

Nikos Chrysoloras

The Triumphal Failure of Greece A Report from the Eurozone's Ground Zero

*But here's the problem, here's the rub:
they make a tremendous fuss
about everything, these Reformers.
(What a relief it would be if they were never needed.)
They probe everywhere,
question the smallest detail,
and right away think up radical changes
that demand immediate execution.*

*....
Maybe the moment hasn't arrived yet.
Let's not be too hasty: haste is a dangerous thing.
Untimely measures bring repentance.
Certainly, and unhappily, many things in the Colony are absurd.
But is there anything human without some fault?
And after all, you see, we do move forward.*

Constantine P. Cavafy
"In a Large Greek Colony, 200 B.C"

The Greek crisis is essentially a déjà vu of the subprime loans catastrophe, which hit the US in 2008, leaving the global economy in disarray. The obvious difference is that, in this case, the insolvent borrower is a state. Other than that, the similarities are striking: the sudden realisation that the Greek debt was 'toxic' initiated a crisis of trust in the financial system, due to the uncertainty over the exposure of major lending institutions to bad loans and raised doubts regarding the solvency of other developed states in the eurozone. The quality of sovereign bonds portfolios became 'anyone's guess', or, to put it more precisely, anyone's speculation. The immediate effect of this crisis of trust was the rise of interest rates in interbank and sovereign loans, resulting in a liquidity shortage and, perhaps, a double dip recession in 2012.

The fears were, in many respects, self-fulfilling: skyrocketing interest on sovereign bonds and declining growth rates due to the credit crunch made it virtually impossible even for solvent state-borrowers to service their debt without suffocating their economies. Credit rating agencies, notorious for their utter failure in 2008, exacerbated the panic mood through a wave of downgrades even to bonds, which, given the state of the public finances in the issuing countries, were obviously not 'subprime'. At the time this essay was written, Spain and Italy were standing at the edge of the cliff, while France and Belgium were reluctantly queuing behind them.

Leaving aside the troubling questions and issues regarding the structure and founding premises of the global financial system in general and the Eurozone institutions in particular, I will instead focus on the much more 'manageable' case of Greece. The questions I will be attempting to answer are, how did Greece get into this mess and how it can get out of it, who is responsible, what impact does the crisis have on the political situation in the country, what is expected from the EU, how are the measures of the so-called Troika (IMF, ECB, EU) perceived in Greece and what impact do they have on the political attitudes of the Greek people.

A tale of stereotypes

With a few notable exceptions, the coverage of the Greek financial crisis in international press is filled with stereotypes, which mud the waters and constitute more of a nuisance rather than a helpful analysis of what is really going on in the country. A common narrative, for example, is that Greeks 'live beyond their means'. However, Greeks as a whole, meaning the state, the people, financial institutions and corporations, are not as indebted as the stereotype suggests. An authoritative study by McKinsey showed that, in 2009, when the sovereign bonds crisis broke out, Greek's total debt (public and private) stood at 230% of GDP, half of what it was in the UK (466%) and much less than it was in Germany (285%) and France (323%). Greece also fared much better than the UK, France, Belgium, Portugal and, obviously, Ireland, when it came to total external debt.

Greece's low total debt levels, at least at the onset of the crisis, can be explained by the fact that private and corporate debt in the country is negligible by Western standards. Greek banks were also careful to avoid exposure in the US, Irish and Spanish real estate bubbles as well as the subprime loans market. On the other hand, even if the Greek people and businessmen did not borrow much, this is not to suggest that they are not collectively responsible for the debt accumulated by their democratically elected governments, which stood at 129% of GDP in 2009, at the beginning of the crisis and is projected to climb to 162% of GDP at the end of 2011 according to the European Commission. The problem is that a large part of the population in the country does not accept they should be held accountable for the debt of the state, hence the reactions to the austerity measures adopted in the framework of the EU-IMF bailout agreement. Indeed, apart from the 750,000 or so public sector employees who enjoy the benefits of permanent contracts, often decent salaries (depending on the post) and early retirement, the rest of the society expects to receive nothing else by the state other than poor public services, bribery demands and obscene bureaucratic obstacles to their business. The usual response to this is an 'I don't expect anything by the state, I don't give anything back to the state' attitude.

