When the Greek Political System Clashed with Europe: Why the Greek Sovereign-Debt Crisis is Taking so Long to End?

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When the Greek Political System Clashed with Europe: Why the Greek Sovereign-Debt Crisis is Taking so Long to End?

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ABSTRACT

The central argument of this essay is that, in order to understand the reasons behind the Greek economy's inability to recover sooner from its 8-year recession, analysis must focus on the institutional, political and cultural traits of the country rather than take a primarily "economistic" approach and simply blame "excessive austerity" and/or the euro. In fact, it will be argued that Greece's positive performance under the euro (until government actions derailed the economy) is generally underappreciated, suggesting that if the country's institutional weaknesses are addressed, the economy will grow. If they are not, the country's long-term economic potential will almost certainly remain unfulfilled.

Keywords: Greek Economic Crisis, Austerity, Structural Reforms.

Yunan Siyasal Sistemi Avrupa'yla Çatışınca: Yunan Ulusal-Borç Krizinin Sona Ermesi Neden bu Kadar Uzun Sürdü?

ÖZET

Bu makalenin ana argümanı, Yunan ekonomisinin 8 yıldır devam eden durgunluğundan kurtarılmasındaki yetersizliğin arkasındaki sebepleri irdelemektir. Bu amaçla, yapılacak analizlerin 'ekonomik' bir yaklaşımla ve kolaycı bir biçimde 'yoğun kemer sıkma politikası' ve/veya Euro'yu sebep olarak göstermek söyleminden ziyade ülkenin kurumsal, siyasal ve kültürel özelliklerine odaklanılması gerektiği ileri sürülmektedir. Yunanistan'ın Euro'nun etkisi altındaki pozitif performansının (hükümetin uygulamalarının ekonomiyi dramatik şekilde etkilemesine kadar) değeri yeterince anlaşılmamıştır. Bu nedenle makalede, ülkenin kurumsal zayıflığı üzerinde yeterince durulması halinde ekonomin buna bağlı olarak büyüyeceği öne sürülmektedir. Eğer meseleye bu açıdan yaklaşılmaz ise ülkenin uzun dönemli ekonomik potansiyelinin hakkı verilmemiş olacaktır.

Anahtar Sözcükler: Yunan Ekonomik Krizi, Kemer Sıkma Politikası, Yapısal Reformlar.

Introduction

The unprecedented duration and depth of Greece's economic crisis have provided ample ground for debate among economists and policy experts. The main objects of dispute have been two: (i) the appropriateness of 'austerity' policies as a means to address issues of sovereign insolvency, particularly when linked to underlying 'competitiveness' problems; and (ii) the wisdom of monetary union in Europe (EMU) based on the current institutional arrangements, absent more decisive steps toward political unification.

The central theme of this essay will be quite different. It will be argued that Greece's current economic problem is not *primarily* one of misguided economic therapies or inappropriate monetary régimes – witness the recovery of such countries as Portugal and Cyprus that were in a similar (though not identical) predicament – but one of tremendous missed opportunities and policy failures linked to Greece's long-standing institutional, political and cultural traits and shortcomings. The extraordinary circumstances of the crisis have merely served to place, again, in sharp relief the latter's sway over Greece's fortunes.

It is not difficult to understand why many people blame excessive austerity and the euro for Greece's economic quandary: no other country has seen such a large and protracted shrinking of GDP and increase in unemployment since the Great Depression of the 1930s, despite being the beneficiary of the biggest international rescue effort ever. In this vein, many commentators have claimed that Greece should never have joined the euro in the first place[1] or, now that it has, should abandon it.[2, 3]

However, no other Eurozone member had also been caught breaking the EMU's rules so extravagantly. This added another level of complexity to Europe's eventual response: European leaders needed to show that EMU rules must not be taken lightly (and if they are, there will be consequences); at the same time, they had to ensure the survival of Europe's most ambitious project. Hence the "moral hazard" element, which constrained European creditors *politically* as to the kind of flexibility they could allow in the adjustment programmes. Yet, among all the 'programme countries' (Greece, Ireland, Portugal, Cyprus, Spain), it was Greece's governments that seem to have had the greatest difficulty 'internalising' this matter, and acting accordingly.

More than focusing merely on the economic policies prescribed, and the euro, therefore, an *ex post* evaluation of the Greek adjustment programme should be set in a wider 'institutional' *problématique*[4] that places at centre-stage such concepts as:

1 German Chancellor Angela Merkel in 2013; see T. Mark Thompson, "Greece joining euro was a mistake: Merkel", 28 August 2013, http://money.cnn.com/2013/08/28/news/economy/merkel-greece-euro/index.html (Accessed on 15 October 2017). Also see, Former French President Valéry Giscard d'Estaing, "Seventeen Countries Were Far Too Many", Spiegel Online, 11 September 2012, http://www.spiegel.de/international/europe/spiegel-interview-with-helmut-schmidt-and-valery-giscard-d-estaing-a-855127.html (Accessed on 25 November 2012).

2 The list of pundits holding this view is too long to catalogue here. They all deplore the loss of the exchange-rate instrument as a means of restoring competitiveness". See, Tim Worstall, "Greece Really Should Leave the Euro, The Economics Is Entirely Clear Here", 25 July 2015, https://www.forbes.com/sites/timworstall/2015/07/25/greece-really-should-leave-the-euro-the-economics-is-entirely-clear-here/#5dd245115bcf (Accessed on 10 September 2017).

3 See also, German (ex-) finance minister Wolfgang Schäuble's infamous proposal, in 2015, for Greece to take a temporary 'time-out' from the euro: an 'economic' solution to what is at core an 'institutional' problem. Constantine A. Papadopoulos, "Wolfgang Schäuble and the temporary 'Grexit': the tale of a dangerous misunderstanding", International and European Policy, Vol.34-35, March-October 2015, p.45-63, Papazissis Publications, Athens (in Greek).

4 The literature taking an 'institutional' approach to the singular Greek case is growing. See, Costas Meghir, Christopher A. Pissarides, Dimitri Vayanos and Nikolaos Vettas (eds.), Beyond Austerity, Reforming the Greek Economy, MIT Press, 2017.

Political will: a sincere desire to learn from the past; an unambiguous determination to forge ahead, irrespective of political cost, fully exploiting the opportunities on offer ('cash-for-reforms'; the chance to introduce additional home-grown reforms).

