Last year, 2019, marked the third year in a row that Greece’s GDP grew by 1.9 percent, surpassing the corresponding EU-28 average GDP of 1.5 percent and the eurozone’s 1.2 percent. The fourth quarter of 2019 was lower than their government’s and the European Commission’s (EC) forecasts, but in line with our own projection (Papadimitriou, Nikiforos, and Zezza 2020). The unemployment rate did not improve in the last quarter, remaining at 16.4 percent, but still recording the lowest rate of the previous 105-month period after recovering significantly from the job losses in the crisis period, especially in the important sectors of tourism and exports, manufacturing, and public administration. Inflation was also kept in check, decreasing in 2019 from 2018 due to decreasing oil prices and reductions in indirect taxation. There were other positive signs registered in 2019 in both the business and consumer confidence indices, which marked their highest values since 2001 while public sector borrowings—post-credit rate agencies reviews—were dramatically decreased. The sole disappointing sign was noted in investment—despite the improved economic climate—keeping both gross and net fixed capital formation in the negative territory.

The COVID-19 pandemic has affected the global economy severely, but more disproportionately the recovering economy of Greece, which is still struggling to cope with the austerity measures imposed by its international creditors, as well as facing an escalation in the number of refugees fleeing from the war zones in Syria and elsewhere. Surveillance of the country’s porous borders of a few islands in the Eastern Aegean nearby Turkey, given Turkey’s hostile stance toward Europe in general and Greece in particular, has been a formidable task for the government to contain. The living conditions of refugee “hot spots” are frequently the headlines in the foreign press. These challenges do not bode well for Greece’s economic prospects and have negatively affected the business confidence level that is crucial to their continuing economic recovery.
Greece implemented the lockdown strategy followed by many other countries to slow the viral contagion. The first case was registered in Greece on February 26, 2020, and the government imposed a total ban on public movement on March 23, acting rather quickly after the first death reported on March 12. The restrictions imposed from the lockdown have been relaxed and are scheduled to end by mid-July. This does not mean that activities will return to the pre-lockdown period.

There are some “known unknowns,” such as the impact of the lockdown, the government’s and EU extent of economic support measures, and the business and consumer behavior post-COVID. Thus, providing an estimate of the lockdown’s economic impact is a hard task, since the crisis is unprecedented—unless we go back to the Spanish flu epidemic of 1918–20, which, in our view, would not be fruitful given the enormous social and economic transformational changes that have taken place since then and overlap with the First World War. What is important to recognize in the case of a pandemic is that the resultant pause of economic activities implies a simultaneous shock to the supply, as nonessential production activities are closed, as well as to demand when workers in such businesses stop earning any income. In economists’ jargon, this amounts to a severe structural break, which is likely to change the behavior of consumers and entrepreneurs—noted in the declines in the business and consumer’s confidence levels—so that any economic models (including the LIMG in use at the Levy Institute) need be used with caution until sufficient time-series data are available for estimating the size and impact of the structural break.

The Organisation for Economic Co-operation and Development (OECD) has provided the first of such estimates: their approach is based on the relative size of the sectors that are expected to be hit more severely by the lockdown, such as activities related to travel (including tourism) and services to households. Following this approach, they found that Greece would have the largest hit among OECD countries, estimated to be almost 35 percent of GDP. Their report also mentioned an alternative way to evaluate the consequences of the crisis by looking at the impact from the drop in private consumption for some member countries, but provided no such estimates for Greece.

More recently, the International Monetary Fund (IMF) and the EC have released their latest forecasts for Greece showing that real GDP growth in 2020 was expected to drop by 10 percent and 9.7 percent, respectively, compared to the previous year: registering the largest fall among the developed and

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1 Source: World Health Organization. https://www.who.int/
EU economies. The IMF and EC forecasts show the 2020 unemployment rate rising 22 percent and 19.9 percent, respectively, then decreasing in 2021 to 19 percent and 16.8 percent. Both the IMF and EC projections are assuming a U-shaped recession, with output recovering in all countries in 2021 by a smaller amount than the fall projected in 2020. The projections are based on the assumptions: a) that the pandemic will fade in the second half of 2020, with a gradual lifting of containment measures and b) there will not be a second wave of the COVID-19 pandemic. Real GDP in 2021 for Greece, according to the IMF and EU, is expected to grow by 5.1 percent and 7.9 percent, respectively, implying that by the end of next year output will not yet have returned to its 2018 level.