The result of this attitude, of course, is widespread tax evasion (according to the EU Task Force in the country, accumulated uncollected taxes are in excess of 60 billion euros) and a grey-black economy accounting for 40% of GDP according to some estimates (although, obviously, it is next to impossible to make precise calculations). As can be easily understood, the country is trapped into a vicious circle, since tax evasion means that public

services are underfinanced, clientelism and corruption in the public sector make things even worse, while this in turn leads to disillusionment with the state and, hence, more tax evasion. Moreover, the majority of the Greek population, which works in the private sector, is a victim to all this. Unlike entrepreneurs, self-employed and civil servants, these private sector employees neither evade income taxes and social contributions (they are automatically deducted by their salaries), nor can they be bribed for their services or enjoy outrageous benefits and ridiculously early retirement schemes. Instead, they have been asked to pick up the bill for the fiscal adjustment programme; one million of them lost their jobs due to the subsequent recession (not a single public sector employee has been laid off so far – November 2011), they are forced to cope with public services of substandard quality and they face the humiliation of borderline racist stereotypes in the foreign press.

One of these stereotypes is the eternally-sun-bathing lazy Greek. Again, reliable data show that this could not be further from the truth. According to the German Federal Statistics Service, Greeks work more than any other eurozone nation, with an average of 43.8 hours per week for men, as opposed to 40.3 hours per week in Germany and 37.5 hours per week in the Netherlands. Eurostat data earlier in 2011 pointed to similar results, as Greeks were shown to work 42 hours per week on average compared to 36 hours in Germany. However, clientelism and corruption in the public sector coupled with limited resources for R&D and widespread tax evasion among the self-employed mean that productivity levels are very low. In other words, most of this work goes to waste, in the basket case of the Greek Leviathan.

The obvious question, which emerges is: why? Why did clientelism, corruption and incompetence found fruitful ground to grow in the Greek public sector? Why are the self-employed persistently refusing to pay taxes? Why do the victims of all this, i.e. private sector employees, not revolt?

A short history of a failed democracy

When WWII broke out, Greek economy, like most developed ones, had not yet fully recovered from the Great Depression. The country had declared bankruptcy in 1932 and, like many other European states; it had been under authoritarian rule since 1936. Despite the clear Fascist influences of his regime, dictator Ioannis Metaxas tried to retain the country's neutrality in the conflict. However, his efforts failed, as Italy issued an ultimatum effectively asking the voluntary surrender of the Greek army to Mussolini's forces. Following a string of stunning victories from October 1940 to April 1941, Greece finally succumbed to the Axis since, in spite of the support of British and Commonwealth Forces, it was impossible to mount meaningful resistance against both the Italian army in the Albanian Front and the German Army on the borders with Yugoslavia.

Subsequently, the country was divided into three occupation zones (Bulgarian, Italian, German), while the remnants of the Greek army escaped to North Africa and continued the fight. The results of the occupation were devastating: Almost half million Greeks lost their lives over these three and a

half years, most of them of malnutrition during the great famine of 1942. Agricultural production decreased by 70% and the occupying forces confiscated most of the crops. Industrial production decreased by 82%, 60% of the livestock was lost, shipping fleet capacity decreased by 72%, exports were reduced to near zero levels, inflation spiked to millions-percent levels, gold stocks were completely depleted through 'mandatory loans' and the population suffered brutal massacres.

