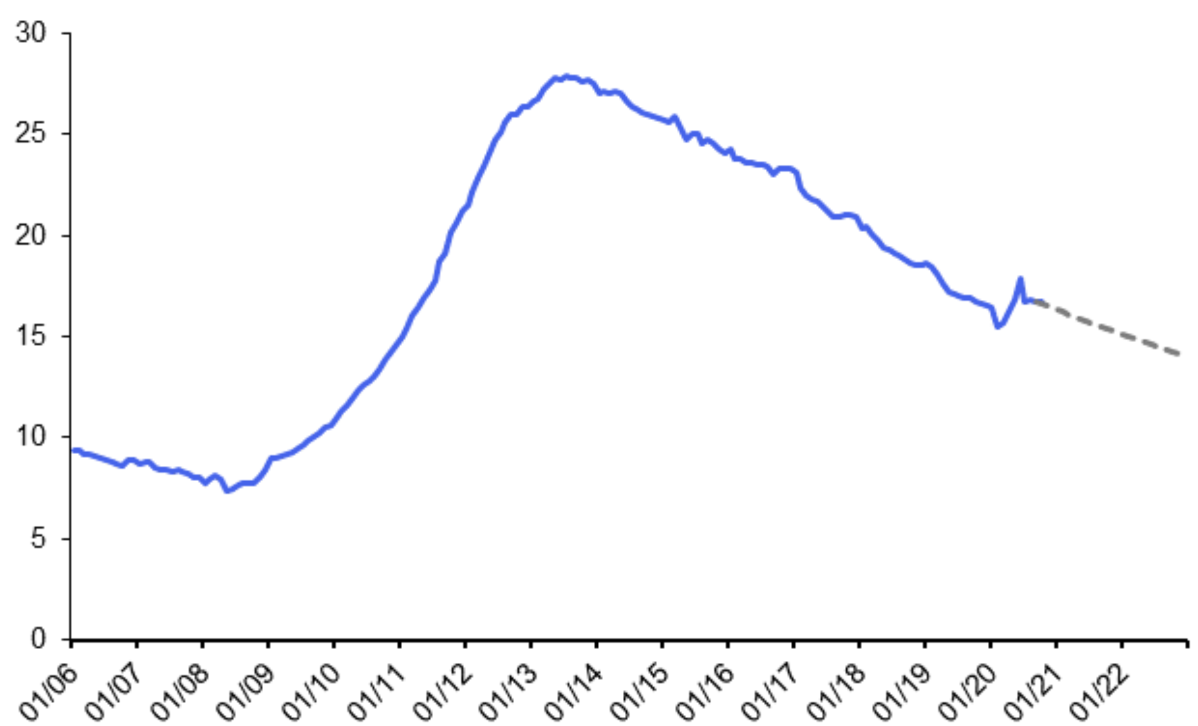
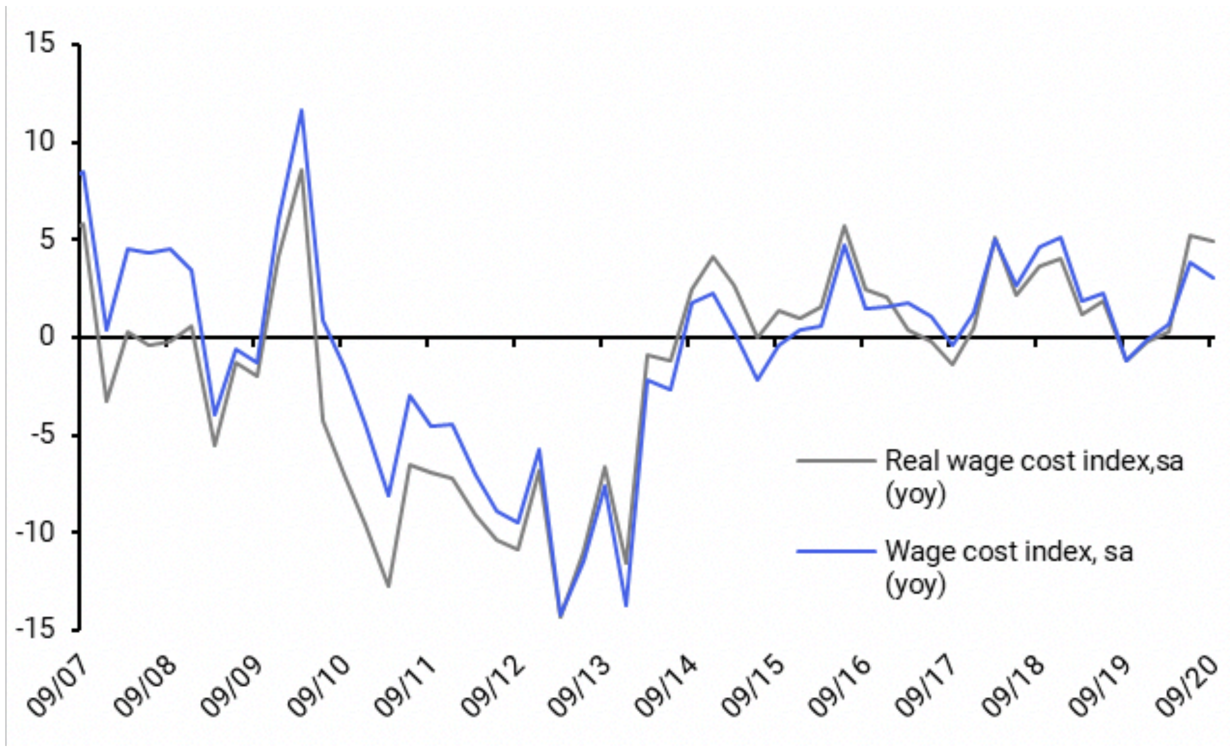
Labour Market

