Macro Keys – Economics

Greece: more headwinds - but overall we remain constructive

Economics

Global

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We lower our 2022 GDP forecast to 4.0% - but remain above consensus

Compared to our view in March, we acknowledge more headwinds to growth in Greece. As a result, we lower our GDP growth forecast to 4.0% in 2022 from 5.5% previously. This mainly reflects four forces: a) smaller growth carry-over from 2021; b) downward revision of Eurozone growth to 2.9% in 2022; c) high frequency data implies a softer start to Q1 2022; and d) inflation is becoming a bigger drag on growth. Nevertheless, our new GDP forecast remains above the recent official projections of 3.5-3.8% (IMF, Bank of Greece) and analyst consensus of 3.2%. Key downside risks are: higher commodity/energy prices and further hit to Eurozone growth and confidence.

Key headwinds to growth

We discuss there downside drags on Greek growth in detail. First, GDP growth eased notably to +0.4% q/q in sequential terms in Q4 2021 with downward revisions to Q3 and Q2 pace. Slower growth reflected weakness in construction and several services and could be also related to tighter mobility restrictions in Q4 2021. This has reduced the carry-over into 2022 to 1.6%. Second, in sequential terms, all of the three high frequency indicators that we follow contracted so far in Q1 vs Q4 2021: industry (-3.2% q/q), retail sales (-1.1% q/q) and car registrations (-1.7% q/q). However, there is no high frequency data on many services, where business sentiment showed further improvement. This makes it possible that Q1 GDP growth could also be modest in sequential terms. Third, Greece's harmonised inflation rose to 8.0% y/y in March, the highest pace since 1996. The pace of HICP almost doubled in three months versus 4.4% y/y in December 2021. More than 40% of the acceleration in HICP in January-March is explained by the housing component (including electricity and gas charge), while another 40% is explained by the jump in food inflation (8.2% y/y) and the rise in hotels & restaurant charges (5.2% y/y).

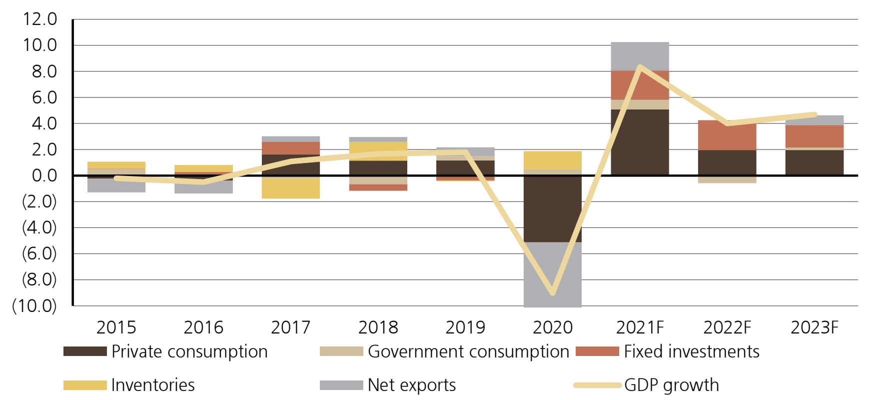
Factors underpinning our still optimistic macro view

We highlight four factors in detail in the note. First, both mobility and activity data point to visible improvements in January-April 2022and business confidence in Q1 reached the best reading since 2000 - aided by industry, services and construction sentiment. Second, labour market improvements remained intact in January-February and the increase in minimum wages should help with household income dynamics. In addition, households have some buffers (increase in deposits) to deal with higher inflation and the government has also mobilised new resources to help. Third, EU fund inflows should continue to be a key factor this year with around EUR 16bn or 8% of GDP available for absorption from the RRF and MFF. Fourth, tourism revenues continued to perform very well in January-February (revenues up 300%), and the earlier start of the season (1 March) and the easing of mobility restrictions between May-August should allow the sector to record solid gains again.

