Smooth end to Greek debt programme

The deal reached overnight confirms a piecemeal approach to Greek debt relief. While concerns about the long-term sustainability of the country's debt look set to eventually resurface, the additional relief measures put in place and post-programme governance should be enough to keep Greek risk under control for some time

Source: Shutterstock

Green light to late-August end of third Greek programme

By confirming that Greece has implemented all of the 88 prior actions under the fourth and final review, eurogroup chief Mario Centeno announced that Greece has successfully completed its ESM (Emergency Stability Mechanism) programme and that there will be no follow-up programme.

Yesterday's meeting was widely expected to disclose a new batch of medium-term debt relief measures to make Greek debt sustainable. These were indeed announced overnight, with a different mix from what the debate had suggested. The growth-related French mechanism was not part of the deal, nor was an explicit liability management exercise. Approved measures involve extensions of interest rates and maturities, medium-term measures, and the creation of a cash buffer. Amid the current, unstable political backdrop, the chances of building the necessary consensus on politically-binding and more ambitious debt relief measures were indeed slim.

Medium-term debt relief measures announced, with conditions attached

The first batch of debt relief, a 10-year extension of the EFSF (European Financial Stability Facility) interest and amortisation, will be delivered upfront. This should help Greece to smoothly return to market financing all along the Greek curve. A second batch of debt relief measures will be agreed upon, with conditions attached. These include the abolition of the step-up interest rate margin related to the debt buy-back tranche of the second Greek programme and SMP profits (Securities Markets Programme) from the ESM segregated account as well as the transfer of ANFA (Agreement on Net Financial Assets) and SMP income. They will be disbursed in semi-annual payments until 2022, subject to compliance with policy commitments and monitoring. The relevant monitoring will be run under the EU Commission's enhanced surveillance procedure to be activated in the next few weeks, which will produce quarterly reports.

Cash buffer set up, with possible flexible use

The eurogroup also mandated the ESM to disburse €15 billion to Greece as the last programme tranche. Some €5.5 billion of it will be placed into a segregated account and will be used for debt servicing. The remaining €9.5 billion will be disbursed to a dedicated account to set up cash buffers to be tapped for debt service in case they're needed. According to the eurogroup statement, Greece should exit its programme with a total cash buffer of €24.1 billion, deemed enough to cover Greece's financial needs for at least 22 months, a substantial backstop against potential short- to medium-term risks.

The use of the cash buffer was not made explicit in the official statement, but the national press conference of the Greek finance minister Euclid Tsakalotos added some useful information. In principle, the cash buffer should be used to manage the debt profile to reduce the burden of financing the Greek economy; as such this could include the possibility of buying back IMF or GLF (Greek Loan Facility) debt. We expect some this to materialise.

IMF to remain a technical partner

As expected, the IMF decided not to enter a stand-by arrangement but will remain involved in the post-programme surveillance framework with the eurozone institutions. The divergence on debt sustainability between the IMF and other lenders was apparently not bridged by the debt relief package approved yesterday. IMF managing director Christine Lagarde said the measures should ensure medium-term sustainability but reaffirmed that the IMF has reservations over the long term.

Need for long-term debt relief to be assessed in 2032

The need to take additional debt relief measures will be reassessed in 2032. Should an unexpectedly adverse scenario materialise by then, the eurogroup could put in place a further re-profiling, capping and deferral of interest rates of ESFS loans to create the conditions for Greece to meet the gross financial needs long-term benchmark (20% of GDP).

The Greek case should fade from the headlines for some time

The agreement on the completion of the Greek programme is certainly good news. To be sure, it does not bring a once-and-for-all solution to the Greek debt problem. But it should ensure an effective hedge against the resurgence of Greek risk for a number of years. The post-programme governance keeps a substantial degree of conditionality on the completion of planned reforms, and the Greek government's growth strategy seems to show a growing sense of ownership of realised and ongoing reforms. Fiscal targets remain ambitious, and the Greek commitment to keep the primary surplus at 3.5% of GDP until 2022, and, most notably, at 2.2% of GDP from 2023 to 2060, looks liable to future downward revisions. Still, the available cash buffer seems big enough to accommodate a gradual return of Greece to the market without excessive external pressure. A favourable environment for the Greek government to work hard at returning the country to a renewed, financially sound footing.

It's now time for the European institutions and political leaders to concentrate on the reform of the entire European project: creaks in the building need quick fixing, not only on the Greek side.

Author

Paolo Pizzoli
Senior Economist, Italy, Greece
paolo.pizzoli@ing.com

Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("**ING**") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies).* The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit www.ing.com.