A Business Leader’s Perspective: Using Two Key Undeniable Facts on Greece to Win the Trust & Confidence of Taxpayers and the Global Capital Markets

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Greece, Out of The Crisis: Debt-End or Dead-End

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Paul B. Kazarian Summary CV

- **Over 100 presentations** on the topic of Greek debt and debt sustainability including: AmCham, BHCC, CEPS, CESifo, CIPFA, EGPA, FEE, HBS, IIF, IFAC, INET Oxford, ISCTE, LBS, OECD, PMI Congress, S&P, and USC.
- **Sole Special Advisor** to the Centre for European Policy Studies Task Force on How Better Managing Government Balance Sheets Can Enhance Growth.
- **Visiting Professor** of Government Financial Management at the ISCTE Business School at the Instituto Universitário de Lisboa in Portugal.
- Received the **2016 William Pitt the Younger Award** for extraordinary leadership in strengthening democracy through government financial management.
- Analysis on Greek debt **cited in prestigious publications** including: HBS Case Study, InterEconomics, The Accountant, Der Spiegel, and the FT.
- **Authored multiple presentations** on IMF best practices not applied to Greece.
- **Creator** of www.MostImportantReform.info.
- **Personal relationships** with executives at the largest SWFs.
- As **CEO and CFO** of Fortune 300 diversified conglomerate, turned around over a dozen multinational businesses from bankruptcy to world-leading successful growth companies.
- Japonica Partners founder (est. 1988), **Chairman, and CEO**.

Two Key Undeniable Facts to Remember

- **Undeniable Fact #1:** Despite political claims to the contrary, the **debt to GDP ratio** is universally recognized as the single most important measurement of Greece government debt sustainability.
- **Undeniable Fact #2:** **Vested interests** refuse to acknowledge that they have agreed to support internationally agreed upon accounting and statistics standards to measure debt, which require that reported debt provide a true and fair view of economic reality.

Undeniable Fact #1:

Despite political claims to the contrary, the **debt to GDP ratio** is universally recognized as the single most important measurement of Greece government debt sustainability.

Examples of Undeniable Fact #1: Debt to GDP

1. IMF uses debt to GDP ratio to determine Greece projected interest rates.
2. The IMF and the EC use Greece debt to GDP in 2060 to measure debt sustainability.
3. The rating agencies cite Greece debt to GDP as one of if not the most important measure of Greece government debt sustainability.
4. Media attention-seeking economists continue to use Greece debt to GDP to justify their misguided conclusions on debt sustainability.

The IMF Should Avoid Concerns About Political Doublespeak and Not Use the Future Face Value of Greek Debt for its DSA

- IMF states that the "debt to GDP ratio is **not a very meaningful proxy** for the forward-looking debt burden" in its June 2015 Greece DSA.
- However, in 2060 DSA projections, the IMF continues to project interest rates **based on future face value** of debt to GDP, including in its February 2017 Greece DSA.
- Using a debt to GDP ratio based on future face value is a **main driver** of the IMF projected debt and GFN increases.
- If the IMF used the same debt to GDP ratio and **2060 projections** methodology for countries such as France, Italy, or Spain, the debt ratios would also be “explosive”.

2060 Debt Projections Can Be Politically Driven Numbers Without Substantive Meaning

As illustrated by IMF baselines for Greece, 2060 projections can be manipulated to show debt at either a small fraction of GDP or a multiple of GDP.

	Feb 2017 Article IV Baseline	May 2016 DSA Baseline	Jun 2015 DSA Baseline	June 2014 Fifth Review Baseline
Debt to GDP - 2060	275%	250%	100%	60%
Gross Financing Needs % of GDP - 2060	62%	60%	22%	12%
International Accounting Standards (IPSAS/IFRS) Balance Sheet Debt Numbers:				
		YE 2016	**YE 2015**	**YE 2014**
Debt to GDP		75%	71%	70%

Notes: IMF data from sources as noted. International Accounting Standards (IPSAS/IFRS) Balance Sheet Debt calculated according to international accounting standards based on EC AMECO and Greece MoF data accessed 13 Feb 2017.