Better fiscal starting point in 2021; public debt should fall visibly in 2022-23

Eurostat's release on the 2021 budget deficit and public debt showed a visibly better picture than expected with the primary deficit of -5% of GDP (vs -7.3% target) and public debt easing to 193.3% of GDP. For 2022 the government now expects a primary deficit of c-2% of GDP (up from -1.2% of GDP previously) and recently adopted a supplementary budget to help households with energy prices. Importantly, tax intakes grew at a healthy clip in Q1 2022. We expect public debt to fall further towards (or even below) 180% of GDP by 2023. Greece's sovereign credit ratings got raised to just below investment grade by DBRS and S&P this year.

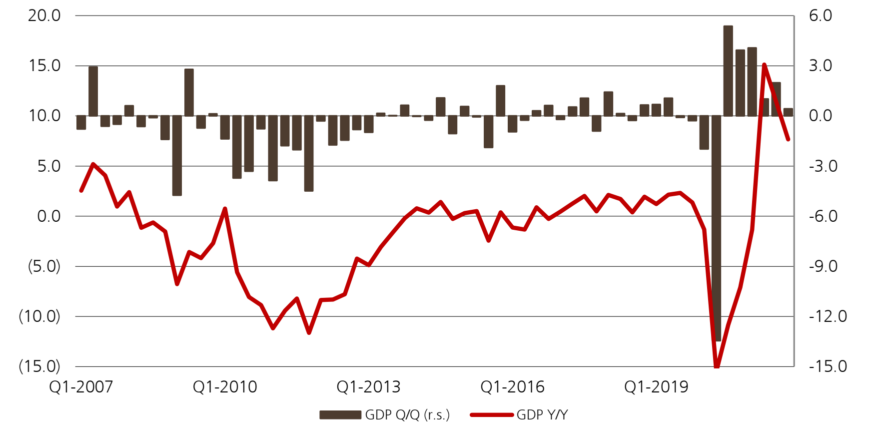
Figure 1: Lowering our 2022 GDP forecast to 4.0% from 5.5% - but remain above consensus



Source: ELSTAT, Haver, UBS

Compared to our view in [March](), we acknowledge more headwinds to growth in Greece. As a result, we lower our GDP growth forecast to 4.0% in 2022 from 5.5% previously. This mainly reflects four forces: a) smaller growth carry-over of 160bps from 2021; b) [downward revision of Eurozone growth]() to 2.9% in 2022; c) high frequency data implies a softer start to Q1 2022; and d) inflation is becoming a bigger drag on growth. We believe the economy will benefit this year from: a) the inflow of EU funds, b) further rebound in tourism, and c) policy measures like the minimum wage hike and additional fiscal support. Our new forecast remains above the recent official projections of 3.5-3.8% and analyst consensus of 3.2%.

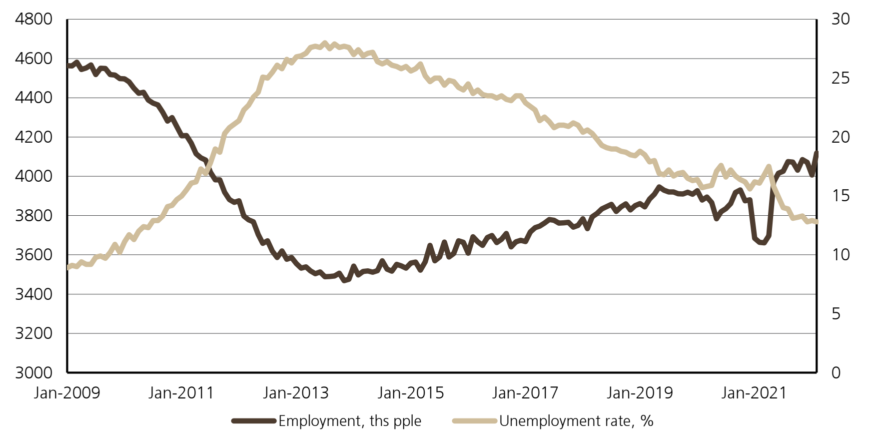
Figure 2: Soft sequential growth in Q4 2021