All three institutions project a relatively more severe impact on Greece because of its reliance on tourism. Indeed, in 2019 the country registered an inflow of more than 18 billion euro—almost 10 percent of GDP—under the heading “travel” in its balance of payments, 90 percent of which was obtained between May and October. It is reasonable, then, to assume that most of these receipts will not materialize in 2020, even if the pandemic starts to fade in May. The government recently announced the ease of travel restrictions from Europe’s Schengen countries and Israel effective July 1 using random sample COVID-19 testing. However, based on authoritative and cautionary pronouncements coming from various quarters, people would not be necessarily willing to enjoy the sun and go swimming in the beautiful Greek islands this summer, knowing that the country’s health system has been under severe stress not only by the austerity measures implemented in the last few years (Nikiforos, forthcoming), but also by COVID-19.

Moreover, the monetary inflow from tourism is only the starting point of a multiplier process: employment in tourism-related activities is a significant share (9.8 percent in 2019) of total employment, with a strong seasonal increase in the second and third quarter of each year. The revenues from the sale of services to tourists become both wages of Greek workers and profits to the tourism industry, while a fall in such revenues, in turn, decreases consumption and investment according to the standard Keynesian multiplier effect.

**Projections**

Projecting the likely impact of the current crisis on the Greek economy is a complex task, given the overwhelming degree of uncertainty of future events and the behavior of economic agents under the “new” normal. This is confirmed by comparing the magnitude of the changes in the major international institutions’ projections for the euro area. In March, when the crisis had already developed in China and was spreading

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5 As measured by employment in “accommodation and food service activities” by ELStat, Labour Force Survey, Table 3a.
to Europe, the OECD\textsuperscript{6} only projected a small slowdown for the eurozone in 2020, still hoping for a positive GDP growth rate (see the bottom of Table 1). In April the IMF updated its projections for their World Economic Outlook Database,\textsuperscript{7} now estimating a fall in real GDP of 7.5 percent for the euro area. The EC,\textsuperscript{8} a few days later, was already more pessimistic, reporting a fall in real GDP of 7.7 percent.

In our projections exercise, we explore the consequences of different assumptions about the fall in the different sources of aggregate demand.

In our model, GDP is determined from the demand side, according to the traditional Keynesian approach (also considering the role of financial markets and of the stocks of real and financial assets). This implies that the ultimate drivers of demand are the exports of goods and services—which are determined separately—along with fiscal and monetary policy. Particular attention has been given to modeling tourism, which, as mentioned above, constitutes a large share of Greek exports of services.

In our baseline scenario, we assume a fall of 90 percent in the number of tourists coming to Greece in the first three quarters of 2020, and a fall of 25 percent in the last quarter of the year. We assume that tourism will resume in 2021, but remaining at around 80 percent of the level it reached in 2019. We follow the latest GDP projection from the EC to project the growth in income of Greece’s trading partners, which determines the exports of goods, along with relative prices.

Next, we assume a drop in consumption of different categories of goods and services in the first two quarters of 2020. More precisely, we assume that while demand for food and beverages, communication, health, and education would not drop significantly because of the lockdown, the demand for clothing, gas, etc. will fall substantially. From our calculation, we estimate a total fall in consumption and investment over the level they would have reached of almost 7.5 percent of 2019 GDP.

We have assumed a moderate increase in government’s current expenditure on goods and services (600 million euro in 2020 against 2019), and an increase of about 600 million euro in social benefits in the first two quarters of 2020. We also assume that the payment of direct taxes and social contributions are postponed in 2020 to 2021. Following recent government announcements, we included an additional stimulus that we assume will start in September and run through the first two quarters of 2021 for an overall amount of 4.5 billion euro. We also considered the announcement of a decrease in the VAT rate.


\textsuperscript{7} See https://www.imf.org/external/pubs/ft/weo/2020/01/weodata/index.aspx

Results for key macroeconomic indicators are reported in Table 1.

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<th>Table 1. Greece: Key Indicators under Alternative Scenarios</th>
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<td><strong>Baseline</strong></td>
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<td>Real GDP (growth rate)</td>
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<td>Gov. total surplus (percent of GDP)</td>
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<td>Current account (percent of GDP)</td>
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<td>External balance (percent of GDP)</td>
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| **Scenario 1: Recovery fund**                             |
| Real GDP (growth rate)                                    | 1.9 | -10.4 | 8.0 | 6.5 |
| Gov. total surplus (percent of GDP)                       | 1.5 | -10.0 | -1.4 | -2.1 |
| Gov. primary surplus (percent of GDP)                     | 4.4 | -6.7 | 1.8 | 0.9 |
| Current account (percent of GDP)                          | -1.6 | -3.6 | -1.7 | -1.0 |
| External balance (percent of GDP)                         | 0.7 | 1.6 | 0.1 | 0.6 |

| **Real GDP projections from other sources**                |
| Greek government: May 2020                                 | 1.9 | -10.0 | 5.0 | n.a. |
| IMF WEO: April 2020                                        | 1.9 | -10.0 | 5.1 | n.a. |
| EC: May 2020                                               | 1.9 | -9.7 | 7.9 | n.a. |

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<th><strong>Real GDP projections from other sources for the euro area</strong></th>
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<td>IMF WEO: April 2020</td>
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In our baseline scenario public debt is expected to increase to 207 percent of GDP in 2020, and to decline as the economy recovers to 192 percent of GDP by the end of the simulation period in 2022.