To make things even worse, civil war broke out almost immediately after liberation, as the Communist Party, the most effective resistance movement during the occupation, attempted to seize power by force, counting on the support of a large part of the population (not the majority though). The civil war not only destroyed what was left of the Greek economy. It also buried the hopes of restoring meaningful democracy. The government forces finally won, but they outlawed the Communist Party and imposed semi-authoritarian rule. The ban effectively meant that communists, socialists and even some social democrats were segregated from the political process. During the next decades, thousands were imprisoned for their political beliefs, while others were sent into exile on deserted islands and died there. Elections were rigged and the king often intervened arbitrarily to weaken the power of even centrist political forces. The fear of a 'leftist resurgence' meant that in the context of the Cold War authoritarianism and exclusion enjoyed the support of the US. (Greece had become, in the meantime, a member of NATO). In 1967, after a protracted period of political upheaval, the country suffered yet one more military dictatorship, which lasted for seven years and faced no massive resistance, until 1973.

When democracy was finally restored, in 1974, the new centre-right government lifted the ban on the Communist party, the king was overthrown by a referendum and the new constitution secured all basic political and social rights. Nonetheless, the damage had already been done: since 1936, two generations of Greeks had been born and grown up in a country where state authority enjoyed little or no democratic legitimation whatsoever. The clock of democratic development had stopped in the Interwar period.

However, despite its poor economic condition and its underdeveloped democracy, Greece became a full member of the European Communities in 1981. It was a unique event, in the sense that this was the only European enlargement which included only one new member and it was decided despite against the advice of the European Commission and despite the unanimous disapproval of the Greek opposition. It was ironic that the Socialist Party (PASOK), which opposed membership in the EEC more than anyone else, won the elections just a few months after Greece became a member. PASOK had promised a referendum on the issue, but never fulfilled its promise.

Andreas Papandreou, the charismatic leader of PASOK and a Harvard-trained former professor of economics at Berkeley, achieved a landslide victory in 1981 thanks to one major promise: to empower those who were excluded from Greek politics for the past decades. Although a son of a former prime minister (George Papandreou), he attempted to position himself outside

the political mainstream, articulating a radical populist political discourse. He claimed that all of Greece's problems were caused by the country's dependency on foreign powers and the interventions of the US in Greek politics. In other words, with the exception of junta sympathisers and right wing extremists, Greeks were not to blame for the continuing underdevelopment of their homeland. This 'soothing' narrative of victimisation became and still remains hegemonic in the public discourse of the country.

Besides the ethno-populist rhetoric, the first-ever electoral victory of a leftist party in Modern Greek history resulted in the abolition of the last remnants of post-war authoritarianism. WWII National Resistance fighters were given pensions, civil wedding was legalised, family law was modernised to secure gender equality, voting age was reduced to 18, dowry was abolished, a National Health Service was created, the first ever environmental protection measures in Greece were adopted, press freedom was finally realised and education, police and armed forces were all liberalised.

On the other hand, Papandreou's unfortunate idea for enfranchising the excluded was to hire them in the public sector. At least 220,000 more civil servants were added to the state workforce over the next eight years. Private companies at the brink of collapse were nationalised and hundreds of new ones were created. Even if Papandreou hoped that he could build 'national champions' this way, the result was the creation of national liabilities. Examinations for entry in the public service were abolished and one of the first actions of PASOK after taking office was to announce immediate pay raises in the public sector of up to 88% (!) and pension raises of up to 76% (!).

Obviously, the only way to finance this gigantic public sector was through loans and money printing (currency devaluation). Public debt increased from 34.5% of GDP in 1981 to 69.9% in 1989. The government of New Democracy which succeeded Papandreou claimed that the true numbers were much worse and that it was forced to reveal hidden debt, amounting to several GDP percentage points. Public deficit reached double digit numbers in 1985 (11.4%) and remained persistently high for a whole decade, reaching a whopping 16.1% in 1990. For all these years, Greece struggled to avoid bankruptcy.