Source: ELSTAT, Haver, UBS

GDP growth eased notably to +0.4% q/q in sequential terms in Q4 2021, following a downwardly revised 2.0% q/q in Q3 and 1.0% q/q in Q2 (previously 2.7% and 2.1%). In year-on-year terms growth also eased to 7.7% y/y from 11.4% y/y in Q3 2021. Gross value-added dropped by -0.2% q/q, reflecting a sharp decline in construction (-19.6% q/q) and several services value-add (IT& communication, finance and real estate) despite gains in industry and trade. In addition, tighter mobility restrictions due to the Omicron wave and declining mobility in the quarter could have also held back growth. As a result, the growth carry-over into 2022 is around 100bps lower at 1.6ppt than what we expected in March.

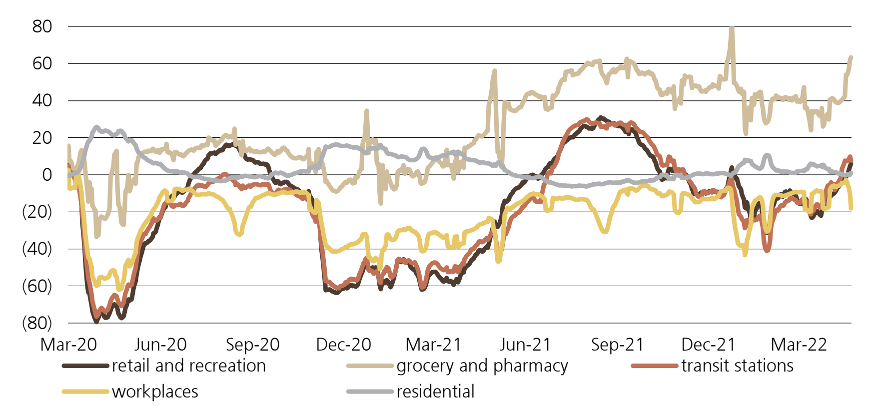
Figure 3: Labour market recovery continued in Q1 2022, continues to buttress consumption



Source: ELSTAT, Haver, UBS

Improving labour market conditions remain a key support factor to our constructive macro view on Greece. The unemployment rate dropped to 12.8% (seasonally adjusted) by February 2021, the lowest level since 2010. Employment reached 4.12mn in February 2022: up by an impressive jump of 12.4% y/y and posting the highest reading since Q1 2011. Nevertheless, the number of people in the labour force was yet to recover to pre-pandemic levels. We look for 6.5% increase in employment in 2022. In addition, wage growth is likely to receive a boost from the two increase in minimum wages: 2% from 1 January 2022 and a combined 9.7% from 1 May (vs 2021). The minimum wage increase should affect c650k people directly (c16% of employed).

Figure 4: Mobility started to rebound in 2022, further easing of restrictions from 1 May



Source: Google, UBS. https://www.google.com/covid19/mobility/

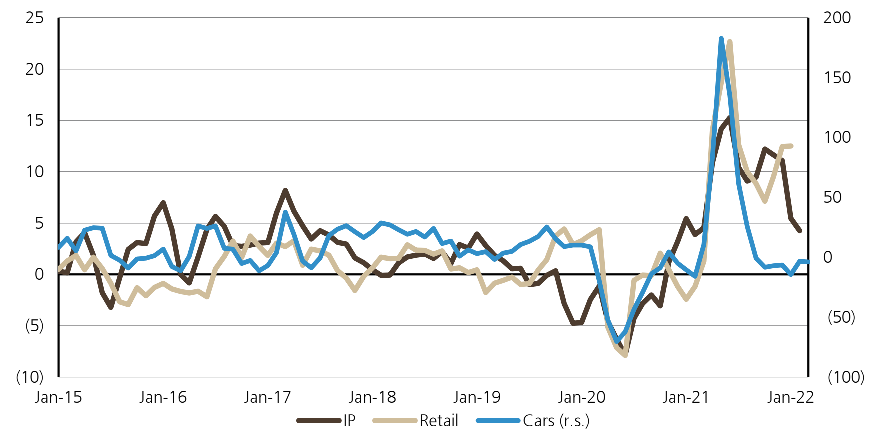
Greece started to ease mobility restrictions from January onwards as Covid-19 cases started to drop – see our [mobility restrictions tracker](). From 1 May until end of August - i.e. during the main tourist season - there would be no restrictions on occupancy rates in restaurants, shops and sport venues. 71% of Greece's population has been fully vaccinated, with 55% of population having received a booster shot. Google's mobility data points to a recovery in activity in January-April (levels are above corresponding 2020 and 2021 prints). This mainly reflects improved mobility for retail and grocery spending and transit stations.

