EURECA project

Hellenic Recovery Fund – a solution for Greece and Europe

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Preface

- The Greek solvency crisis – in combination with speculative attacks on several euro zone countries – has placed a tremendous strain on fiscal and monetary policy in Europe
- It will not be possible to protect the integrity of the euro zone without **austerity** (substantial savings in the affected countries), **solidarity** (a willingness to share the burden) and **creativity** (understanding the workings of the capital market and playing the game by the corresponding rules)
- The current conundrum for European policymakers does not seem to have a "mathematical solution space" – In real fiscal terms, it has so far only aggravated the problems for all concerned
- Yet we believe that resolving this conundrum is vital if the EU is to return to a pattern of ongoing economic integration and progress
- This document describes the foundation on which such a solution can be built

Source: Roland Berger

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Executive summary

1. Bundle Greek state assets worth EUR 125 bn in a central trustee organization (holding company)
2. Sell entire holding company to European Union for EUR 125 bn
3. Allow Greek state to use proceeds to repurchase bonds from ECB and EFSF
4. In so doing, reduce Greek debt from 145% to 88% of GDP
5. Reduce ECB's and taxpayers' exposure to Greek debt to zero
6. Invest EUR 20 bn in restructuring assets to maximize value of privatization (plus EUR 40-60 bn)
7. Add 8% GDP stimulus to Greek economy as side-effect of restructuring program
8. Drive growth swing from -5% to +5%, producing additional tax revenue equivalent to 4% of GDP
9. Cut interest burden by more than 50% thanks to debt reduction and rating improvements
10. Combine (8) and (9) to enable debt repayment worth 1% of GDP p.a., leading to a debt ratio that is clearly within the 60% debt ceiling of the Maastricht criteria.
11. Payout of any surplus to Greece in 2025 to fund additional debt reduction – Any shortfall should be covered by Greece provided the required sum does not exceed 30% of GDP (i.e. no more than EUR 150 bn by 2025/26)
12. Side-effect 1: CDS spreads will collapse, causing speculators to incur losses and preventing attacks on Ireland, Portugal and Spain
13. Side-effect 2: 100% privatization of Greek public sector will stamp out corruption and foster long-term growth and investment
14. Side-effect 3: Greek banks holding Greek bonds will see value gain of EUR 30 bn, restoring solvency of banking system and reducing collateral risk for ECB by 95%, thereby ending Greece's credit supply crisis
15. Safe non-default repurchasing option on Greek bonds could also be implemented as an option

Source: Roland Berger

Impact of our proposal

- This paper outlines actions to solve the Greek debt crisis and protect the integrity of the euro
- It is designed to achieve the following goals:

In the short term

→ Reduce Greek debt from 145% to 88% of GDP in one step, without debt restructuring

→ Allow Greece to regain investment grade rating (A or A+) in the short term

→ Reduce interest burden by reducing CDS spreads from currently over 20% to less than 5% virtually overnight

→ Reduce ECB exposure to Greek sovereign debt to zero

→ Ensure maximum risk containment and risk reduction for the European taxpayer

→ Credibly repel speculation against both the euro and the peripheral euro member countries

In the medium and long term

→ Prevent the value destruction that would be triggered by a "fire sale" privatization

→ Support structural reform with a view to long-term growth in Greece

→ Kick-start the Greek economy and revive growth and job creation

→ Enable Greece to begin taking steps that will ultimately reduce its debt to significantly below 60% of GDP by 2025

Source: Roland Berger

The concept (1/2)

- Market's judgment of Greek debt sees the country firmly locked in a debt trap – Probability seen by the markets that Greece will NOT default over the next five years is close to zero based on current CDS spreads
- Current debt restructuring efforts have had the advantage of putting very considerable pressure on Greek politics to initiate structural adjustments. However, the marginal impact on political action in the country is waning as frustration about the ratio of effort to return begins to affect market sentiment
- "Fire sale" privatization is not an option, as such a process would further depress the value of assets
- Nor is gradual privatization a realistic option, as the staggered impact of resultant revenue would be swallowed up by the ever-growing interest burden on debts that continue to grow in the meantime
- Solution: Create a European asset purchase and privatization vehicle combined with a conditional residual guarantee to drive down funding costs:
  - Bundle Greek state assets in one or several privatization holding companies established as European SEs
  - Group assets into participating interests (banks, industry, utilities, etc.), real estate, etc.
  - Trigger wholesale purchase of SEs by a European facility (potentially under the EFSF program) for a sum of EUR 125 bn and repurchase Greek bonds held by ECB and other European institutions and states
  - Manage privatization program by EU institution with private cooperation partners (public-private partnership) to leverage best practices in restructuring, asset management and placement
  - Avoid fixed sales closure dates to reduce market pressure from vulture funds

Source: Roland Berger

The concept (2/2)

- Solution (contd.):
  - Set up a EUR 20 bn investment program to optimize asset values and thus maximize sales revenue (asset restructuring) – Use money from the European Structural Funds to some extent
  - This will simultaneously provide additional demand stimulus to the Greek economy and improve both the tax base and the debt/GDP ratio
  - Introduce a structural debt reduction program of 1% of GDP per year to further reduce Greek public debt to below 60% of GDP by 2025 (and possibly under 40% if the 1% of GDP per year repayment rule is strictly applied)
  - Target closure of the transaction in 2025, including a surplus/shortfall sharing feature
    - → If privatization yields a surplus after initial investment plus the interest burden on funding costs, the proceeds should be transferred to Greece to fund further debt repayment
    - → If the transaction yields a shortfall, remaining assets should be repurchased by Greek state at the discounted amount but with a cap of 30% of Greek GDP. The resultant total debt burden should likewise be limited to 75% of GDP. Structural repayment program should in this case be continued through 2040 to comply with Maastricht criteria

This transaction would effectively repel speculation targeted at other European Union member states as well, since speculative investors (who do not trust European governments and institutions to come up with a creative solution or have the strength to toe the line) would suffer severe losses triggered by falling CDS spreads

Source: Roland Berger


It's character that creates impact
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