Trust: the political leadership's ability (or inability) to inspire confidence in others (citizens and foreign partners) about one's political will to actually reform, all the while abjuring any resort to delaying tactics or attempts to surreptitiously roll back adopted reforms.

Political and societal concord vs. divisiveness: the ability of the political system to work together (or not) in the national interest in the face of unprecedented economic and social, almost existential, challenges.

Technical competence (at the level of the political leadership and the administration), including an ability (or incapacity) to take a pro-active, as opposed to passive, stance *vis-à-vis* the reforms task ahead. This item is linked to the wider, longer-term, issue of the overall robustness (or weakness) of the country's institutions (government, civil service, the judiciary, educational system, the press, etc.).[5]

In Greece, there is near-universal agreement that the country suffers enormously on every one of these counts. The inordinate length of the adjustment – Greece, after all, has been under international (EU-IMF) tutelage for nearly eight years; originally, a 3-year IMF-style Stand-By Arrangement was thought (rightly or wrongly) to suffice – has served to promote/validate this impression, one which an increasing number of academic, technocratic and political sources have called attention to since, albeit in a piecemeal way.[6] In such circumstances, abandoning/relaxing policies of adjustment/reform or leaving the euro not only would not solve the underlying problem, *viz*., the country's institutional/structural deficiencies; it would aggravate it due to the removal of any external discipline to craft better public policies. Moreover, leaving the euro would compound the situation, *inter alia*, due to the impact of a range of potentially devastating short-to-medium-term economic consequences, fully acknowledged, ironically, even by proponents of "Grexit".[7]

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5 This issue is related to the wider notion of 'competitiveness' understood to include all those variables routinely analyzed in various international competitiveness and governance rankings developed by such organizations as the World Bank, the World Economic Forum, the Institute of Management Development, etc., including quality and efficiency of governance, rule of law, property rights, enforcement of contracts, flexibility of labor markets, availability of credit, customs formalities, administrative procedures, regulatory transparency, etc.

6 Kevin Featherstone attributes recent 'reform failures' to the crafting of the conditionality strategy and to conflicting interests, administrative traditions and cultural norms. Kevin Featherstone, "External conditionality and the debt crisis: the 'Troika' and public administration reform in Greece", Journal of European Public Policy, Vol.22, No.3, 2015, p.295-314; Klaus Regling, European Stability Mechanism managing director, has expressly blamed Greece's 'weak administration' for the inordinate duration of the programs. See, Klaus Regling, "Wie die Währungsunion wetterfester wird", Frankfurter Allgemeine Zeitung, 11 August 2017, https://www.esm.europa.eu/sites/default/files/2017_11_08_faz_op-ed_de.pdf) (Accessed on 10 November 2017). More diplomatic, Cypriot finance minister Harris Georgiades has suggested the need for Greece to get rid of the 'deadweights' holding back its prospects for development. "Ten governments, four prime ministers, 433 portfolios", Kathimerini, 30 September 2017 (interview). For a broader discussion of all these themes, see, Spyros Economides (Ed.), Greece: Modernisation and Europe 20 years on, Hellenic Observatory, London School of Economics and Political Science, p.54-63, July 2017, http://www.lse.ac.uk/europeanInstitute/research/hellenicObservatory/CMS%20pdf/Publications/Modernisation_%20Publication.pdf (Accessed on 10 October 2017).

7 Hans-Werner Sinn, "Why Greece Should Leave the Eurozone", The New York Times, 24 July 2015, http://www.nytimes.com/2015/07/25/opinion/why-greece-should-leave-the-eurozone.html?_r=0 (Accessed on 5 October 2017); James K. Galbraith, Welcome to the Poisoned Chalice: The Destruction of Greece and the Future of Europe, Yale University Press, New Haven and London, 2016, Chapter 30.

Greek Membership of the Euro: a success story…

Critics of Greece's participation in Europe's monetary union focus on the crisis that broke out in 2009 and ignore the Greek economy's achievements during the whole period from the start of nominal convergence in the mid-1990s until the latter part of the following decade whereupon the government then in power (conservative New Democracy, 2004-2009) hugely violated the Maastricht convergence rules. In so doing, the critics have often ended up advocating major policy shifts that, in effect, either require more (foreign) money (relaxing fiscal consolidation policies/debt relief), or promulgate the monetary equivalent of throwing the baby out with the bathwater (returning to the drachma).

Five economic measures indicate just how much Greece profited from euro membership: First, GDP growth. Whereas Greece's first decade as a member of the European Communities in the 1980s was another instance of EU-driven opportunities foregone (average annual growth in the drachma period 1981-1990 was 0.9%[8], leading Greece to *diverge* from its new partners), in the following two decades the country fared better, especially after the mid-1990s, when the government embarked in earnest on the road to nominal convergence. From 1996 until 2007 (when GDP peaked at €250.7bn), the average rate of growth was 3.9% *per annum*, a performance second only to Ireland's.[9]

Second, productivity growth. In the period 1996 to 2007, *productivity in Greece grew at the fastest rate anywhere in the Eurozone*: 2.6% per annum on average. This was more than eight times faster than in Spain (0.3%), almost twice as fast as in Portugal (1.4%), and almost two-and-half times faster than in Germany (1.1%). Even Ireland's productivity growth was less rapid (2.5%).[10]

Third, exports. Exports of goods and services have always been the Greek economy's Achilles' heel. Yet the period under examination saw considerable progress on this score. Whereas in the Eurozone member states as a whole, in the period 1996-2007, exports of goods and services grew on average 7.6% *per annum*, in Greece they grew one-and-two-thirds times as fast, *viz.*, 12.8%. This growth rate was faster than Germany's (8.3%), Spain's (8.7%) or Portugal's (7.2%), and was even marginally ahead of star-exporter Ireland's (12.5%).[11] Furthermore, it occurred in a novel "hard" currency environment.[12]

Fourth, gross fixed capital formation as a percentage of GDP.[13] Prior to 1996, GFCF as a percentage of GDP never exceeded 20% in Greece (20.9% in the Eurozone in 1996). After 1996, this ratio began to gradually surpass the Eurozone average[14], reaching a peak of 24.6% in 2007 *vs*. 23% in the Eurozone (and 20.1% in Germany, 29.6% in Spain, 22.1% in Portugal and 26.2% in Ireland).[15]

Fifth – indicative of the Greek economy's increasing extroversion and growing influence as a regional power – outgoing foreign direct investment. From the mid-1980s to the mid-1990s, the stock

8 All GDP rate-of-change calculations are based on Gross Domestic Product at 2010 constant prices data provided by the European Commission's Macro-economic database AMECO.