- The unemployment rate (seasonally-adjusted) remained at 16.7% in October, staying roughly flat since July, following a short-lived surge to 17.9% in June.
- Employment began to recover in September 2020 on a yoy basis. Currently, the surveys are not yet strong enough to signal a robust labour recovery, but there are initial indications that EU funds absorption is improving and FDI is brisk, which should lead, in our view, to a recovery in unemployment going forward, even with modest tourism.

Unemployment rate projection



Wage dynamics



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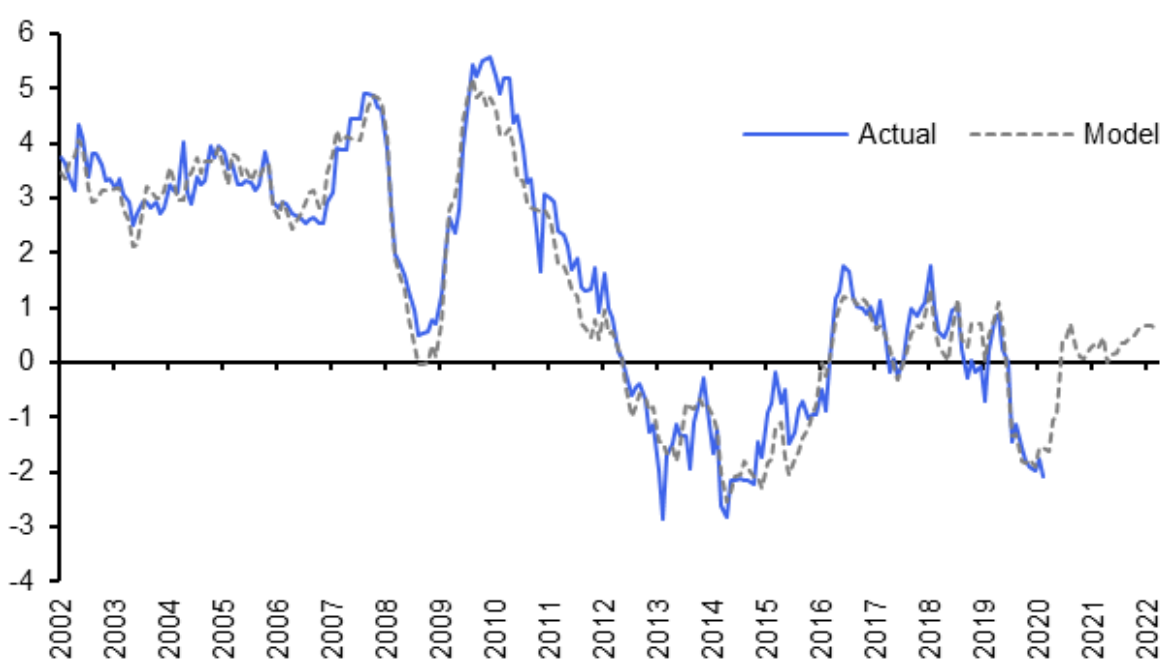
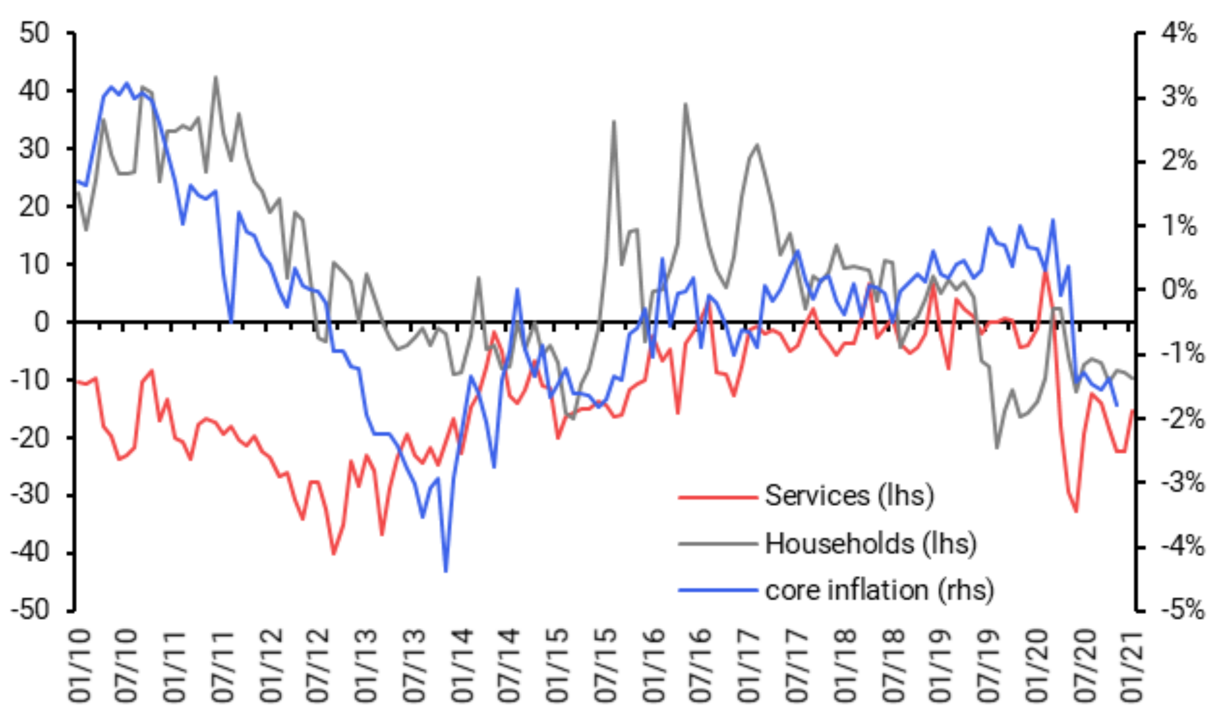
Inflation dynamics