It is also worth mentioning that these expansionary policies had no effect whatsoever on growth, which remained stagnant to near zero levels through the 1980s. This was because no consistent efforts were made to build a solid productive base for the Greek economy, to stimulate research and innovation, to enhance competitiveness. Moreover, the gargantuan public sector gave a whole new meaning to the concept of bureaucracy by continuously inventing obstacles to entrepreneurship and making the life of the people who had to deal with the state miserable. Even more importantly though, this perverse enfranchisement effort did not repair the broken trust bond between citizens and state. Cronyism, corruption and nepotism by the post-war authoritarians were replaced by cronyism, corruption and nepotism by PASOK supporters. The culture nurtured by Andreas Papandreou meant that the major incentive to join a big political party was the expectation for a placement in the public

sector, not the willingness to participate in the political process. Finally, PASOK lost the 1990 elections, amid a climate of scandals, anaemic economic growth and social unrest.

The centre-right New Democracy embarked on a project of liberal economic reforms and fiscal consolidation. The problem was that PASOK still controlled the trade and workers' unions and led them to revolt against the new measures. Moreover, the tightening of fiscal policy had adverse effects on the fledging economy. Hence, in 1993, PASOK re-emerged victorious after the parliamentary elections. However, times had changed, the country was on the brink of a catastrophic economic implosion and, hence, PASOK was obliged to change its ways. During the following years, it re-established a sense of meritocracy in the public sector by re-introducing impartial exams, organised by an independent watchdog (ASEP), for those interested in working for the state. PASOK also followed a hard-currency policy, which helped bring skyrocketing inflation under control. Moreover, fiscal consolidation continued but, at the same time, a gigantic public investments and infrastructure programme, co-funded by the EU, fuelled sustainable growth. Also, the new government adopted measures to combat tax evasion, introduced significant structural reforms and reduced bureaucracy and the hiring of civil servants. Finally, after the illness and subsequent death of Andreas Papandreou and his replacement by Costas Simitis at the PMs office, the government implemented an ambitious privatisation programme thanks to which public debt did not increase despite all the money spent on public investment.

Nonetheless, two contingent developments threw Greece off course: the first one was the sentimentally driven decision to host the Olympic games in Athens. Obviously, the public works projects, which started in 1997, in order to prepare the Greek capital for this event, fuelled growth. But the cost was unbearable, since almost all of these sports facilities proved useless after the Games. Much needed funds were misallocated. Not only was Greece the smallest country ever to host the Olympics, but, also, due to the security paranoia in the aftermath of the 09/11 attacks, it was forced to host the most expensive Games in history. Even if there were no bribes and overspending involved, this was too much for a country striving to achieve balanced budgets.

In addition, Greece and Turkey reached at the brink of war in January 1996.¹ The fear of an imminent attack after the incident, led the Greek government into the adoption of the largest military build-up programme in the country's modern history. This was another poor decision, since it was clearly impossible for Greece to match NATO's second largest army in spending. Still, relative to GDP, the country spent far more than any other European nation on defence.

¹ On 8 September 1996, a pair of Greek Mirage 2000's intercepted a pair of Turkish F-16's over the Aegean. One of the Turkish F-16's was shot down by a Mirage, its pilot got killed. The incident took place in the context of Greek-Turkish controversies over sovereignty and related rights in the area of the Aegean Sea.

The result was that Greece achieved good progress and steady growth during the 1990s, but not enough fiscal consolidation to fulfil the Maastricht criteria for the adoption of the euro. We now know with certainty that it managed to get in with false data. For most Greeks, this is not a reason to be ashamed, since “everybody cheats on their stats. It’s just that Greece got caught”. Even though there is no way to prove that this common belief in Greece is valid, it is certainly true that, even according to official Eurostat data, most countries in the eurozone (including Germany and France) systematically overshot the 3% deficit limit throughout the first decade of the 21st century.