Figure 5: Business sentiment most optimistic since 2000 despite the Russia/ Ukraine situation

Source: European Commission, Haver, UBS

Business sentiment improved in Q1 2022, with an average level of 113.8. Q1 business sentiment was at the highest level since December 2000. Business sentiment only marginally deteriorated in March (to 113.2 from 114 in February) - this was the first month to reflect the potential impact of Russia's invasion of Ukraine. Improving sentiment was led by industry (PMI also reached 56.8 in Q1) and services, where levels were not far off from all-time highs. The optimism in construction (best reading since 2006) could reflect the inflows of EU funds (RRF+MFF). However, sentiment in the retail sector and consumer confidence are yet to climb back to pre-pandemic levels.

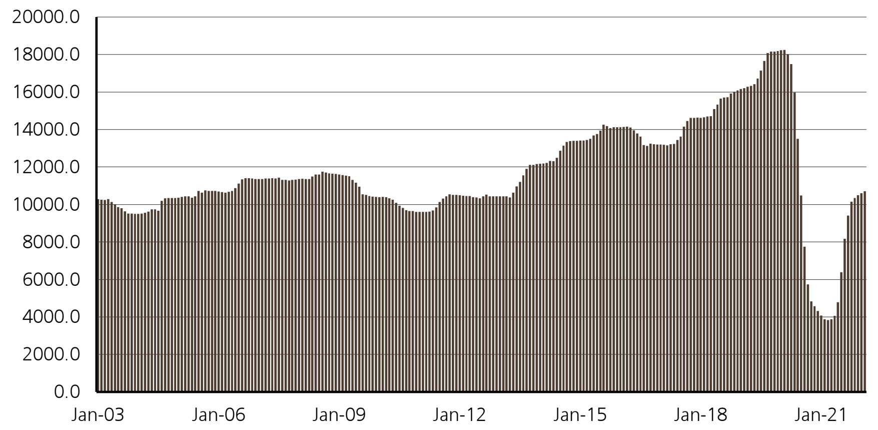
Figure 6: High frequency data for Q1 (% y/y) suggests a more cautious picture than soft indicators



Source: ELSTAT, Haver, UBS

It is important to point out that high frequency economic data paints a more cautious picture than the very positive message of business confidence. In sequential terms, all of the three indicators we follow contracted in Q1 vs Q4 2021: industry (-3.2% q/q), retail sales (-1.1% q/q) and car registrations (-1.7% q/q). The slowdown is also visible in y/y comparison. True, there is no high frequency data on many services, where business sentiment showed further improvement.

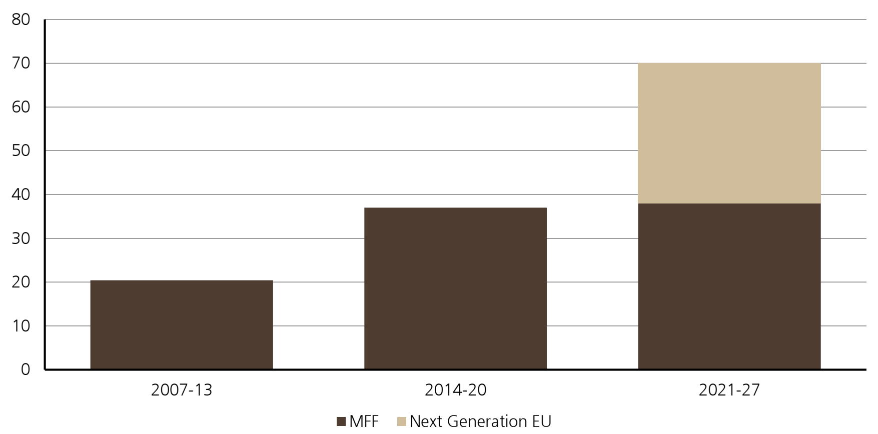
Figure 7: We continue to expects further normalization in tourism revenues in 2022* (EUR mn)



Source: Bank of Greece, Haver, UBS. *12-month rolling.