Debt to GDP Remains Most Important Metric to Credit Rating Agencies: Recent Greece Examples

Moody's	Standard & Poor's	Fitch	DBRS
Caa3	B-	CCC	CCCH
28 Feb 2017	*20 Jan 2017*	*3 Mar 2017*	*9 Dec 2016*
We assess Greece's Fiscal Strength as 'low', because of the government's high debt burden, which we estimate at around 180% of GDP at the end of 2016, one of the highest debt burdens in our universe of rated sovereigns. While we forecast the debt ratio to slowly decline in the coming years - based on the expectation of continued positive growth and gradual fiscal consolidation - it will remain at very high levels and highly susceptible to shocks.	...at an estimated 180% of GDP in 2016, Greece has the second highest debt-to-GDP ratio of all the sovereigns we rate. ...we estimate that net general government debt will amount to 168% of GDP, among the highest projected debt burdens of all rated sovereigns.	Weaknesses: Despite public debt restructuring in recent years, general government debt (177% of GDP in 2015) and net external debt (125% of GDP) are among the highest in the world. Fitch uses stylised projections for a sovereign's gross general government debt/GDP ratio to illustrate the sustainability of its debt burden and its sensitivity to economic growth, the cost of borrowing, fiscal policy and the exchange rate. The Greek government agrees with the IMF that further debt relief is needed... *(24 Feb 2017)*	The CCC (high) rating reflects Greece's very high level of public sector debt and the political challenge the Greek authorities and the institutional creditors face in placing this debt on a downward path. Challenges: ...Very high level of public sector debt. Using conventional stock analysis, Greece's gross general government debt-to-GDP is extremely high, at 177.4% of GDP at end-2015, the highest in the Euro area. DBRS applies shocks to a baseline path of gross debt-to-GDP to assess Greece's resilience. Under DBRS' debt sustainability analysis of a weaker economic scenario in which GDP growth averages close to zero in 2016-2021, debt-to-GDP increases to 188.2% by 2018, before declining to184.8% in 2021. This compares with a debt peak of 181.6% in 2016 in the baseline scenario. Fiscal underperformance from 2016 to 2018 would also increase the debt ratio, while a contingent liability shock of 6.2% of GDP applied in 2017 would have a more severe impact. A temporary growth shock of one standard deviation would also have a more severe impact. In a tail risk scenario of a combination of weak growth, fiscal slippage and a contingent liabilities shock, debt-to-GDP would rise to 201.3% in 2018.

Undeniable Fact #2:

Vested interests refuse to acknowledge that they have agreed to support internationally agreed upon accounting and statistics standards to measure debt, which require that reported debt provide a true and fair view of economic reality.

There are Two Types of Internationally Agreed Upon Standards to Measure Government Debt and Both are Harmonized in Seeking to Provide a True and Fair View of Economic Reality

1. International agreed Upon <u>accounting standards</u>.
    - International Public Sector Accounting Standards (IPSAS)
    - International Financial Reporting Standards (IFRS)

2. Internationally agreed upon <u>statistics standards</u>
    - 2008 System of National Accounts (2008 SNA)
    - European System of Accounts (ESA 2010)

International Public Sector Accounting Standards (IPSAS)

- IPSAS is <u>the only</u> internationally agreed upon accounting standards for the public sector.
- IPSAS is recognized as the <u>global best practice</u> for governments.
- IPSAS standards are relied upon for financial reporting by the <u>most highly respected governments</u> in the world, including New Zealand, the UK, Canada, Australia, Switzerland, the US, France, and Israel.
- <u>IPSAS goal</u> is to provide a true and fair view of economic reality, including restructured and concessional debt.

International Financial Reporting Standards (IFRS)

- IFRS is the only internationally agreed upon accounting standards for the private sector.
- IFRS is recognized as the global best practice for the private sector and served as the basis for developing IPSAS for the public sector.
- IFRS goal is to provide a true and fair view of economic reality, including restructured and concessional debt.
- IFRS is virtually identical to IPSAS on measuring debt.

System of National Accounts (SNA 2008)

- SNA 2008 has been officially endorsed by the five leading global entities: the European Commission, the IMF, the World Bank, the UN, and the OECD.
- All five signed the SNA 2008 Forward to "encourage all countries to compile and report their national accounts on the basis of 2008 SNA as soon as possible."
- SNA 2008 goal is to best reflect economic reality.
- SNA 2008 is harmonized with IPSAS, IFRS, and ESA 2010 for the calculation of restructured debt.

European System of Accounts (ESA 2010) Calculation of Government Debt Intended to Amplify Maastricht

1. ESA 2010 was passed by the EC with the force of law.
2. ESA 2010 provides the necessary detail to provide a true and fair measurement of the economic reality of government debt, which supersedes debt at future value.
3. ESA 2010 is significantly harmonized with internationally agreed upon accounting (IPSAS and IFRS) and statistics (SNA) standards for the calculation of restructured debt.
4. The European Commission signed 2008 SNA and urged rapid adopting, with the measurement of government debt harmonized with internationally agreed upon accounting standards.