When the sky fell on our heads

What triggered the 2009 crisis was not false data. The decisive factor was that Greece essentially ceased its efforts to reform after the adoption of the euro. Haunted by the stock market bubble of 1999 and exhausted by the continuous fights with trade unions, the Simitis government called it quits. Growth continued to be strong though, because the public investment programme peaked ahead of the Olympics, while the sharp reduction of interest rates on government bonds and bank loans after the adoption of the euro kept the economy afloat. The international climate was also favourable for the powerhouses of the Greek economy (tourism, shipping) and tension in Greek-Turkish relations eased. Even more importantly, continuous pay rises in both the public and the private sector boosted private consumption. Salary expenses in the Greek public sector increased by 117% between 1999 and 2009!

For some time, it all seemed perfect. Public debt was still above 100% of GDP, but growth was strong enough to keep it under control. Greece was ranked among the 30 richest countries in the world and the 22 most developed ones according to the UNDI. All measures that could combat tax evasion, corruption and bureaucracy, reduce the size and increase the efficiency of the public sector and all structural reforms which could enhance innovation, transparency, and competitiveness were postponed until the distant future. The Karamanlis government, which succeeded Simitis in 2004, never pursued them. Why lose time in bloody skirmishes with vested interests, when everything is going well?

It should have been obvious then, that it was all too good to be true. To paraphrase the word of the architect in the movie “The Matrix”, it was “a triumph equalled only by its monumental failure”.

The recession of 2008-09 had adverse effects on both tourism and shipping (Greek shipping tycoons own the largest fleet in the world), while the collapse of Lehman Brothers and the subsequent tightening of money supply had catastrophic effects on an economy which rested on private consumption and public investment to grow. Immediately, Greece fell into recession. The real problem, however, was that when fiscal deficit numbers overcame GDP growth numbers, the country’s huge public debt could no longer be serviced in an environment of scarce liquidity. It would be an understatement to say that the government of George Papandreou, which won the October 2009 elections, fell into panic mood.

With little knowledge of finance, the new PM, who owed much of his popularity to the fact that he was the son and the grandson of two former prime ministers, immediately started discussing, in private, the possibility of an IMF loan. However, he underestimated the amount of money that Greece needed in order to continue refinancing its debt. He also delayed adopting fiscal consolidation measures in the hope of a drastic European intervention. His expectations proved unfounded, since neither Berlin nor Brussels understood the full extent of the crisis and Greece finally asked for IMF/EU assistance. The stability programme agreed on, in unprecedented haste, projected the most drastic deficit reduction in modern history for any developed country and it was certain that it would deepen recession. Moreover, the Troika of international lenders (Eurozone, IMF, ECB) did not press the government enough on the issue of tax evasion and the combating of black economy. For them, any additional benefit on these two fronts would only be a welcome bonus, not a premise for the success of the programme.

In spite of this, 54.2% of Greeks supported the IMF Fiscal Adjustment Programme, according to a survey conducted a few days after it was approved in Parliament (May 2010). Their trust in the expertise of the IMF/EU technocrats and Greek government officials was shattered by harsh reality. Indeed, the virtual annihilation of public investment, salary cuts and steep tax rises, led to an immediate 5% slash in public deficit. At the end of 2010, Greek deficit stood at 10, 5% of GDP (from 15, 7% in 2009). By comparison, British deficit stood at 10, 3%, Portuguese deficit at 9, 8% and Spanish deficit at 9, 3%.

However, although Britain, Spain and Portugal had similarly high deficits, none of them was forced by the EU or attempted by itself to slash them as sharply as Greece. A 5, 1% deficit drop in one year is one of the largest, if not the largest, ever achieved in any OECD country. However, the price of such harsh austerity was the deepening of the recession way beyond the projections of both the Troika of international lenders and the Greek government. The result was that public debt to GDP ratio increased, since GDP decreased. Thus, the fiscal consolidation programme has so far failed to achieve its targets

Public attitudes towards the EU and the IMF changed, as the rise in debt gave the impression that all those sacrifices had been in vain. In September 2011, the majority of Greeks still supported structural reforms, but – according to most polls – eight out of ten were against the specific fiscal consolidation programme pursued.