9 AMECO.

10 Calculations based on AMECO. Productivity is defined as GDP at 2010 constant prices per person employed.

11 Own calculations based on 'exports of goods and services at current prices (National accounts)' data from AMECO.

12 In the period 1981-1995, exports grew only 2.9% annually on average, despite the fact that the drachma lost over 80% of its value vis-à-vis the ecu; in 1996-2007, 9% (constant 2010 prices). For historical exchange rates, see http://fxtop.com/en/historical-exchange-rates.php?A=1&C1=GRD&C2=EUR&YA=1&DD1=01&MM1=01&YYYY1=1974&B=1&P=&I=1&DD2=31&MM2=12&YYYY2=2000&btnOK=Go%21.

13 Results calculated using the relevant tables (GFCF and GDP) from AMECO.

14 In the period 1996-2007, GFCF grew at an average annual rate of 7.5% vs.3.3% in the Eurozone.

15 AMECO, 2010 constant prices.

of outward Greek FDI hovered at just under US$ 3bn. However, by 1999 this number had doubled, and, starting in 2001, Greek companies embarked on a new wave of investment abroad. Thus, in 2001 the stock of outward Greek FDI was evaluated at just under €8bn; by 2007 it had reached €21.5bn and by 2010, €31.9bn.[16] This was an extraordinary development for a country that for decades had been used to exporting people, not capital.[17]

These five elements succeeded in deeply transforming the Greek economy. Without government efforts to meet the Maastricht convergence criteria, there is every reason to believe that Greece would have continued to suffer from high inflation, slow growth and low competitiveness. The arrival of the euro was the single most effective shock to both the politics and economics of the country since the 1950s and 1960s when a devastated Greece emerged from the ruins of the Second World War and a three-year civil war to become, by the beginning of the millennium, one of the most affluent nations in the world.[18]

… Turned own Goal

However, none of these achievements was without its downside. Growth performance, though satisfactory in nominal terms, was not necessarily sustainable or of high *quality*. Misguided government policies and institutional weaknesses have to carry much of the blame.

The underlying investment performance was not suggestive of a longer-term strengthening of the country's productive base. For example, in 2007 "dwellings" accounted for 40% of GFCF (42.4% in 1996), when a rate of approximately 30% was more typical in the Eurozone (28.9% in 2007).[19]

Exports as a percentage of GDP – despite their earlier remarkable growth rates – display one of the worst overall performances in the EU[20], being far lower than one would expect based on GDP, *per capita* income, Greece's membership of the Single Market, the size of its trading partners and geographic distance.[21] Indeed, exports in 2016 were lower than at their peak in 2008, even as the other ex-programme countries experienced an export revival.[22]

16 UNCTAD uses dollar figures prior to 2001; euro figures post-2001. UNCTAD, "Investment Country Profiles, Greece", February 2012, p.5, http://unctad.org/en/PublicationsLibrary/webdiaeia2012d9_en.pdf (Accessed on 15 September 2017).

17 Greek firms active abroad created no fewer than 90,000 jobs in the wider region by 2008, the lion's share being accounted for by banking (45,000), ibid., p.16.

18 Per capita GDP in 1950 was US$ 1,951, i.e., Greece was poorer than Peru, South Africa or Portugal (NationMaster). By 2007, Greece was almost on a par with Hong Kong, and richer than Israel or South Korea. See, Central Intelligence Agency (CIA), The World Factbook, Country Comparison: GDP - per capita (PPP), http://www.newestideas.com/factbook/rankorder/2004rank.html (Accessed on 4 November 2017).

19 AMECO.

20 Even at their peak in 2008, exports of goods and services did not exceed 23.3% of GDP (Eurozone: 39.9%). In 2016, the corresponding numbers were 30.1% (an arithmetic increase due entirely to the shrinking of the denominator, GDP) and 45.7%. France (28.8%) and Italy (30.0%) had similar relative performances to Greece in 2016, but their GDPs were over 11 and 8 times larger, respectively, i.e., they can afford to be more self-sufficient. Source: AMECO.

21 For a study that attributes this phenomenon, for the larger part, to weak institutional quality, see Uwe Böwer, Vasiliki Michou and Christoph Ungerer, "The Puzzle of the Missing Greek Exports", European Economy, Economic Papers 518, European Commission Directorate-General for Economic and Financial Affairs, June 2014, http://ec.europa.eu/economy_finance/publications/economic_paper/2014/ecp518_en.htm (Accessed on 1 November 2017).

22 Konstantinos Efstathiou and Guntram B. Wolff, "How export growth achieved adjustment of massive trade deficits in the euro area", Blog Post, Bruegel, 31 May 2017; http://bruegel.org/2017/05/how-export-growth-achieved-adjustment-of-massive-trade-deficits-in-the-euro-area/ (Accessed on 1 November 2017).

The stock of inward Foreign Direct Investment – one of the lowest in Europe even at its peak (2009: 12.8% of current GDP *vs*, *e.g.*, 48.5% in Portugal)[23] – was indicative of severe problems in terms of the general ease of doing business in the country. This was reflected in Greece's lamentable performance in the associated world rankings, among others, the World Bank's[24]. Furthermore, this only served to exacerbate the country's already poor showing in the European Commission's Internal Market Scoreboard[25] (a state of affairs, however, which improved dramatically once Greece came under the Memoranda régime.[26])

A considerable amount of the growth registered, especially after 2003, can be explained by the observed increase in net new borrowing by the government (*excluding* interest), causing overall fiscal and monetary policy (the former even more so than the latter) to be strongly pro-cyclical. Whereas from the mid-1990s until 2002 the country was actually recording primary budget surpluses (essentially, borrowing to pay down existing debt), from 2003 to end-2009 (just a few months before Greece was cut off from international markets), the government embarked on a new borrowing spree. In fact, *primary* net borrowing rapidly accelerated toward the end of the period[27] – no doubt in a futile effort to counter the oncoming recession. It peaked at €24bn in 2009, or 10.1% of GDP![28]

As this government borrowing was channelled to public-sector spending more than anything else (hiring and salary increases[29]), it already added to a weak current-account position, leading in 2008 to a near world-record current-account deficit of 15.8% of GDP.[30] By 2009, state spending amounted to the equivalent of 54.1% of GDP; most years from 1996 to 2006 it hovered between 45% and 47% of GDP.[31]

In this environment of artificially-boosted aggregate demand, excessive wage-and-salary increases were not limited to the public sector. Economy-wide unit labour costs increased faster than anywhere else, eroding competitiveness further.[32]

23 Own calculations based on data from UNCTAD's Data Center.

24 In 2009, Greece was 96th in the world on the overall score. In 2017, this ranking had improved, and Greece had moved up to 67th place, but still was last in the EU. See, various Doing Business reports of the World Bank. Also, the Institute of Management Development, in its 2017 World Competitiveness Yearbook, placed Greece in 57th position (out of 63 countries), second to last in the EU. Finally, Greece occupied the last position in the EU (48th overall) in the World Economic Forum's 2017 Global Human Capital Index.

