Greece Running Out of Cash; Government Under Threat

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Greece's downward spiral has come to the top of the euro zone agenda again, with economists and analysts warning that it is closer than ever to running out of cash, and that the survival of a coalition government brought in just five months ago is under threat.

"Greece is running out of cash.The current strategy is really not working and there is substantial political risk," Thanos Vamvakidis, head of European G10 currency strategy at Bank of America Merrill Lynch, told CNBC Thursday.

Greece's economy has disappointed on every key metric – growth, unemployment and debt reduction - since the initial bailout terms were agreed. Its debt-to-GDP ratio, already the highest in the euro zone, will reach 189 percent, rather than 179 percent, Finance Minister Yannis Stournaras announced Wednesday.

This means that the targets agreed as part of the bailout are based on over-optimistic forecasts. The country's privatization program is also not proceeding as quickly as hoped.

Greece's government also wants the deadline for its primary surplus to reach 4.5 percent to be extended by two years, to 2016.

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"Greece is likely to receive its next disbursement of aid only because it's in everybody's interest to keep Greece ticking over until the next review. This is "muddling through" in its purest form," Nicholas Spiro, managing director at Spiro Sovereign Strategy, warned.

The Hellenic country is facing a yawning 40 billion euros ($51.7 billion) "funding gap" if the extension is granted, analysts at Credit Suisse warned.

While 16 billion euros of this can be covered by a reallocation of funds in the current program, a "combination of measures" will be needed to finance the remaining shortfall, they argued.

These may include haircuts to the debts owed to the bailout fund, and the euro zone taxpayer, another hefty loan from its creditors, or a reduction in the interest rate on existing loans.

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The gap was supposed to be addressed by Greece returning to the markets in 2015-16, which now looks increasingly unlikely as its economic performance deteriorates.

"Markets are not really focusing on Greece, because there is the assumption that Germany will somehow keep Greece in the euro zone until the German elections. Yet the debt dynamics are unsustainable, you need another official sector haircut, and this decision is politically very difficult," Vamvakidis said.

He described the **euro/dollar** trade as "very cheap" and "below Greek crisis levels" at the moment and added that peripheral spread volatility is likely to remain elevated for the next week over concerns on Greece.

The government's credibility has been damaged by the publicity surrounding the arrest of a journalist who published the "Lagarde list" – a list of close to 2,000 wealthy Greeks with money in Swiss bank accounts to avoid tax compiled by the current head of the International Monetary Fund (IMF) while still France's Finance Minister.

Placing the spotlight on tax avoidance at the top echelons of Greek society puts Greece's leaders in an unflattering light with both a population champing at the bit of austerity, and its international creditors. Tax evasion – not avoidance - costs Greece 28 billion euros annually, or around 15 percent of the country's gross domestic product, according to a study by Margarita Tsoutsoura of The University of Chicago Booth School of Business.

The coalition government, born after a fraught election campaign in June, has recently lost two members of parliament, bringing its majority to a slim 27. Pasok, one of two political parties which have dominated Greece for decades, was in disarray Wednesday night over whether or not to report reforms. One of the coalition's junior partners, the left-wing Democratic Left, are threatening to vote against proposed labor market reforms – and a general strike has been called for next week, putting pressure on parliament as it debates the reform.

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"Yet more "muddling through" may not be enough for the fragile Samaras government to remain in office," according to Spiro.

"The three-party coalition has a tenuous grip on power at a time when it's being asked to jump through yet more policy conditionality hoops with little sign of light at the end of the tunnel."

"The domestic politics and economics of Greece's adjustment remain fraught with risk and uncertainty," he added.

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