Note: Future value also known as nominal value.

The Meaning of Maastricht Treaty Debt is Misunderstood and Misused

1. The Maastricht definition of debt was <u>never intended</u> to provide a true and fair view of the economic reality of debt.
2. Created <u>before</u> the European Union/European Commission endorsed ESA, IPSAS, and SNA.
3. The <u>60% criterion</u> has long ago lost any substantive relevance.
4. The debt is a future value that is <u>incorrectly and widely assumed</u> to be in compliance with internationally agreed upon standards to provide a true and fair economic reality.

Greece 2016 YE Balance Gross Sheet Debt, Correctly Calculated in Accordance with International Accounting or Statistics Rules is 75% and 91% of GDP, Respectively

(€, Billions)

		Internationally Agreed Upon Standards Designed to Reflect Economic Reality			Rules Set Politically with Little to No Regard to Economic Reality		
		International Accounting Standards (IPSAS/IFRS) Balance Sheet Debt	2008 System of National Accounts (2008 SNA) Correctly Calculated	European System of Accounts 2010 (ESA 2010) Correctly Calculated	IMF Debt Sustainability Analysis (DSA) Correctly Calculated	IMF Baseline Future Face Value	Lisbon Treaty Excessive Deficit Procedure* (EDP) Future Face Value
1.	**Gross Debt**	**€ 132**	**€ 161**	**€ 161**	€ 204	€ 325	€ 317
2.	**Gross Debt % of GDP**	**75%**	**91%**	**91%**	116%	184%	180%
3.	**Net Debt**	€ 84	€ 113	€ 113	€ 186	NA	NA
4.	**Net Debt % of GDP**	48%	64%	64%	106%	NA	NA

Debt metrics for Greece EZ member state peers are not reduced under ESA 2010, 2008 SNA, or IMF DSA as there is no qualifying concessional or reorganized debt; under IPSAS/IFRS, Portugal, Spain, and Ireland would report lower debt by approximately €22 billion, €18 billion, and €11 billion, respectively.

Notes: Based on EC AMECO, Eurostat, and Bloomberg data accessed 17 Feb 2017 with percentages based on GDP of €176 billion, except IMF Baseline from Greece Article IV (Feb 2017) with percentage based on GDP of €176.6 billion. *EC 479/2009 "Whereas (4)" states "The definition of ‘debt’ laid down in the Protocol on the excessive deficit procedure needs to be amplified by a reference to the classification codes of ESA 95”.

Truthful Facts Require Correctly Calculated Numbers Complying with Internationally Agreed Upon Standards of Evidence

Greece vs. Investment Grade Peers

1. Debt to GDP ratio
2. Debt service
3. Debt relief
4. Floating vs. Fixed debt

According to the internationally agreed upon standards for measuring debt.

ESM's Regling is Correct: Greece Has Among the Lowest 2016 Debt Metrics Compared to Peers and Now it is About Winning the Trust & Confidence of the Global Capital Markets

(% of GDP except Avg. Maturity of Debt)

		Greece	Peer Average	Cyprus	Ireland	Italy	Portugal	Spain
1.	Balance Sheet Net Debt	48%	70%	47%	43%	113%	79%	70%
2.	Balance Sheet Debt	75%	102%	88%	71%	133%	119%	98%
3.	Cash Interest	2.5%	3.2%	2.8%	2.3%	3.9%	4.3%	2.8%
4.	Debt Service	6.6%	10.3%	7.7%	5.2%	15.0%	10.6%	12.9%
5.	GFN	12.7%	14.0%	7.1%	4.2%	20.6%	16.2%	22.1%
6.	GFN - Adjusted	5.2%	9.6%	5.2%	3.9%	14.1%	9.6%	15.5%
7.	Avg. Maturity of Debt (Yrs)	25.5	9.6	9.7	14.0	6.7	10.7	6.9
8.	Interest Expense (ESA)	3.3%	3.2%	2.8%	2.3%	3.9%	4.3%	2.8%

Notes: Based on EC AMECO data accessed 13 Feb 2017. Balance Sheet Debt calculated according to international accounting standards; Balance Sheet Net Debt net of estimated financials assets based on Eurostat data accessed 13 Feb 2017. Greece Cash Interest is AMECO less EFSF deferred (non-cash) interest of an estimated €1.2 billion and SMP/ANFA rebates of €0.4 billion. Adjusted GFN assumes T-Bills refinanced at five year market yield except Greece at ESM rate of 1% with 10 year even amortization.