25 The Scoreboard indicates compliance with new Single Market rules. European Commission, *Single Market Scoreboard*; http://ec.europa.eu/internal_market/scoreboard/performance_by_member_state/greece/index_en.htm (Accessed on 1 October 2017).

26 See the European Commission's *Single Market Scoreboard*.

27 See European Central Bank Statistical Data Warehouse, https://sdw.ecb.europa.eu/quickview.do?SERIES_KEY=325.GFS.A.N.GR.W0.S13.S1._Z.B.B9P._Z._Z._Z.XDC_R_B1GQ._Z.S.V.N._T (Accessed on 10 October 2017).

28 AMECO. In fact, in the period 2003-2009, the average annual rate of growth of primary borrowing outstripped the corresponding rate of GDP growth (current prices) by a factor of 46! (GDP growth: 2.9% *p.a.*; net borrowing growth: 133.5% *p.a.*).

29 In the period 1996-2004, the total public-sector wage bill averaged 22.9% of total government spending. In the period 2005-2009, it had edged up to 24%. In the period 2007-2009 alone, the public-sector wage bill increased from €25.8bn to €31.1bn, a 20.5% nominal increase! See, AMECO.

30 AMECO.

31 AMECO, own calculations.

32 Between 2000 and 2010, real unit labor costs grew faster in Greece than anywhere else in the group of 28 'industrial' countries examined by AMECO.

The Years of Living Insouciantly

In the earlier part of the euro-fuelled boom years, the good overall performance of the Greek economy lulled policy-makers into complacency, leading them to gloss over the weaknesses of the economy and continuously postpone the necessary reforms.

In fact, the problem might have been worse than that. There is evidence that the government then in power (socialists Pasok) did not appreciate the fact that achieving euro membership was not the end of the road, but actually the beginning of a whole new chapter of policy-making requiring fundamental reforms to make the real economy more flexible and adaptable, *inter alia* to compensate for the surrender of the exchange rate as a policy instrument.

Thus, early euro-era economic policy was entirely dominated by the Maastricht-sanctioned twin concerns of keeping inflation low and pursuing a budgetary policy that did not lead to runaway deficits. These goals were reasonably achieved in the first part of the previous decade, but any attempt at serious reform was quickly put to rest for fear of stoking popular reactions and generating undue 'political cost'. This whole paradigm is exemplified by the failed attempt, in 2001, to modernise the social-security system. Instead of voluntarily embarking on a serious programme of structural and administrative reforms and communicating to the public the vital importance of such a policy, the Pasok government reverted to Greek political parties' age-old strategic proclivity to make crowd-pleasing proclamations, backed by promises of largesse, in the event epitomised by the so-called 'Convergence Charter', a vain blueprint promising to distribute, prematurely, to the public the 'dividend' from Greece's entry into the Euro.[33]

The next government, New Democracy, placed an even bigger –fatal, this time – wedge between its policies and the real needs of the economy. Though nominally wedded to the idea of fiscal rectitude (and a standard set of minimal reforms), ND presided over a budget deficit that shot up to 15.1% of GDP in 2009 (from an already excessive 6.4% in 2003)[34]; the public debt increased by 64% in absolute numbers (2004-2009) to reach 130% of GDP, and public *external* debt went from 71% of GDP in 2004 to 111% of GDP in 2009, *i.e.*, it doubled in absolute terms in just five years![35] Therefore, not only was there no real attempt to push through significant supply-side reforms; the government massively failed to abide even by the default position, *viz.*, simple adherence to the basic Maastricht fiscal-management framework. The most paradoxical element in all of this was the fact that it was the in-coming New Democracy government that raised, in 2004, the issue of the veracity of Greek statistics (mainly to belittle the achievements of its predecessor), only to be told by the European Commission, a full six years later, that it had found evidence of 'severe irregularities' in the statistics

33 The 'Convergence Charter', the brain-child of then PM Costas Simitis, offered a roadmap toward a more socially and regionally just society, and included essentially a series of declaratory statements advocating improvements in the economy (many of which were mere repetitions of the EU's Single Market programme) and the public administration. It was also notable for avoiding any reference to the economy's most acute problems (*e.g.*, the lack of extroversion; the unsustainability of the pensions system), and for promising to increase social spending to levels surpassing the EU average. See, Costas Simitis, "Convergence Charter", Speech at the Zappeion Palace, 10 September 2003.

34 AMECO.

35 This largely explains the near doubling of the public-sector wage bill in those years, and, *e.g.*, the reported rise in public expenditures for medicines from €4bn to €8bn in the same period. International Monetary Fund, *GREECE, Request for Stand-By Arrangement*, 5 May 2010, p.125, http://www.imf.org/external/pubs/ft/scr/2010/cr10110.pdf (Accessed on 30 August 2017).

submitted in April and October 2009[36], leaving "the quality of fiscal statistics subject to political pressures and electoral cycles."[37]

Equally embarrassing for the ND government, the Commission, after placing Greece under the Excessive Deficit Procedure in May 2004 until early 2006, was forced to re-initiate the EDP in 2008 after it found that in 2007 the general government budget deficit had exceeded the permissible (3%-of-GDP) limit again (it reached 3.5%)[38], despite still-high growth rates. It was only in July 2017 – after eight years of relentless austerity – that the Commission finally recommended that Greece be removed from the EDP procedure.[39]

Thirty Years' Worth of Reforms in Three?