The Greek government did too little too late to reform and downsize the public sector and, until its fall, in November 2011, had not privatised a single public company, nor did it sell or lease a single hectare of public land. Private sector employees continued paying in order to feed the Leviathan. Even though public servants also suffered wage cuts, they got to keep their often unnecessary jobs, since the government wanted to keep its 'clients' on the payroll at any cost. With the exception of the 'Kallikratis' programme to

improve local and regional governance, no efforts were made to reform the efficiency of the public sector. Structural reforms in the social security, health and pension system were also too timid to address the challenge of a rapidly ageing population and vested interests were not touched. Some measures to combat tax evasion and corruption were adopted, but paled in comparison to the size of the problem. Other reforms (e.g. education) will take long before showing real results. At the same time, public sector workers and practitioners of closed and protected professions staged continuous strikes, giving the final blows to an economy and society already on their knees. It is worth underlining that not all Greeks revolted against reforms; only public servants and closed professions. One should always remember that each time 50,000 people belonging to the aforementioned groups staged a rally, there were 4,000,000 people in Athens still trying to get to work or just survive in a city where nothing was functioning.

Faced with unrealistic expectations from its creditors and governed by people clearly not up to the task at hand, Greece failed, despite the sacrifices of a significant part of the population. The government of Georgios Papandreou eventually fell, after an ill-judged attempt to hold a referendum and the necessity of a 50% haircut for privately held Greek bonds in order to keep the country in the eurozone. However, this decision meant that the unthinkable was now possible: if a developed eurozone member can get away with writing off some of its debt, why not others as well? Spreads in both the periphery and the core of the eurozone increased, while uncertainty paved the way for a new recession.

What is to be done?

No matter what happens in the eurozone, there are no easy fixes to the Greek problem. Until the outbreak of the crisis, Greece's economy was based on five pillars: private consumption, public investment, housing and construction, tourism and shipping. Private consumption cannot resume in the absence of cheap credit and public investment projects are now unthinkable given the size of the public debt (even after the haircut). Construction and housing have reached their limit and Greece only narrowly escaped a catastrophic bubble. Tourism and shipping are extremely volatile and depend entirely on global economy trends. The bonds haircut will only help Greece if the eurozone does not fall into another recession, which would eliminate its benefits. And, finally, leaving the eurozone does neither make political nor economic sense. Unlike Argentina, Greece is not a net exporter of raw materials and exports only marginally affect its GDP. It would have no resources whatsoever to support its new currency and devaluation would not help, just as it did not help back in the 1980s.

Obviously, the issuing of Eurobonds and a generous 'quantitative easing' from the ECB would give Greece, as well as the region as a whole, valuable breathing space and it is necessary in order to save the European unification process. Investment and public private partnerships could also resume if the Eurozone offers lines of credit to healthy and solvent Greek businesses. Most importantly though, Greek governments should be pressured by their European counterparts to lay the foundations for a solid production base in

fields where the country enjoys competitive advantages, like renewable energy, tourism, shipping, sea and air transport hubs and organic farming. This reshaping of the economy will take time and it will require the expertise of the IMF and the EU as well as the active involvement of the Greek private sector. The same can be said for structural reforms in the direction of competitiveness, productivity, transparency, openness and efficiency. In other words, time is what Greece desperately needs in order to strengthen its democratic institutions and its economy. But, in our days, this is a resource even more scarce than money.

Dr. **Nikos Chrysoloras** is a journalist at the Greek daily [Kathimerini](#), where he is currently managing the opinion pages. He studied International Relations at the University of Wales, Political Theory at the University of Essex and Government at the London School of Economics, where he was awarded his PhD, with a full scholarship. He has also worked as a columnist for the business news website [Reporter.gr](#) and as a researcher for [SKAI TV](#) in Greece and taught Political Theory and Media History in London and Athens respectively. The views expressed here are personal.



Europe for Citizens
Programme



This project has been funded with support from the European Commission.
This publication reflects the views only of the author, and the Commission cannot be held responsible for any use which may be made of the information contained therein.