Interview with Klaus Regling, Managing Director ESM

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We are facing a very important vote tomorrow. The government says a 'no' vote is not an exit from the euro, although a series of EU leaders says that it is. What is a 'no' vote for you?

I am a democrat and a European, so I fully respect the referendum. We need to wait for the sovereign decision of the Greek people and then see how the government reacts to the result. There are many uncertainties now about the future of Greece. I want Greece to continue to be part of Europe and the euro area, therefore I hope for a positive result in this difficult process.

The problem is that the referendum question requires a 'yes' or 'no' vote on specific measures, not on the euro itself.

I understand that the question might be difficult for people who are not experts in economics and have not followed the negotiations in such detail over the past months, or the programme of previous years. It may be difficult for the people to really understand the far-reaching consequences of this decision.

For you what would the implications be?

I lead the institution that is the largest creditor of the Greek government, therefore I have a very clear interest in positive developments in Greece.

For me it's very clear why this adjustment was overall unavoidable. During the decade before the crisis, there were wrong economic policy decisions which led to unsustainable developments. Examples are a fiscal deficit of 15.3% of GDP in 2009, and a big loss in competitiveness because wages increased much faster than productivity. In 2008, unit labour rose 40% faster in Greece than in the rest of the euro area. In the end, this led to a loss of market access, as private investors were no longer willing to lend money to Greece.

Under these circumstances, an adjustment was unavoidable. This was the situation in Greece when the euro area countries and the IMF stepped in to provide emergency financing. No one else was willing to do so. But money is only provided if there is a clear commitment to correct what went wrong in the first place. This is why Greece went through a very difficult adjustment, which was very painful for the population.

Did Greece have to take the hardest measures of all programme countries?

Greece's starting point was much worse than those of Cyprus, Portugal, and Ireland. That's why we see today that Ireland and Spain have the highest growth rate in the euro area. Greece was also on a path for positive results, growth had returned, the unemployment rate had dropped by two points in 2014 and the Greek government was able to issue a bond. So market access started to be restored. Our strategy was beginning to work in Greece. Growth projections at the end of 2014 were for 2.5% in 2015 and 3.5% in 2016. That shows that with continued reforms Greece could have left this desperate situation behind.

What if the people say 'no' now?

With a 'no' vote there would be great scepticism as to whether the necessary follow-up reforms would be implemented. To implement a programme requires ownership, the government needs to be convinced that it is necessary to implement difficult measures in a credible way. If conviction and ownership are not there, then we will not see the positive results that Greece needs.

Why would one vote 'yes' if he/she knows beforehand that a new, tougher programme will follow?

Greece needs to continue reforms, but the measures required on the fiscal side and on competiveness are much smaller than in the past. The large reduction from the deficit of 15.3% of GDP has mostly been achieved. Compared to what was done in the past five years, the remaining fiscal adjustment is relatively small but necessary. Also, competitiveness has been restored. We can see that by looking at the good export growth of the Greek economy last year. What are needed are structural reforms to stimulate future growth. I would not subscribe to the view that adjustment and reforms will need to be tougher than in the past.

How could the situation deteriorate so fast? Last December we were here talking about ECCL. The government says that it cannot be their fault since they have only been in power for a short time.

If confidence is lost, situations can change rapidly. Good policies lead to positive results and the opposite is also true. With growth- friendly policies I am confident trust will come back and eventually market access can be regained. This happened in Greece last year. The objective is to get back to that situation quickly.

How quickly?

It will depend on the strong implementation of the right economic policies and on the government implementing them with conviction. Market access could return as soon as next year.

Compared to other countries, is Greece a special case?

The magnitude of the imbalances was bigger than in any other euro country. But when I look at the results that were visible last year, such as falling unemployment, growth returning after six years of recession and market access coming back with a 5-year bond, Greece is not such a special case after all. That is why I am confident that Greece can be successful again like the other countries.

The IMF says we need debt relief. Will there be debt relief on this third programme?

There is no conflict among institutions here. Our lending terms have become so beneficial they have produced effective debt relief. Given loans of more than 30 years, very low interest rates, and a 10-year interest deferral, the Greek budget saves around €8 billion every year. That corresponds to more than 4% of Greek GDP. That is solidarity from the euro area.

In addition, the Eurogroup said in November 2012 that, if reforms continue to be implemented, Europe would be ready to consider additional relief measures, if they are necessary.

When will that take place? The IMF is pushing for that.

The IMF shares my view that we are providing permanent debt relief by having these very favourable lending terms: the EFSF loans are six times larger than the IMF's, they are far cheaper and have much longer maturities. If needed, these relief measures could even be reinforced.

What is the impact of Greece's non-payment to the IMF for the EFSF?

I am deeply concerned by this development. The Greek government has repeatedly stated that it would honour its obligation towards all its creditors. A non-payment to the IMF constitutes an event of default for the EFSF because we have cross-default clauses. This gives the EFSF the right to cancel the loan and demand immediate full repayment, to waive its rights, or to reserve its rights.*

* For developments in this regard since the interview was done, please check here: http://www.esm.europa.eu/press/releases/efsf-board-of-directors-reserves-its-rights-to-act-upon-greeces-default.htm