Greece Floating Rate Debt is Only 17% of Total Debt, Not the 70% Reported

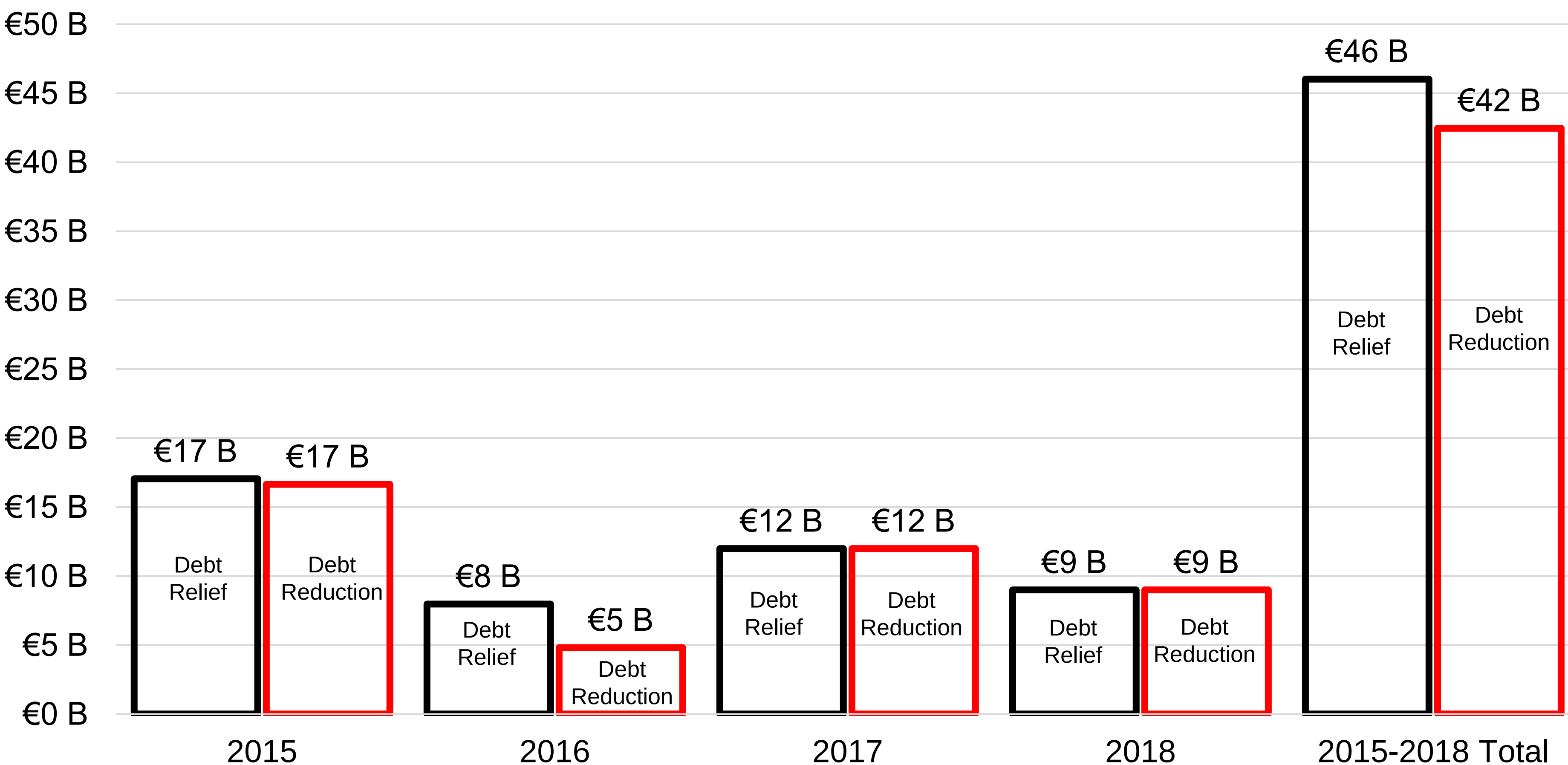
(€, Billions; as of 31 Dec 2016)

ESM and EFSF loans are clearly not floating by any international accounting standards definition, as they relate to each entity's entire capital structure, unlike the GLF loans that float based on 3-month Euribor plus 50 bps. ESM weighted average life of debt capital structure is approximately eight years, which is similar to many sovereigns.