- Inflation has been around -2% yoy in the past few months, levels relatively close to its 2012-14 lows. The current print is a combination of: negative transport inflation; deflationary pressures from low demand; and the impact of temporary tax cuts to support the most affected sectors. We believe inflation is likely to be below 1% in the medium term, as pricing expectations remain at negative levels and the economy at a negative output gap.
- We forecast inflation, on average, at 0.1% in 2021E and 0.4% in 2022E.

Inflation model



Businesses' pricing expectations and core inflation

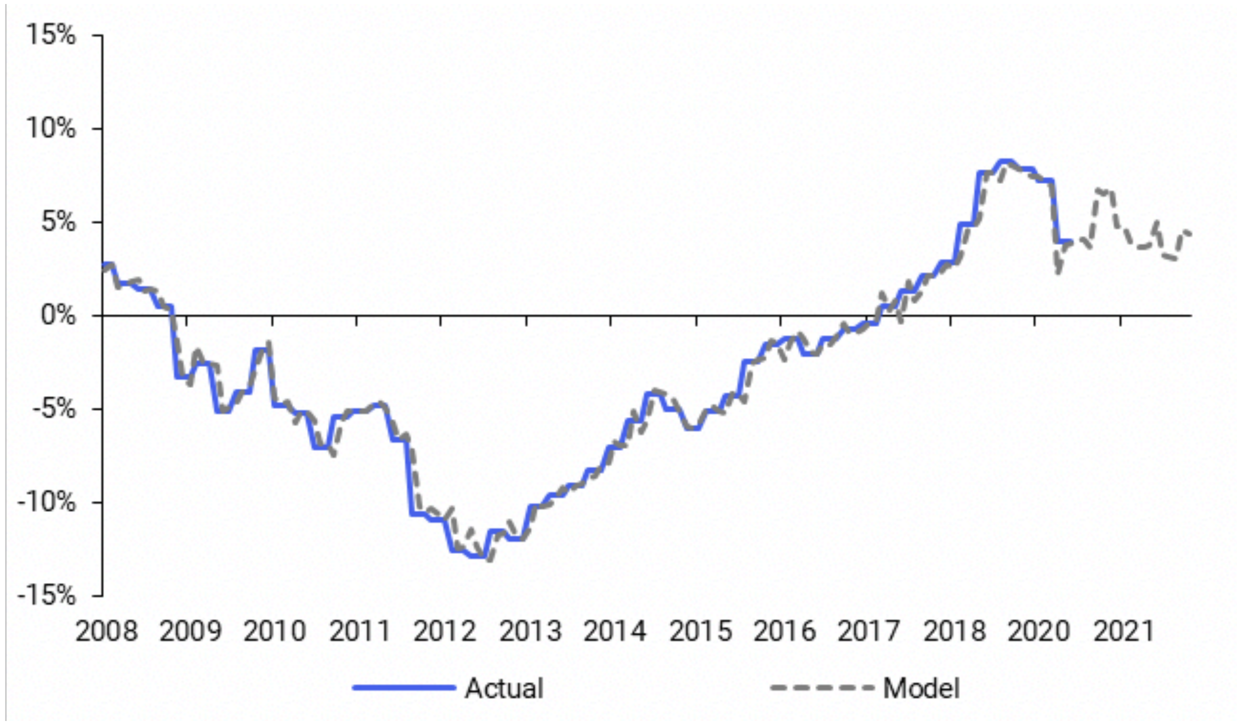


Sources: ADA Economics, CEIC

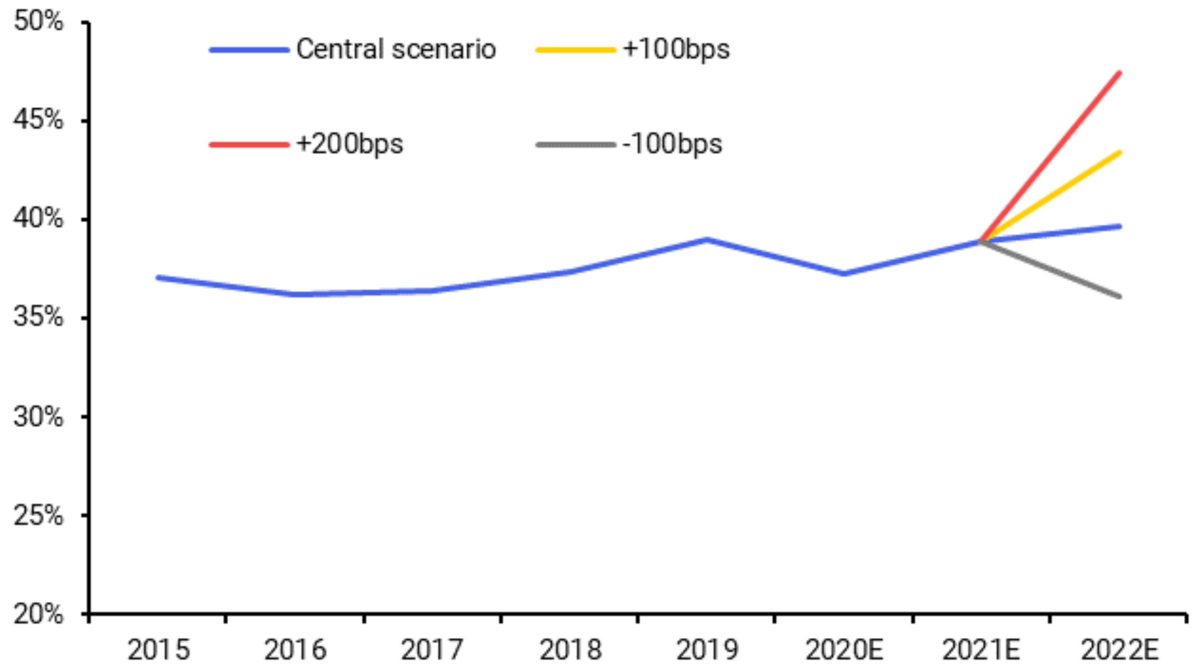
House prices affordability

- House prices softened from the 8.3% yoy high in 2019 to 4.0% yoy in 2Q20E; while prices rose 2.1% in the first half of the year vs. the end of 2019. Our model projects house inflation around current levels in the medium term. We believe that the loan moratoria, extended until December 2021E, should support the market temporarily.

House prices



Housing affordability



Sources: ADA Economics, CEIC, Bank of Greece, NUMBEO

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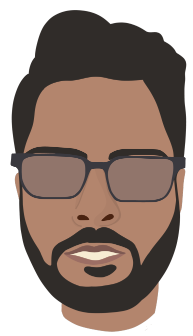

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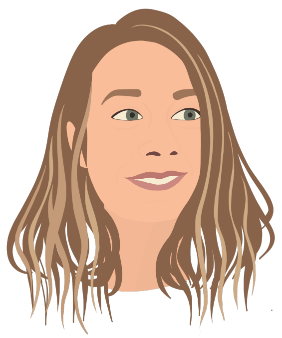

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