Can **Greece** Meet the Challenge?

By Eirini Karamouzi & Vassilis Paipais

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In an interview with a Finnish magazine, Oli Rehn, the European Commissioner for Economic Affairs, said that the 'bankruptcy of Greece would potentially have for the global economic system, effects similar to those of the Lehman Brothers, if not worse'. How did Greece get to possess such a notorious privilege among the Eurozone countries?

Pundits and policy-makers alike agree that as much as the Greek government would like to cast the blame solely on international speculators or German intransigence and lack of European vision, the country's public debt crisis bears the mark of some uniquely Greek peculiarities. Notwithstanding the international dimension of the Greek crisis, Greece is to a large extent suffering the effects of an infantile political system and a diseased social and economic model.

To capture the dynamics of the situation, one has to revisit its founding moment. For Greece, the year 1974 was hailed as the dawn of a new era that brought the end of military interventionism in politics and the opening up of the political system to marginalised social and political groups. What began, however, as a long-awaited process of democratisation degenerated pretty quickly into an unprecedented orgy of populism sustained by European funds. Mainly since the early 1980s, successive Greek governments have run large deficits to finance public sector jobs, pensions, and other social benefits. The public sector grew exponentially to the intimidating number of 1.1 million out of a workforce of five million, treated as a privileged outlet for rewarding party clients. Clientelism gradually eroded all public institutions, from tax offices and health services to universities and the judiciary. For a short period, the Greek economy managed to sustain a high rate of growth due to the favourable conditions created by the introduction of the EURO, the influx of European funds and an extensive program of public and private investment. However, the impressive growth of national income was primarily generated by public spending and largely depended on domestic consumption, which accounted for over 70% of Greek GDP. Far from being in any sense coincidental, this state-funded model of economic development reflected the deep deficiencies of the Greek economy and political system.

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On the evening of October 4, 2009, the socialist party PASOK (Pan-Hellenic Socialist Movement) won an overwhelming majority 43.92% of the popular vote and 160 of 300 parliament seats on the promise that harsh austerity measures could be avoided. The new socialist government succeeded an utterly discredited conservative one which was rightly deemed principally responsible for the country's unprecedented fiscal derailment. It was not long after that the new government revealed the country's deficit to be around 12.7% of GDP (now 13.6%), more than twice the previously announced figure. Greece's widening deficit, coupled with reasonable suspicion about the accuracy of the country's statistics spread fears throughout the markets and undermined the credibility of EU budget rules. However, instead of following Ireland's example, Prime Minister George Papandreou's initial reaction failed to assess the severity of the situation. Clinging on unrealistic development strategies and ideological fixations he ceded valuable time, a commodity markets proved very reluctant to grant.

Greece's soaring financing costs eventually pushed the EU to bend its rigid 'no bail out' clause and join the International Monetary Fund to offer a three year €110 billion rescue package. The agreement includes belt-tightening measures such as severe cuts in salaries and public pensions and further increases in indirect taxes in the hope of reducing the deficit below 3% of GDP by 2014. Apart from fiscal consolidation, the loan terms call for a number of important structural reforms: a comprehensive pension reform, labour market liberalisation, opening-up of closed professions and reducing bureaucratic barriers to foreign investment. Greece seems to have bought valuable time to implement the structural changes necessary to put the economy back on track.

Given the urgency of the situation, one would expect the political parties to seize the opportunity to redress the fiscal chaos and improve the economy's low competitiveness. The response so far, however, is rather disappointing, vindicating those who think that the country's main problem is political. With the exception of the ruling party and the extreme-right, the opposition parties voted against the bill, opting for short-term party benefits over the attainment of a national consensus. Furthermore, just two weeks after the signing of the Memorandum of Understanding with the IMF, some ministers raised the issue of a more 'flexible' implementation of the agreement (e.g. in pension reform), while others have jeopardised the credibility of market liberalisation by proposing mock reforms.

As things stand, few people believe that the fiscal measures attached to the joint EU-IMF plan are enough to increase production, spur growth and rescue Greece from bankruptcy. Both economic experts and public opinion doubt the capacity of government initiatives to effectively combat corruption and implement the right mix of fiscal and development policies. Moreover, the pain from the austerity measures has just began to be felt. Angered by their politicians, especially the two main parties - PASOK and New Democracy - which have alternated in power over the past 36 years, taking turns in blaming each other for the country's woes, Greeks are fighting back. The violence that erupted on May 5th during a widespread national strike, resulting in the death of three innocent people, was a reminder that democratic governments can impose only so much hardship before people rise up.

The Greek Prime Minister has regularly repeated that Greece is at war but he has not yet moved to redress the dysfunctionalities of a faltering cabinet or reshuffle the government. With his personal credibility at stake, much depends on how he will cope with the pressing demands for addressing widespread tax evasion, the country's delinquent political system, inefficient state bureaucracy and unproductive economic model. For Greece to escape its predicament, it is not enough to reduce salaries and pensions, slash public spending and reform the social security system and labour market. Rather than lament conditions it is unable to wish away, the incumbent government should redirect its energies towards attracting foreign investment, reducing red tape and boosting exports. The Greek economy still holds many underexploited prospects in sectors such as the shipping and tourism industry, quality food production, culture and green energy. Managed wisely, these sectors could form the foundation of truly sustainable development. What is most urgently needed is a New Deal between the public and private sector that would restore trust in public institutions and unlock the productive forces of the economy.

Mr Papandreou is well known for his admiration of President Obama's political style and rhetoric. He might wish then to join one of Obama's favourite public intellectuals of the past century, Reinhold Niebuhr, in his public prayer: 'God, grant me the serenity to accept the things I cannot change, the courage to change the things I can, and the wisdom to know the difference.' ■

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