	PDMA Public Debt Bulletin No. 84 Dec 2016		Estimate Based on Publicly Available Data	
			Amount	**% of Total**
Fixed Rate	30%	**Fixed:**		
Floating Rate	70%	ESM	€ 31.7	
Total	100%	EFSF	€ 130.9	
		PSI GGBs	€ 20.6	
		ANFA/SMP GGBs	€ 18.1	
		T-bills	€ 12.0	
		2014 GGBs	€ 4.5	
		IMF	€ 12.9	
		Other	€ 31.7	
		Subtotal	€ 262.4	**83%**
		Floating:		
		GLF	€ 52.9	
		Other	€ 0.8	
		Subtotal	€ 53.7	**17%**
		Total	€ 316.1	100%

Notes: Hellenic Republic Public Debt Management Agency (PDMA) data from Public Debt Bulletin, which notes "Fixed/floating participation is calculated including Interest Rate Swap transactions." Estimate Based on Publicly Available Data from Japonica Partners collaborative analysis of Greece general government debt.

Who Will be Held Accountable for Not Recognizing the €46 Billion of Debt Relief and the €42 Billion of Debt Reduction from the 3rd Programme Concessionary Loans?



Notes: Prepared under the direction of Japonica Partners based on ESM and Bloomberg data as of 14 October 2016. 2017 estimate assumes present value of 22% of €15.7 billion disbursement; 2018 estimate assumes present value of 27% of €12.9 billion disbursement. 2017-2018 debt reduction estimates may require adjustment upon further disclosure of use of proceeds.

Greece is NOT Required to, nor Should it, Use a Maastricht Debt Number to Communicate with Key Stakeholders

1. Greece should provide an internationally comparable debt numbers that provide a true and fair view of economic reality to taxpayers, global capital markets, and rating agencies.
2. Greece is solely responsible for providing correctly calculated debt numbers in accordance with internationally agreed upon standards.
3. In the absence of correctly calculated debt numbers, key stakeholders have no choice but to use the Maastricht number that overstates debt, does not provide a true and fair view of economic reality, and violates both internationally agreed upon accounting and statistics standards.

Justifications for Using Overstated Greece Debt Numbers are Flawed and Destructive

1. Greece must only report the Maastricht debt number. **Wrong.**
2. Greece is not solely responsible for reporting the correct debt numbers, but it is someone else who is responsible. **Wrong.**
3. The Greek government will not implement reforms unless the debt continues to be overstated. **Wrong.**
4. Voters will not accept reforms unless the debt continues to be overstated. **Wrong.**
5. Voters will not be happy to learn that the debt has been overstated. **Wrong.**

Reporting Highly Concessional Restructured Debt at Future Value (aka Nominal or Face value) Violates ALL Internationally Agreed Upon Accounting and Statistics Standards on Reporting a True and Fair Debt Number and Attempts to Defy Economic Reality

For example, does changing the terms on CCC rated government from 7% debt due in five years to 0% debt due in 1,000 years change the value of the debt?

- Yes, according to economic reality.
- Yes, when seeking to report a true and fair debt number.
- Yes, according to internationally agreed upon accounting standards (IPSAS and IFRS).
- Yes, according to internationally agreed upon statistics standards (SNA and ESA).
- No, if you want to make up a number that defies economic reality and all internationally agreed upon standards.

Since 2010, So-Called Sovereign Debt Economists Have Refused to Acknowledge the Existence of Internationally Agreed Upon Accounting and Statistics Standards to Measure Greek Government Debt

- They continue to hide their huge mistakes in overstating Greek government debt.
- They will not publicly debate their use of the future value of debt.
- They publish papers blatantly not citing the existence of accounting or statistics standards.
- They organize debt conferences and refuse to allow any accounting or statistics debt measurement experts.

A Sovereign Nation has the Sole Responsibility to Correctly Calculate its General Government Debt

- It is no one else's responsibility.
- Inexperience or unawareness is no excuse.
- Don’t blame others for not correctly calculating Greece government debt.
- Don’t blame it on Maastricht, the EC, the ESM, the IMF, or the ECB.
- Official sector partners, capital markets, and credit rating agencies need to be educated by the Greek government.

Not Correctly Reporting Past Debt Relief and Asking for More is Perpetuating Economic Malaise in Greece

1. Not correctly reporting a true and fair economic reality of Greece government debt results in an largely overstated number.
2. Not correctly reporting 3rd program debt relief as a reduction in debt deprives Greece of claiming a debt reduction success.
3. Claiming that additional debt relief is necessary:
    a. Tells the capital markets Greece debt is unsustainable and the government deserves very high borrowing costs.
    b. Tells credit rating analysts that a below investment grade rating is merited for Greece.
    c. Suffocates economic growth and international economic competitiveness.
    d. Ignores internationally agreed upon standards that can win the trust & confidence of taxpayers and the global capital markets.