Greek tourism revenues started to rebound in at a fairly rapid clip since April 2021. Last year tourism revenues reached EUR 10.5bn or 58% of the peak 2019 revenues. The first two months of 2022 actually delivered strong momentum in tourism receipts with revenues up by c300% y/y. Given the backdrop of slower growth and higher inflation in the Eurozone, there is a worry whether tourist arrivals from Europe could be more negatively affected. Greece started the tourism season in early March this year and [anectodal evidence points to results coming through](). While we see further normalization, we remain doubtful whether the 2019 revenues could be realized this year (in line with [recent official indications]() aiming for 80% of 2019 revenues).

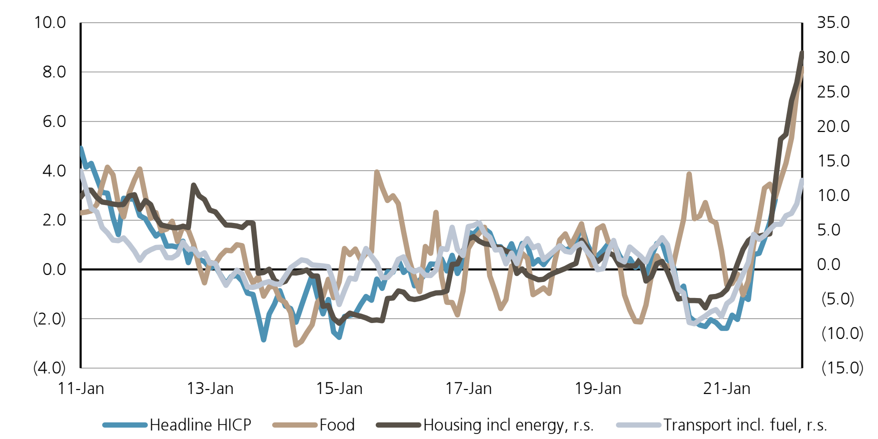
Figure 8: Available EU fund sources (EUR bn) – this year the focus is on the leftover from 2014-20 MFF



Source: European Commission, UBS. MFF stands for the Multi-annual Financial Framework. The largest part of the Next Generation of EU funds is the RRF.

Despite the focus on the Resilience and Recovery Facility funds, it is important to point out that the most important source of EU fund inflows this year are the leftover funds from the 2014-2020 cohesion funds (MFF). [EC data shows]() that Greece has more than EUR 11bn available for absorption in 2022, while for 2022 the government targets to receive EUR 5.3bn from the RRF. (Greece has approved projects to cover 129% of the MFF envelope.) The EC endorsed preliminarily the request to pay out EUR 3.6bn (EUR 1.7bn in grants and EUR 1.9bn in loans). Nevertheless, going forward the RRF is going to become more important in terms of total EU fund mix.

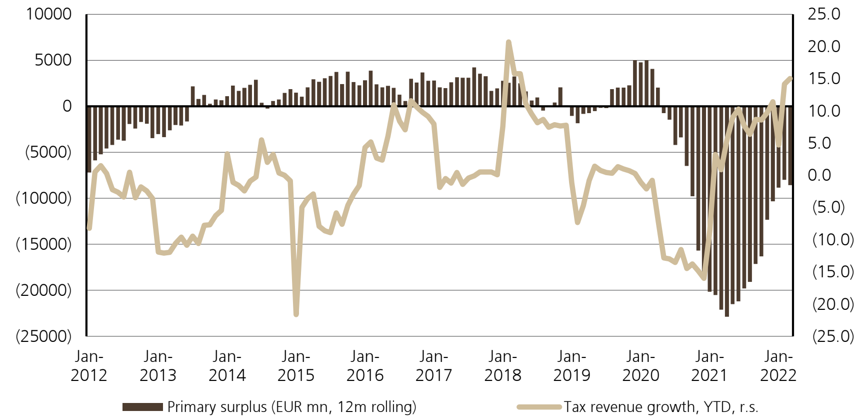
Figure 9: Elevated inflation takes a toll on households (% y/y)*