It is impossible to guess what the Greek economy's reaction to the international financial crisis would have been in the absence of such grave fiscal mismanagement and structural rigidities. There is an argument according to which the country's relatively closed economy would have spared it some of the most severe consequences affecting Europe. Be that as it may, it remains a fact that, once begun, the recession in Greece took longer to reverse precisely because the Greek economy was not sufficiently integrated with the outside world (exports; inward foreign direct investment). These were exactly the structural factors that should have been addressed first and foremost following the onset of the recession. Though occupying very prominent positions in the country's adjustment programmes, these "chapters" never received the kind of attention they deserved from the government, due partly to the latter's inability to understand and correctly prioritise the needs of the country, partly to the very complexity of the issues at stake (which often went beyond the change-instituting capacity of the state apparatus), and partly to a basic antipathy, on the part of Greek politicians and public opinion in general, to change *per se*, including privatisations and often foreign investment as well. Instead, the onus of adjustment was placed on fiscal consolidation – understandable, in the short term, given the severity of the problem, but counterproductive in the medium term (insofar as the associated contractionary effects upended any expansionary effects coming from the implementation of reforms, such as they were[40]) and, of course, ineffectual in the long term.

This is not to deny that many reforms have been adopted (though, often, actual implementation is another matter, as noted by the lending institutions[41]). Greece has eliminated its enormous budget

36 European Commission, "Report on Greek Government Deficit and Debt Statistics", Brussels, 8 January 2010 COM(2010) 1 final, p.3-4; file:///C:/Users/CONSTA~1/AppData/Local/Temp/COM_2010_report_greek.pdf (Accessed on 15 September 2017).

37 Ibid., p.4.

38 Commission of the European Communities, *Report from the Commission – Greece – Report prepared in accordance with Article 104(3) of the Treaty*, Brussels, 18.2.2009 SEC(2009) 197 final, p.3-5, http://ec.europa.eu/economy_finance/economic_governance/sgp/pdf/30_edps/104-03/2009-02-18_el_104-3_en.pdf (Accessed on 5 October 2017).

39 European Commission Excessive Deficit Procedure, https://ec.europa.eu/info/business-economy-euro/economic-and-fiscal-policy-coordination/eu-economic-governance-monitoring-prevention-correction/stability-and-growth-pact/corrective-arm-excessive-deficit-procedure/ongoing-excessive-deficit-procedures/greece_en (Accessed on 5 October 2017).

40 Nicos Christodoulakis, "Sisyphus vs. Ulysses: Reform failure and the need of a new policy framework for Greece", Spyros Economides (ed.), *Greece: Modernisation and Europe 20 years on*, Hellenic Observatory, London School of Economics and Political Science, p.54-63, 2017, http://www.lse.ac.uk/europeanInstitute/research/hellenicObservatory/CMS%20pdf/Publications/Modernisation_%20Publication.pdf (Accessed on 5 November 2017).

41 Hence, many of the 'prior actions' demanded by the lenders to release loan funds included the implementation, *in practice*, of measures previously adopted in the context of earlier reviews.

deficits, while reducing public-sector employment by a quarter. According to the OECD, Greece was by far the fastest-reforming country from 2010 until at least end-2014 (though slipping very substantially in the period 2015-16[42]).[43] However, such was the backlog of needed reforms that even today certain important performance indices continue to be below the OECD and EU averages (due to, *e.g.*, regulatory barriers to competition in network industries such as energy and transport, administrative inefficiencies, and poor educational outcomes[44]).[45]

The Troika, despite oft-repeated objections to the introduction of more and more taxes and salary and pension cuts, and its insistence on the need to accelerate the implementation of structural reforms (expressed at least since May 2011[46]), proved unable to correct the skewed manner of implementation[47] of the programme on the part of the Greek authorities. By default, it focused meticulously on the fiscal targets, a tendency probably also owing much to the structure of the 'conditionality' clauses contained in the loan agreements: whereas the loan instalments are approved on the basis of more general assessments regarding the programme's progress, quantitative criteria are comprehensively applied only to the fiscal targets. In contrast, progress on the 'structural reforms' agenda is monitored by means of a series of 'benchmarks', by nature more flexible and 'qualitative'; indeed, such benchmarks have not been adopted in all sectors. Which helps explain why the Troika regularly confirmed that the programme remained on track, at the same time that its officials publicly admitted that key structural policies such as the fight against tax evasion, the opening of closed professions and the modernisation of the public administration had disappointed on many counts, not to mention engendered a socially-unfair distribution of the adjustment burden.[48]

For their part, Greek governments, in a tacit acknowledgment of these weaknesses, have frequently over-performed on the fiscal targets, thus hoping to compensate for any failings in other areas.

The public administration's resistance to implementing reforms in the economy, as well as to reforming *itself*, is probably the least understood and least appreciated variable in the whole adjustment

42 In the period 2015-2016, Greece came eighth (with Mexico and China) among 41 countries surveyed. OECD, *Economic Policy Reforms: Going for Growth*, OECD Publishing, Paris, 17 March 2017, Ch. 1, Fig. 1.2, http://www.keepeek.com/Digital-Asset-Management/oecd/economics/economic-policy-reforms-2017/the-pace-of-reform-has-slowed-in-more-than-half-of-the-countries-but-has-accelerated-in-some_growth-2017-graph2-en#.WcpzqNFx1PY (Accessed on 1 October 2017).

43 OECD, *Economic Policy Reforms 2017: Going for Growth*, OECD Publishing, Paris, 17 March 2017, p.2, http://www.keepeek.com/Digital-Asset-Management/oecd/economics/economic-policy-reforms-2017/overview-of-structural-reform-progress-and-identifying-priorities-in-2017_growth-2017-4-en#.WcphjNFx1PY#page5 (Accessed on 1 October 2017).

44 OECD, "Greece", in *Economic Policy Reforms 2017: Going for Growth*, OECD Publishing, Paris, p.201, http://dx.doi.org/10.1787/growth-2017-24-en (Accessed on 1 October 2017).

45 For further evidence, see also the World Economic Forum's *Global Competitiveness Report 2017-2018*, which places Greece 87th out of 137 countries and last in the EU. World Economic Forum, "2017 Global Human Capital Index", https://weforum.ent.box.com/s/dari4dktg4jt2g9xo2o5pksjpatvawdb (Accessed on 4 October 2017).