The private sector had been deleveraging before the crisis started. In December 2019, the last period for which data are available, the household sector had reduced its stock of overall liabilities, including long-term loans both because of reduced borrowing and defaults on existing debt. Nonfinancial corporations had also reduced their end-of-period stock of loans outstanding, this time because debt write-offs exceeded new borrowing, which increased over 2019. The net financial position of households improved over 2019. This was due to the appreciation in the market price of listed and unlisted shares, most of which are on the liability side of nonfinancial corporations, so that the net financial position of the nonfinancial private sector as a whole improved, but marginally. It is interesting to note that the increase in the market price of Greek shares
was also reflected in an increase on the asset side of the rest of the world, reflecting the growing financial investment in the Greek private sector from abroad. The Greek household sector therefore entered the COVID-19 crisis in a weak financial position and with a declining stock of liquid assets: at the end of 2019 deposits were somewhat below their 2018 level.

This was expected since the lockdown and the implied fall in income forced households to increase their consumption out of their stock of liquid assets, reducing their bank deposits. On the other hand, data up to March 2020 show a moderate increase in household deposits, possibly implying that—in the face of the uncertainty generated by the health crisis—households, on average, reduced their consumption level relative to income.

We also consider a more optimistic scenario, in which the recently announced Recovery Fund proposed by the EC materializes allowing the government to increase public consumption as well as investment through EU grants and loans. We assume the plan to take effect from the third quarter of 2021, with an additional expenditure of 2 billion euro per quarter. This enables the economy to achieve a much faster growth rate contributing to the decline of the public debt-to-GDP ratio, which falls to 177 percent by the end of 2022.

As Figure 1 shows, without the additional intervention of the Recovery Fund, the trajectory of Greek real GDP would have been L-shaped. This would entail a recovery insufficient to fill the gap in income generated by the COVID-19 health crisis, and a growth rate insufficient for restoring GDP to its precrisis trend. The additional stimulus from the Recovery Fund directed to public investment that has a much larger...
multiplier, would change the recession-recovery into a U shaped one, although a robust recovery still requires a further boost to return to the previous trend, as can be seen clearly in Figure 1.

It remains to be seen if the stimulus expenditure will translate into a structural increase in government expenditure (i.e., an increase in employment in health services, education, etc.) or will be mainly targeted to sustaining firms and workers through the losses in income occurred because of the health crisis. In the latter case, as the emergency period ends, public debt sustainability will return to the top of the EC’s priorities, with a new period of austerity to follow.

**Policy Initiatives**

What can the government do to alleviate the impact of the shock and help put the economy back on track when the epidemic has died out?

Some appropriate measures have already been taken by the government.⁹ They include:

- No calculation of late payment, interest, or surcharges for tax liabilities/payments suspended.
- Immediate refund of debts due from the Tax Administration to taxpayers for amounts up to 30,000 euro.
- If paid on time, a 25 percent reduction in tax and social security contribution (SSC) obligations (excluding VAT) for employees of halted firms, as well as for the self-employed, freelancers, and firms affected by the coronavirus crisis.
- The SSCs of employees (of firms affected by the coronavirus crisis, whose labor contracts have been suspended) and self-employed (considered as employees) affected by the coronavirus crisis based on specific Statistical Classification of Economic Activities in the European Community (NACE) codes will be covered by the state.
- Firms can reduce their employees’ work time to a minimum of two weeks per month for at least 50 percent of all employees within a firm on the condition that they do not dismiss any workers. The measure can be applied for up to 6 months.
- Extension of the regular unemployment benefit payments, as well as extension of the long-term unemployment benefits and the unemployment benefits to freelancers and self-employed workers, for two months (March to May)—a recent government announcement indicated the possibility of extending these benefits to the end of July.

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⁹ This list was obtained from oecd.org, along with other country information, but it is no longer available on the OECD website.
• Allowance of 800 euros (March to May, with the possibility of extending to July) for the self-employed, freelancers, individual businesses, and employers up to five employees and affected by the coronavirus crisis based on specific NACE codes.