Source: EuroStat, Haver, UBS. *HICP

Greece's harmonised inflation rose to 8.0% y/y in March, the highest pace since 1996. The pace of HICP almost doubled in three months versus 4.4% y/y in December 2021. More than 40% of the acceleration in HICP in January-March is explained by the housing component, in particular the pick-up in electricity charges by 79% y/y in March (gas tariffs were up by 127% y/y). Another 40% is explained by the jump in food inflation (8.2% y/y) and the rise in hotels & restaurant charges (5.2% y/y). We believe that average inflation could reach around 5.5% in 2022, with year-end inflation around 3.5% y/y - a clear drag on consumption. The elevated savings of households - as reflected by the c10% of GDP increase in deposits in 2020-22 - should provide some buffer.

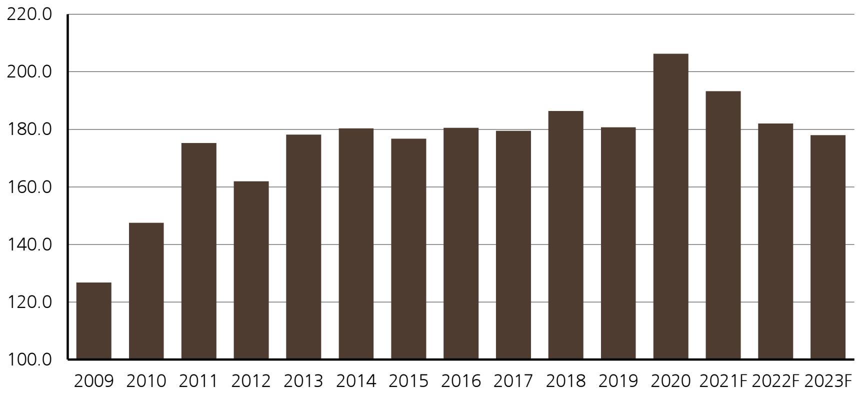
Figure 10: 2021 budget outperformance; challenging 2022 backdrop



Source: Ministry of Finance, Haver, UBS

Greece registered a primary budget deficit at -5.0% of GDP in 2021, versus the -7.3%of GDP target and the EC's latest projection of c-6% of GDP primary deficit. The 2021 outperformance is important, given the pressures coming up for this year's budget. Although tax collection remained strong in Q1 2022, the primary deficit reached EUR 1.65bn versus the EUR 1.33bn target (though admittedly it was influenced by the delay in releasing the RRF payments). In addition, the government now foresees c-2% of GDP primary deficit in 2022 and had an EUR 2.6bn worth of supplementary budget approved in April, aimed at protecting households from energy costs. The government now puts the total costs of social protection measures at EUR 4bn or 2.1% of GDP so far this year.

Figure 11: Public debt on an improving trajectory; sovereign upgrades started to come through



Source: Ministry of Finance, Haver, UBS

Public debt has declined to 193.3% of GDP in 2021 (better than expected) from 206% of GDP in 2020. In our view, public debt should drop further to below 180% in 2023. Greece has repaid the IMF in full in April, savings around cEUR 0.2bn in debt service costs. The government also has a cash buffer of EUR 35bn at the Bank of Greece. This year both DBRS and S&P raised Greece's credit rating by notch to BB (high) and BBB+ respectively, just below investment grade. Fitch also raised Greece's outlook to positive. Greece already raised EUR 3bn out of the planned EUR 12bn borrowing on the markets this year (including a green bond) in January, and mandated banks for a re-opening of a 7-year bond.

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