GREECE
In Greece, debt and deficits climbed to precipitous levels. The massive spending increases behind this drove up wages and prices, badly undermining competitiveness, and setting the stage for the crisis.
1. Design of the SBA
Fiscal adjustment was expected to boost market confidence and restore financing.
Structural reforms were designed to improve competitiveness and trigger an export-led recovery. (which would help reduce the impact of fiscal adjustment).
2. SBA IMPLEMENTATION

Experience and outcomes
Competitiveness problems have proven less tractable, and the recession has proven deeper than expected.
Significant fiscal adjustment, but soaring debt and spreads…

**Primary Deficit (percent of GDP)**

- **SBA Request**
- **5th Review**

**Gross Public Debt (percent of GDP)**

- **SBA**
- **5th review**

**GGB Spreads over Bunds (percent)**

- **2-Year**
- **10-Year**

Program dates:
- Dec'07
- Dec'08
- Dec'09
- Dec'10
- Dec'11
3. The new EFF program

Policy Adaptation
The new program places emphasis on directly securing faster competitiveness improvements to bring forward the recovery.
Additional financing, including via debt relief, provides Greece with time to restore external sustainability.
Fiscal adjustment has been slowed down and debt relief has placed public debt on a better (but still risky) trajectory.

[Graph showing primary fiscal deficit and debt as a percentage of GDP over years 2007 to 2019.]

SBA request, EFF baseline, SBA-5th review, EFF alternative scenario.
Portugal
Problem 1: Unsustainable fiscal policies

Primary Government Spending (ratio to GDP)

- Blue line: In percent of GDP
- Red line: In percent of potential GDP

General Government Debt, 2010 (ratio to GDP)

- Spain
- EA
- Ireland
- Portugal
- Italy
- Greece
Problem 2: High corporate, household and financial sector indebtedness
Problem 3: Loss of competitiveness, resulting in low-growth and a high current account deficit

Unit Labor Cost Change (Total Economy), 2001-08 (percent change)

Unit Labor Cost Change (Manufacturing), 2000-08 (percent change)

1/ Negative = increase in labor productivity.
Pillar 1: Fiscal Solvency

Magnitude and Timing of Fiscal Adjustment in Euro Area
(change in structural primary balance as percent of GDP)

1 Since structural adjustment started -- between 2009 and 2012 depending on the country (2011 for Portugal).
Pillar 2: Enhancing Growth and Competitiveness

OECD Employment Protection Index, 2008

Source: OECD. 2009 data for Portugal and France.

Labor Cost Index 2008 =100, y/y % change

Annual average

Source: OECD. 2009 data for Portugal and France.
Pillar 3: Private Sector Deleveraging

Loan to Deposit Ratio, end 2010
(Percent)

Credit and Real GDP growth
(Percent)

Private credit (percent change, rhs)
Real GDP (percent change, rhs)
11-months into the program, some encouraging signs…

Output Loss and External Adjustment, 2007-2011

Change in the current account: 2011-2010
So far so good, but significant challenges ahead

**Alternative Scenarios (percent of GDP)**

- Deeper recession (2012-14)
- Potential growth at 1 percent
- Extreme scenario: potential growth at 1 percent (nominal primary expenditure unchanged compared to baseline)

**Public Debt (percent of GDP)**

- Program Request
- Third Review
Ireland
Pre-Program Policy Response was Substantial but
Bank Funding Runs Force Program in late 2010

**Bank Funding Outflows**
(Euro billions)

- Debt securities, net repayment
- Deposits, private sector (net outflows)
- ECB liquidity support

**Government Debt, Net**
(Percent of GDP)

- Bank support costs
- Deficits and other debt

- 2008
- 2009
- 2010: 40.2%
- 2011: 55.7%
High Private Debts Increase the Risk of a Pernicious Downward Cycle

- **Fiscal**
  - higher deficit & further tightening
  - fiscal tightening reduces DI

- **Households**
  - High debt to DI ratio
  - HH deleveraging leads to higher saving and weak demand
  - Further weakens HH balance sheet

- **Property market**
  - house price declines

- **Real economy**
  - weak output/income growth
  - Lower HH DI raises debt DI ratio

- **Banks**
  - higher loan losses
  - Banks restrict lending

- **DI** = disposable income
- **HH** = households

DI= disposable income
HH = households
Bank Recapitalization—Credible, Cost Mitigated

Recapitalization (Billions of euros)

Losses and Capital Needs - Existing Capital = Capital Injection Required = Capital Sources

- Additional Capital for Adverse Stress Test Scenario
- Deleveraging Losses
- Loan Loss Forecast (Blackrock)
- Existing Capital and Provisions
- Buffer for post 2013 losses
- Capital for 6% Core Tier 1 end 2013
- Total €24 billion
- Buffer €5.3 billion
- o/w CoCo €3 billion
- Government €16.5 billion
- Private Investments €1½ billion
- LMEs on Sub-debt €16.5 billion

Loan Loss Forecast (Blackrock) = Total €24 billion

€16.5 billion - €5.3 billion = €11.2 billion

Additional Capital for Adverse Stress Test Scenario = Capital Injection Required

Total = €24 billion

Capital Sources = Government + Additional Capital + Private Investments
Deleveraging—Phased, mostly Offshore Assets

Deleveraging, 2011-2013

- **Loan to Deposit Ratio**: 122.5%

- **Non-core Assets**: 180%

- **Core Assets**: End 2010

- **Loan to Deposit Ratio**: 122.5%

- **End 2013**: Non-core

- **Disposals**: Core Assets

- **Net amortization**: Core Assets

- **Impairments and other**: Core Assets

(Euro billions)

(Loan/Deposit %)
Fiscal Consolidation: Front-loaded but Phased (Target 3% Deficit in 2015)

Fiscal Adjustment
(Percent of GDP)

Program Starts

Consolidation measures

Change in structural primary balance

<table>
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<tr>
<th>Year</th>
<th>Consolidation measures</th>
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Positive Experience So Far, But Risks Remain

![Government Debt Graph]

- GDP growth, baseline
- GDP growth, shock
- Debt, baseline scenario, RHS
- Debt, shock scenario, RHS

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<th>Debt Baseline</th>
<th>GDP Growth Shock</th>
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