

## IOBE/FEIR Notes on Economic Facts

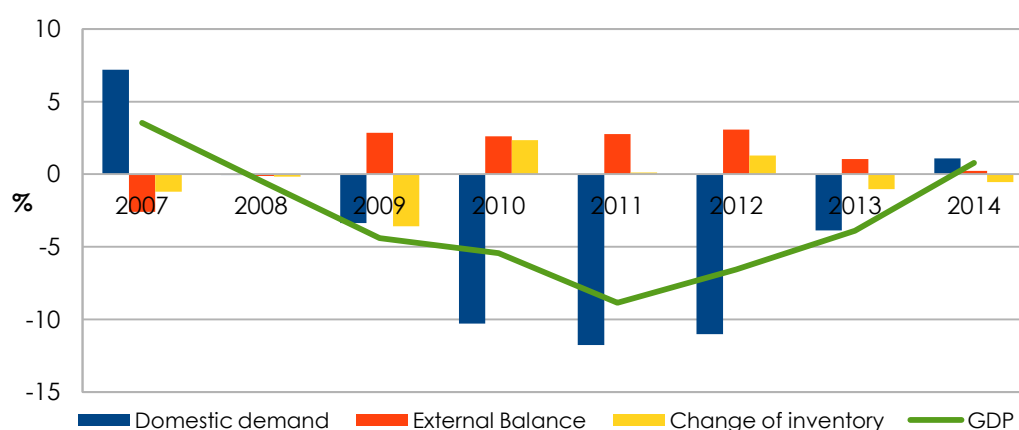
### Recovery of the Greek economy in 2014, with a likelihood of a reversal

March 19<sup>th</sup>, 2015

According to the annual National Accounts statistics released by the Hellenic Statistical Authority on 13 March 2015, Greek GDP (at constant prices) increased by 0.8%, for the first time since 2007. Thereby, it slightly exceeded the 0.6% GDP growth forecasted by the Greek government and the international organisations. **Over the course of the recession of 2008-2013, GDP plummeted by 26.4%. Furthermore, the produced gross value added in 2014 (at 2010 constant prices), was approximately that of the year 2000.**

The **main driver behind the mild Greek recovery of 2014 was domestic demand** (namely, private and public consumption, as well as investments). It increased by 1.1%, for the first time since 2007, while also contributing 1.1% to the growth of GDP. The contribution of the external sector was slightly positive (0.2%), whereas the negative change in inventories reduced the GDP growth rate by 0.5 percentage points. The composition of the demand components that determined GDP growth in 2014 was considerably different than the composition of demand in the period 2009-2013. Over the period 2009 - 2013, the positive contribution of real net exports was substantial mainly due to the decline in imports, while, as opposed to 2014, domestic demand acted as a drag on growth since it carried the burden of the stabilisation effort.

**Figure 1: Contribution of demand components to annual GDP growth (percentage points at 2010 prices)**



**Source:** Annual National Accounts, EL. STAT, March 2015

A more careful look at the Greek economy in 2014 reveals that the **recovery of the Greek economy was primarily the result of an increase of private consumption by 1.3% and the**

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**reinvigoration of the increase in exports (9.0%).** Investments in fixed capital remained meager in 2014 although they grew by 2.6% against a decline by 9.5% in 2013, while **the increase of imports by 7.4% curtailed the improvement of the external balance.** **The increase of private consumption** that was instigated in the second quarter of 2014 **was not based on the main determinants of households' consumption behavior, since disposable income and wealth further declined in 2014.** The increase of consumption, came mostly at the expense of a further decline in the households' saving rate, reflecting the improvement of consumer expectations, as recorded in the IOBE/FEIR Economic Sentiment Indicator. Moreover **private consumption stood at a record high of 72% of GDP, thus signaling that the intended shift of the domestic growth model towards a "new growth model" based on investment and exports is not yet under way.**

**Investments in fixed capital increased slightly,** despite the boost during the last quarter of 2014 by the capitalisation of defense expenditure (as dictated by the ESA 2010 methodology) and the positive impact from public construction. **Investment as a percentage of the GDP stood at 11% in 2014,** as in 2013, a level which is the lowest over the period 1995-2014. Such a level of investment is inadequate to **offset the disinvestment** that has occurred over the past years. An 11% investment rate cannot sufficiently **strengthen the medium-run potential productive capacity of the Greek economy, which has undergone hysteresis as a direct result of the prolonged crisis.**

**Moreover, the substantial increase in exports is a noteworthy breakthrough** that appears to have come to fruition as a result of the competitiveness gains of the previous years. **In particular, exports in other services (mainly software and construction services)** increased by 20% in 2014 (according to the Bank of Greece BoP statistics) and represent 14% of total exports receipts in services. In combination with tourism and maritime receipts, such services are morphing into the driving force behind the private sector driven growth of the Greek economy.

**In light of the components of GDP that triggered the mild recovery of the Greek economy in 2014, it becomes evident that 2014 does not ensure the onset of a sustainable growth path for the Greek economy. The prerequisite for a sustainable growth path is a substantial increase in investment's share of GDP over the medium run.** A recovery instigated by improved consumer sentiment is unsustainable as it spurs consumption and creates demand for imports in the short run, thus limiting the benefits associated with a positive rate of exports. Nevertheless, the modest growth observed in 2014 is an important first step towards growth. Yet, this positive development will be reversed if political and economic uncertainty persists.

The mild recovery of the Greek economy in 2014, coupled with the successful fiscal adjustment, should not downplay the importance of establishing policies that will place the Greek economy onto a sustainable growth path. This sustainable growth path will be achieved through investments in fixed capital, the removal of political and economic uncertainties, as well as the adoption of pro-business reforms so as to attract investments. Furthermore, the transfer of resources into sectors of internationally tradable goods that will increase exports and simultaneously substitute imported goods and services with domestic production is essential in establishing a sustainable growth path for the Greek economy.