

Can the Greek state pay for itself?

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The Greek saga has not arrived at a decision point. On the surface the key sticking point is that the government party, Syriza, will not accept any 'recessionary' measures. The discussion is now centring on the target for the *primary* balance. This makes sense because only a government that can at least achieve a primary balance can pay salaries and pensions on time. Whether it can achieve at least a primary balance without 'recessionary measures' must be a key consideration for the government, since it will be able to spend only what it collects in revenues should there be no agreement with the creditors.

Unfortunately, it seems that nobody knows the true state of Greek public finances with any precision and the government might harbour illusions on this question.

The Greek finance ministry has been claiming officially that it achieved a considerable primary surplus during the first months of this year, even larger than planned (2.7% of GDP for general government). If this statement were true, no further measures would be needed to achieve the new target for this year, which seems to be a surplus of around 1 % of GDP. However, closer inspection reveals that the primary budget is not in surplus. The government is keeping cash by simply not paying key suppliers, skimping on investment expenditure and relying on "extra-ordinary" items among the revenues.

As discussed below, all three aspects are important, but can be documented only for the January-March 2015 period:¹

1) Key suppliers have not been paid. The detailed accounts up through March show that current expenditure is lower by about €800 million (€5,000 million instead of €5,800 million), compared to the same period in 2014, of which €150 million should have gone to local government, €150 million to social funds and €500 million to hospitals. The very same government that has argued that Greece is experiencing a humanitarian catastrophe is not paying the very institutions that provide support for the neediest members of society (local governments, social funds and hospitals). It is thus not surprising that officially-recorded arrears have increased by over €700 million since the end of last year.

2) Investment is cut. Here again there is a gulf between the rhetoric on the need for investment and the reality, which is that investment has been cut by €400 million relative to the budget and over €500 million with respect to last year.

¹ The detailed data for April were supposed to have been published last week, but they are still not available publicly.

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3) *Tinkering with extra-ordinary revenues.* Two items stand out: first of all the government has cashed in already a large part of the EU funds pencilled in for the entire year. The €560 million ‘over-performance’ on EU funds, which the government counts among revenues, will not be available later. A second item is a transfer from so-called ‘extra budgetary institutions’ of €670 million.

The key to understanding the budget numbers published so far by the Ministry of Finance, is that they mostly relate to cash payments. This allows the government to sign large defence contracts and claim at the same time that military expenditure has been lower than planned. However, not paying suppliers is usually very costly for the government itself (because most contracts foresee heavy penalties for this case) and because any delay in payments from the government ripples down the supply chain, with deleterious effects on the suppliers who are themselves facing a credit crunch.

That the reduction in expenditure has been mainly cosmetic is acknowledged by the latest bulletin of the Finance Ministry with the giveaway in the last paragraph:

The lower expenditures are mainly due to the rearrangement of the cash payments projection, according to the prevailing conditions. It is estimated that after the stabilization of the conditions, expenditure will revert to the levels of budget targets.

Summing up all the three major elements of budgetary cosmetics and one-offs, one arrives at a total of €2.3 billion, which is higher than the primary surplus the government has claimed it had achieved. In other words, the Greek government is already now running a primary deficit, rather than the surplus planned under the old programme.

This is not the first time that the Greek government keeps the cash during the first months of the year, but then has to pay out more during the summer. In 2014, for example, there was a difference of about €2.8 billion difference (worth over 6% of its first quarter GDP) between the deficit measured on a cash basis, and the official numbers, as determined later based on the European (ESA) standard. The creditors know this of course. Moreover, they will keep in mind that the forecasts for the budget balance that have made during the current year have been consistently several percentage points of GDP too optimistic over the life time of the programme. This is why they insist this time on nailing down the measures that would actually deliver the, very modest, primary surplus requested for this year.

The Syriza government had pledged that, contrary to its predecessors, it would never run a primary deficit. However, this promise seems to have been broken already. Achieving even a primary balance will require further measures. These measures might have to be even stronger if no deal can be reached, because in that case no money will be available to plug any even temporary shortfall, and revenues are likely to tank along with the economy.² Accepting a realistic programme should be preferable to continuing with the traditions of spending first and the looking for the money.

² See <http://www.ceps.eu/publications/why-greece-different> on the underlying reason why the economy has been so weak for long in Greece: no growth in exports.