Let the good times roll

Greece’s new government promises tax cuts and spending increases

But its official creditors are nervous

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OVER THE past decade Greece has not been the easiest place for politicians who want to be liked by voters. The newly elected centre-right government is trying its best. In his first few weeks in office Kyriakos Mitsotakis, the prime minister, has announced tax breaks for ordinary Greeks as well as for corporations. He has promised not to cut social benefits or fire any public-sector workers. Jobs are being created in areas that suffered deep cuts during the country’s eight-year crisis: the health ministry is preparing to hire 2,400 hospital workers and another 1,500 police officers are being recruited.

Sadly, the good times are not guaranteed. The prime minister’s policy choices could derail Greece’s chances of hitting tough budget-surplus targets set by its creditors, the European Union and the International Monetary Fund. Economists fear that the relatively inexperienced Mr Mitsotakis—he held a fairly junior ministerial post from 2013 to 2015—may be overestimating his government's capacity to shake up the country's sleepy bureaucracy and push through reforms.

So far the markets have given Mr Mitsotakis and his New Democracy party a vote of confidence. On July 16th Greece issued its first seven-year bond since 2010. A modest target issuance of €2.5bn ($2.8bn) was hugely oversubscribed: offers exceeded €13bn, pushing down the yield on the new bond to 1.9%. Greece now borrows at the same rate that Italy does.

Winning over the EU and the IMF will be harder. Asked about the new Greek government at her annual summer press conference, Angela Merkel, the German chancellor, called the bond issue "very positive" but sounded a note of caution: "We will have to see how things evolve."

Mr Mitsotakis's eagerness to accelerate growth by cutting taxes as fast as possible is risky. In his first policy statement in parliament on July 21st, Mr Mitsotakis announced an immediate 22% cut in "enfia", an unpopular annual property tax, and a cut of four percentage points in corporate tax to 24%. Both measures will take effect in September, four months earlier than originally expected. The lowest income-tax bracket will fall from 22% to 9%; value-added tax will drop by two percentage points. Further cuts will follow in 2020, Mr Mitsotakis says.

He has also made it clear that he will not broaden the tax base, a long-awaited reform that Syriza reneged on last year. Miranda Xafa, a former IMF economist, points out that seven out of ten Greeks pay less than €100 a year in income tax. Getting more people to pay tax "would help pay for the tax-rate cuts and make burden-sharing fairer," she says.

Meanwhile, there are gaping financial holes to be plugged at several state-owned companies. Poor management and a failed privatisation attempt under the Syriza government have pushed the Public Power Corporation (PPC), which provides electricity to half of Greece's households, to the brink of collapse. A struggling state-owned nickel producer owes PPC more than €200m in unpaid bills. Salaries for 7,000 workers at the loss-making Greek post office are being covered out of budget revenues. Christos Staikouras, the new finance minister, has warned of other "bombs with lit fuses" lurking in the national accounts.

The prime minister nonetheless promises that Greece will stick to a harsh budget target this year and next already agreed with its creditors: a primary surplus (before debt-servicing costs) of 3.5% of GDP. The Syriza government led by Alexis Tsipras, Mr Mitsotakis's predecessor, outperformed this target last year by increasing taxes and making deep cuts in the public-investment budget. Creditors were impressed by Syriza's fiscal rigour, but growth was subdued. This year's GDP forecast is around 2% (after 1.8% in 2018), well below the 3.5-4% needed to make up for the recession quickly. Greek GDP is still about 25% below its pre-crisis peak.

The new government hopes that political stability (thanks to its majority in parliament) and business-friendly reforms (cutting red tape as well as taxes) will attract foreign investment. "Greece will be a totally new country for business," promises Adonis Georgiadis, the minister for development and investment. As a sign of seriousness, he is leading a push to make sure the long-stalled privatisation project at Hellinikon, a prime site that used to be Athens's airport, gets under way this year.

Mr Staikouras will present a draft budget for 2020 in September. Although Greece is no longer in an official rescue programme, details of the budget must be approved by the creditors under the terms of a post-bail-out "surveillance" agreement. He is betting on drastic cost-cutting at government ministries to offset immediate revenue reductions from lowering taxes. If Mr Mitsotakis can please both voters and Greece's creditors, he will have done well.