46 Poul Thomsen, Deputy Director, European Department, IMF, Speech, "15th Roundtable with the Government of Greece", Economist Conferences, Lagonissi, Attica, Greece, 18 May 2011.

47 European Court of Auditors, "The Commission's intervention in the Greek financial crisis", *Special Report,* No.17, European Union, 2017, p.8-10, https://eca.europa.eu/en/Pages/DocItem.aspx?did=43184 (Accessed on 20 November 2017).

48 Poul Thomsen, Deputy Director in the IMF's European Department, Speech at the 17th Economist Roundtable with the Government of Greece, Athens, Greece, 15 April 2013, https://www.imf.org/en/News/Articles/2015/09/28/04/53/sp041513 (Accessed on 20 September 2017); Public-sector compensation-of-employees-as-a-percentage-of-GDP shrank between 2009 and 2016 (from 13.1% to 12.4%), but only half as much as in the rest of the economy (22.7% to 21.2%), AMECO.

programme policy mix. This fact has critical implications in terms of a proper *ex post* evaluation of the effectiveness, appropriateness and viability of the original policy prescriptions – or of possible alternatives.

Naturally, the assumption is that the weaker the state apparatus, the greater the scope for beneficial reforms. Such reforms are deemed part-and-parcel of the programmes' future success; they are never seen as a possible insurmountable impediment to achieving the latter's overall objectives. Some economists have even seen the economy's relative backwardness as an element to be exploited; using the vast room for improvement available as a potential lever to deliver high growth and prosperity.[49]

However, other economists view the very slow progress of the Greek economy as indicative of conceptual flaws in the adjustment programme, combined with the wrong currency environment. In so doing, they perilously overlook the fact that the country would require a strong administration, capable of carrying out strict macroeconomic policies and sweeping structural changes, under *any* type of adjustment programme.

Probably the Greek programme's most insistent critic among economists of international repute, Paul Krugman sees Greece's deep economic recession as a result of excessive "austerity" imposed by the lenders, exacerbated by membership of the euro.[50] Perhaps taking their cue from Keynes – who raised no objection to how free markets basically operated, so long as there *was* full employment[51] – most modern-day Keynesians remain unconcerned with the details of the underlying economy, positing that the latter's performance depends essentially on the right macroeconomic-policy mix. Nowhere in Krugman's critique is there any role for the fundamental structural characteristics of the Greek economy, or the ability of government and public administration to deliver on structural and administrative reforms. Indeed, he assumes that the Greek economy's "competitiveness" problems can be meaningfully addressed by jettisoning the euro and devaluing, despite the fact that the latter's problems are the exact opposite of being temporary, reversible in nature and/or of external provenance, the circumstances in which devaluations *might* work (in conjunction with a set of other, important conditions). This leap to the wrong policy conclusion leaves no room for such crucial considerations as the need for Greek entrepreneurs to have access to affordable foreign inputs (if they are ever to successfully upgrade the Greek economy through a big expansion of the currently seriously underdeveloped export sector) or inexpensive finance. Nor does it allow for such typical traits of the Greek economy as its observed low responsiveness to incentives to increase exports (in the event, *via* internal devaluation), as evidenced by the country's still poor export performance in the face of the biggest reduction in nominal wages of all troubled Eurozone countries, a result attributable to a noxious combination of oligopolistic, or otherwise inefficient, market structures and administrative obstacles. Instead, this analysis effectively moves at a level of abstraction that ends up obscuring the role of the real culprits: institutional inefficiencies,

49 Costas Meghir, Dimitri Vayanos, Nikos Vettas, *The economic crisis in Greece: A time of reform and opportunity*, 5 August 2010, www.greekeconomistsforreform.com, (Accessed on 25 September 2017).

50 Providing an excellent idea of Krugman's hostility to the whole euro project is Krugman (2015). Paul Krugman, "Europe's Impossible Dream", *The New York Times*, July 20, 2015, p.A19, https://www.nytimes.com/2015/07/20/opinion/paul-krugman-europes-impossible-dream.html?mabReward=CTM (Accessed on 1 October 2017).

51 John Maynard Keynes, *The General Theory of Employment, Interest and Money,* Macmillan 1936, p.378–379.

human failures, political fiascos and deep-seated market distortions[52] and rigidities[53] most of which can be traced, in essence, to various policy failures, past and present.

Jeffrey Sachs' position is much more nuanced – and ambiguous: on the one hand, he has placed the austerity *vs.* stimulus debate in the right perspective by, *inter alia*, highlighting the need for real structural reforms to impel export-led growth; on the other hand, in June 2015 he did advocate a default by the Greek government on the (mistaken) belief that European creditors refused any discussion about debt relief.[54] The consequent cessation of all financial (and perhaps technical) assistance would have created economic, financial and social mayhem, bearing also in mind that the government in power at the time (radical-Left/nationalist-Right coalition Syriza/Anel) had managed to turn a primary budget surplus of 0.6% of GDP in 2014 into a huge new primary deficit of 4.1% in 2015. (In fact, repeated Eurozone leaders' common announcements did speak of debt relief, but later – see below).

At the other end, economists such as Harvard's Ricardo Hausmann reject the notion that Greece typifies the failure of austerity policies (and insufficient debt forgiveness).[55] Instead, Hausmann draws attention to the weaknesses and defects of the real economy, and claims that, overall, "Greece never had the productive structure to be as rich as it was: its income was inflated by massive amounts of borrowed money that was not used to upgrade its productive capacity."[56] He points to the huge size of the pre-crisis current-account deficit and how it was expressive of the underlying weaknesses of the economy, reminding that the current shrinking of the current-account deficit has come about entirely thanks to the decrease in imports rather than an increase in exports (in contrast to what happened in other peripheral European countries[57]). In fact, Hausmann argues, the policy of massive financial support may have actually delayed, rather than hastened, the needed adjustment in Greece.[58] Hence the critical importance of improving competitiveness *via real* adjustment[59], an objective which,

52 Many of these should not be considered innate characteristics of the Greek private sector but, rather, a rational response to the type of economy fashioned by government-led excessive borrowing: an economy with a collapsing savings rate and booming imports, creating a bias against investment in sectors other than low-risk, low-tech ones such as the retail trade and residential construction. Admittedly, there may be inherent cultural factors at play as well, though in practice it is very difficult to disentangle the culturally-innate traits from the environmentally-conditioned.