• Allowance of 800 euros (the same as above) for employees of firms affected by the coronavirus crisis whose labor contracts have been suspended based on specific NACE codes. This covers 1.7 million private-sector workers (81 percent of private-sector employees).

• A 40 percent reduction in rent for primary residences for March and April, for employees of firms affected by the coronavirus crisis based on specific NACE codes.

• A three-month extension of the deadline for firms’ payment of scheduled instalments of tax and contribution debts, due on March 31 and subsequent months. These payments will start as of June 1, 2020.

• Suspension of VAT and other tax obligation payments that were due between March 11 and April 30 until August 31 for businesses, self-employed persons, and sole proprietorships affected by the coronavirus crisis based on specific NACE codes.

• Suspension of SSC payments due by the end of March until October 31 for businesses, self-employed persons, and sole proprietorships affected by the coronavirus crisis based on specific NACE codes. Suspended payments will be paid in four installments of equal amount without interest and surcharges.

• The interest payment on performing loans of corporates affected by the coronavirus crisis for April, May, and June will be paid by the state (conditional to firms maintaining their job positions).

• A scheme for the support of the economy through the issuance of guarantees by the Hellenic Development Bank has been approved under the EU’s temporary framework for state aid. The scheme will partially guarantee eligible working capital loans, with the total exposure of the Hellenic Development Bank capped at 40 percent of the volume of loans issued by a financial intermediary. The total size of the scheme will amount to 2 billion euro.

• A 40 percent reduction in rent for commercial premises for March and April for firms affected by the coronavirus crisis based on specific NACE codes.

• Suspension of loan repayments (for the principal amount) until September for firms affected by the coronavirus crisis.
In addition, the European Central Bank (ECB) has lowered the standards for credit rating of bonds that are accepted as collateral so that Greek government debt can now be purchased by the ECB on the secondary market. This should help lower the cost of borrowing for the government.

**Conclusion**

Greece’s fragile economic recovery was halted by the COVID-19 pandemic that reversed all economic trends, save the public sector that intervened with various support programs funded from either the EC or the European Stability Mechanism’s loan reserves, albeit thus far, too limited in magnitude and with much delay as compared with those of Denmark, Ireland, France, Germany, and other EU member states. Greek GDP, employment, exports (including the vital sector of tourism and related activities), and investment—both domestic and foreign—are expected to record significantly negative trends. The projections of many institutions, including the IMF, OECD, bank research departments, European think tanks, and our own simulations, are discouraging for 2020, and more so for Greece than any other country of the EU. Most of the projections for GDP growth in 2021 over 2020, however, show a quick V-shaped recovery with positive growth rates of 5–8 percent, which is rather improbable given the economy’s structural inefficiencies. Such recovery is even not in the cards for the larger European economies and the United States. Our simulations for 2021 are less optimistic and can be achievable only with the rapid implementation of all the announced government support programs immediately after the lockdown restrictions are lifted. We are, therefore, expecting the recovery to be a lot more of a U-shaped one that will take at least three years for the economy to return to the pre-COVID-19 GDP and employment levels. We draw this conclusion from our belief that modified consumer behavior, including by tourists visiting Greece, will be influenced by the extra protection, random sample testing of the virus, and social distancing so as to keep the virus in check and avoid a second wave of it. These two factors may result in a slower, L-shaped recovery.

The recently announced EC Recovery Fund of 750 billion euro made up of grants (500 billion euro) and loans (250 billion euro) constitute a share for Greece amounting approximately 32 billion euro (22.5 billion euro in grants and 9.5 billion euro in loans) to be disbursed over a four-year period, giving us the opportunity to simulate an alternate scenario (recovery scenario), as shown in Table 1 and Figure 1. The simulations of this scenario do indeed show that it can be a game changer for Greece. If these funds are used properly, as discussed above, the real GDP growth rate will accelerate for both 2021 and 2022, even though it will still fall short of reestablishing the trend growth shown in Figure 1. At least it is closer than the baseline scenario.
We hope that the Recovery Fund receives definitive approval in June and that disbursements from it are not subjected to strict conditionalities. This Fund offers an opportunity for implementing a European Marshall Plan or a European Green New Deal to reconstruct what has been lost in the fight of the new COVID-19 common enemy and more. In addition, the serious discussions for an increased EU budget are a step in the right direction and maybe the result of European leadership recognizing that concerted actions from all countries are required instead of each member country adjusting her budget. The former will create a union of growth, the latter a union of austerity.

References


Data Sources


OECD: https://stats.oecd.org/