53 In this type of consumption-led and import-biased economy, it is no surprise that 99.9% of Greek enterprises fall under the "small- and medium-sized" category. In 2015, they employed 87.3% of all employees (*vs*. 66.8% in the EU28). Small size prevents domestic firms from exploiting economies of scale and thus more easily penetrating foreign markets. See, European Commission, *SME (Small- and Medium-sized Enterprise) Performance Review*, 24 November 2016, http://ec.europa.eu/growth/smes/business-friendly-environment/performance-review-2016_en (Accessed on 20 October 2017).

54 See interview with Bloomberg on 29 June 2015, https://www.bloomberg.com/news/videos/2015-06-29/greece-should-default-on-debt-stay-in-euro-sachs. In February-March 2012, Eurozone leaders organised the world's largest ever "voluntary" debt write-down *via* a debt swap that reduced privately-held sovereign debt worth €206 bn to €125 bn (after adjusting for the negative impact on Greek banks' balance sheets). See George Papaconstantinou, *Game Over – the Truth about the Crisis,* Kyriakos Papadopoulos S.A., 2016 (Greek edition), Chapter 21 and p.331.

55 Ricardo Hausmann, "Austerity Is Not Greece's Problem", *Project Syndicate*, 3 March 2015, https://www.project-syndicate.org/commentary/greece-export-problem-by-ricardo-hausmann-2015-03 (Accessed on 20 September 2017).

56 Ibid. According to the Atlas of Economic Complexity (2011), which he co-authored, in 2008 the gap between Greece's income and the knowledge-content of its exports was the largest among a sample of 128 countries.

57 See, *e.g.*, Efstathiou andWolff, "How export growth achieved adjustment of massive trade deficits in the euro area", 2017.

58 In a similar vein, Miranda Xafa argues that the huge loans obtained by Greece have helped Greek governments preserve for longer than necessary the 'clientelistic state'. Miranda Xafa, "Public Debt", *Brief Introductions series* No.7, Kyriakos Papadopoulos Publications, Athens, 2017, p.99.

59 Ricardo Hausmann, blogpost, 8 February 2015, https://www.facebook.com/ProfessorRicardoHausmann/posts/342454585949338, (Accessed on 20 September 2017).

according to Hausmann, is altogether underplayed by economists of a more Keynesian bent, such as Joseph Stiglitz.[60]

Unfortunately, Hausmann's more pragmatic approach was ignored in Greek public debate, thus leaving the field open for the much more crowd-pleasing entreaties of Krugman and Stiglitz. Not missing its chance, the Greek government used the question of the debt to divert attention away from the paramount importance of reforms in the here-and-now [61] – ironically, at a time when Greece's annual interest payments were on a markedly downward path, and anyway lower than Portugal's or Italy's.[62] Not, of course, that a reduction in the net present value of debt servicing costs would have meant any more resources becoming available to Greece in the short term.

That said, the lenders will undoubtedly have to countenance some kind of re-profiling of the outstanding debt at some point (a pledge made originally in November 2012 and, even more explicitly, in May 2016[63], but – reflecting the lenders' appallingly low levels of trust in the debtor nation's political élites – not before completion of the relevant programmes, which explains why it has not been fulfilled yet: the 2nd Memorandum was discontinued; the third is not due to expire until August 2018).

The Exorbitant Costs of the Leisurely Pace

Arguably, the feature that best illustrates the low-adjustment capacity (and/or low willingness-to-change) of government (politicians and public administration alike) is the growing delays recorded in the implementation of reforms relative to the timetables contained in the memoranda. The pace of implementation can be usefully read as a proxy for 'adjustment capacity/readiness', the record showing that this indicator, instead of improving with experience, deteriorated sharply over time, further intensifying the sense of uncertainty pervading, among others, the business community.

The success of the adjustment programmes requires a stable political environment, a dogged determination to achieve targets and meet deadlines, a heightened sense of duty and urgency, and a willingness to discard old, petty party-political practices. Instead of political stability, Greece (2010-2017) saw four general elections, ten different governments under four different prime ministers, countless changes in key ministerial posts (including seven finance ministers), one referendum and one aborted referendum.[64] Instead of national unity in pursuit of a higher goal, one observed

60 Joseph Stiglitz, "A Greek Morality Tale", *Project Syndicate*, 3 February 2017, https://www.project-syndicate.org/commentary/greece-eurozone-austerity-reform-by-joseph-e--stiglitz-2015-02 (Accessed on 20 October 2017).

61 For a clear depiction of Greece's debt repayment schedule, see *The Wall Street Journal*, https://graphics.wsj.com/greece-debt-timeline/.

62 The Greek government's interest payments peaked at 7.3% of GDP in 2011, falling gradually to 3.2% in 2016. In that same year, Portugal paid 4.2% of GDP and Italy 4%; See, AMECO, general government expenditures (interest).

63 In May 2016, the Eurogroup promised a series of debt-alleviation measures, including "smoothening the repayment profile" (but excluding "nominal haircuts"). Council of the European Union, "Eurogroup statement on Greece", 9 May 2016, http://www.consilium.europa.eu/en/press/press-releases/2016/05/09-eg-statement-greece/ (Accessed on 10 October 2017). Already in February 2012, repeated in November 2012, the Eurogroup committed to "providing adequate support to Greece during the life of the programme and beyond [...] provided that Greece fully complies with the requirements and objectives of the adjustment programme". The latter statement implies that, for a full discussion on debt restructuring, Greece would have to complete the programme first. Unfortunately, the latter was never fully completed and was superseded by the Third Memorandum. Council of the European Union, "Eurogroup statement on Greece", 21 February 2012, http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ecofin/128075.pdf (Accessed on 10 October 2017); Council of the European Union, "Eurogroup statement on Greece", 27 November 2012, http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ecofin/133857.pdf (Accessed on 10 October 2017).

64 Georgiades, *Kathimerini*, 2017.

the confrontational politics of old carry on unabated.[65] Probably the epitome of this type of counterproductive tactics was the main opposition party's (New Democracy) vote against ratification of the first Memorandum in Parliament (May 6, 2010) – only to reverse course once in power.

Each of the three memorandums experienced increasing delays in implementation.[66] Indeed, the first two were never officially completed. Periodical reviews by the Troika were supposed to take place on a quarterly basis. The first memorandum (May 2010-June 2013), under Pasok, saw the carrying out of five reviews through autumn 2011, but was never concluded: despite a relatively strong start, the programme was wrecked by the crisis then engulfing the whole Eurozone periphery. The second memorandum came into effect in March 2012 (2012–end-2014, later extended to end-June 2015). Only four of the five scheduled reviews took place, and the intervals between them twice reached nine months. This loan arrangement, too, was never completed because ND, then in power, sensing electoral defeat, toward the end lost interest. It was replaced by a third, harsher, memorandum (Aug 2015-Aug 2018) agreed to under dramatic circumstances, following the extreme uncertainty-provoking referendum of July 5, 2015, by a government (Syriza/Anel) that, earlier, had been falsely promising voters a huge debt write-off that would obviate the need for further austerity policies.[67] Review delays now broke every precedent (second review: *fourteen* months). Delays were a product of a lack of determination (often typified by an inability/unwillingness to translate adopted laws into actual implementing measures, a feature not unique to Syriza/Anel) to outright political repudiation of the entire exercise.[68] Ironically, the net effect of the government's tergiversations and bogus "negotiations" with the Troika (purportedly designed to "protect" citizens from the full brunt of the offensive reforms) was to shatter consumers' and investors' confidence in the future, extinguish the embryonic 2014 recovery, bring back the primary budget deficits (2015), cause exports to contract (2015-16)[69], prolong the recession and concomitant misery, and necessitate further assistance from the Eurozone (2015) – just when the rest of Europe was beginning to recover.

Conclusion

The basic premise of this essay has been that political, institutional and administrative weaknesses have been the main cause of Greece's inability to recover more quickly from its sovereign-debt crisis and profit more from the ensuing adjustment programme and associated opportunities.[70]

65 This antagonism often reached down to the level of personal relationships within ruling factions. See, George Papaconstantinou, *Game Over – the Truth about the Crisis,* Kyriakos Papadopoulos S.A., 2016 (Greek edition), p.264-5, 319.

66 An authoritative source is the Commission's dedicated website, "Financial Assistance to Greece".

67 The individual best personifying this kind of one-dimensional economic-policy crusade was, of course, Greece's finance minister in early 2015, Yanis Varoufakis, who is on record for not having made a single sensible proposal about how to modernise the public sector or improve the business environment, but who *did* use extremely aggressive tactics with the lenders to force them (unsuccessfully) to grant debt relief.

68 Syriza/Anel cadres repeatedly disowned the reforms prescribed by the memoranda, calling them essentially a 'necessary evil'.

69 *Inter alia*, due to the imposition of capital controls at end-June 2015.

70 The government committed, under the terms of the 3rd Memorandum, to "develop a genuine growth strategy which is Greek-owned and Greek-led [… and …] to finalize [it] by March 2016 in collaboration with social partners, academics and international organisations". Such a plan has never been delivered. See, *Memorandum of Understanding between the European Commission acting on behalf of the European Stability Mechanism and the Hellenic Republic and the Bank of Greece,* 19 August 2015, https://ec.europa.eu/info/sites/info/files/01_mou_20150811_en1.pdf (Accessed on October 2017).

These explanatory factors – many of which have deep historical and cultural roots[71] – have been underestimated or discounted by economists and policy-makers, for three main reasons: (i) the difficulties involved in accurately assessing, *ex ante*, their potential impact on the effectiveness of the policies prescribed; this, then, (ii) reinforces a professional bias among economists that tends to view issues that are "economic" as best analysed, and tackled, basically by economic tools[72]; policy-makers readily endorse this view because of the need to reduce the size of the problem and render any remedial action more manageable; and (iii) both economic-policy mistakes and non-cost competitiveness factors linked to institutional causes have outwardly similar economic consequences, heightening the risk of a mis-diagnosis.

In the case of Greece, there is overwhelming circumstantial evidence that weaknesses in the above three fields have impeded a more rapid and effective implementation of the needed reforms. Admittedly, this evidence only now is being more systematically catalogued and evaluated (though it did provide a sufficiently compelling *prima facie* case to convince the European Commission, already in July 2011, to set up a special Task Force to provide technical assistance to the country's public administration). As a result, there is still serious – but, in important ways, misguided – debate in policy and academic circles about such 'theoretical' issues as the appropriateness of 'austerity' at a time of deep adjustment, and why the lending institutions were often so inaccurate in their growth predictions. Invariably, this was put down to substantive policy errors and not, primarily, to implementation, or other, more deep-seated, weaknesses. Thus, a variable that over time became endogenous to the system (*viz*., the *additional*, and self-reinforcing, contractionary effects directly attributable to mismanagement, delays and very weak programme 'ownership') kept being conflated with the natural tendency to economic deceleration implicit in any fiscal consolidation programme, and, therefore, misconstrued as an externally-imposed, exogenous parameter. Similarly, those who insist on strict and unwavering adherence to the programme's guidelines as the only way out of the current immobility underestimate the system's resistance – for calculated or unintentional reasons – to change.

The essential reason why there must be a shift of focus in any evaluation of the Greek programme from the economic-policy parameters to the institutional, political and cultural characteristics of the country is the need to become cognizant of the system's true flaws. To this day, the majority of Greeks do not know how the crisis came about.[73] Without public recognition of these flaws, and a vast national effort to remedy them, not only will the country's future economic potential remain unfulfilled; there will be a high risk of relapse some time in the not too distant future.

71 A germane thesis is the one compellingly expounded by Acemoglu and Robinson. See, Daron Acemoglu and James A. Robinson, *Why Nations Fail*, Profile Books Ltd, London, 2012; Kazakos, Liargovas and Repousis use the former authors' concepts of 'extractive and inclusive economic institutions' to argue that the three Memoranda reflect the idea of a need to transition from an extractive to an inclusive system. See, Panos Kazakos, Panayiotis Liargovas, Spyros Repousis, *Greece's Public Debt*, Parliamentary Office of the State Budget, Papazissis Publications, 2016 (in Greek), p.304-306.

72 Hence the inconclusive debate about the validity of the IMF's 'fiscal multipliers'. In fairness, it must be mentioned that Greece's IMF/EU-designed adjustment programmes often went much deeper, *e.g*., prescribing concrete measures for the depoliticisation of the administration.

73 A conclusion derived indirectly from opinion poll data showing former prime ministers' popularity ratings. See, KAPA Research, *Panhellenic Survey*, September 2017, http://www.iefimerida.gr/sites/default/files/kr.pdf (Accessed on 1 November 2017).