

## Greece and the Euro Crisis: From the Brink of Collapse to the Inevitable Reform

As the global financial crisis transformed into a European sovereign debt crisis in late 2009, Greece has ever since occupied a central position in all discussions about the present and future of the Eurozone. Following the disclosure about Greece's false statistics and the readjustment of the country's current account deficit from 6 to 15.6 percent, Greece has been dragged into the heart of an economic and political maelstrom that has questioned at times the very viability of the European project. The dramatic disclosure of the country's dismal economic situation led to the eventual downgrade of Greek bonds to junk status and the country's exit from the financial markets. Meanwhile, the crisis had a spillover effect and dashed market confidence in the public finances of other Eurozone member states, which were collectively called with the rather unflattering acronym PIIGS.<sup>1</sup> It is no surprise that leaders of other Eurozone members that also got into deep economic distress attempted to convince the international community that their "situation is not like Greece's" or else that they "would not become Greece." In April 2010, the Greek government appealed to the International Monetary Fund (IMF) and the European Union for a rescue package. In May 2010 a bailout agreement was signed between the Greek government, the IMF, the European

Central Bank (ECB) and the European Commission (EC), which came to be known as the "troika." Greece would take a loan of 110 billion Euros over a period of three years in return for committing to deep fiscal cuts and comprehensive economic reform. Nevertheless, the failure to meet the economic targets with respect to the current account deficit and public debt led to the need for a new agreement. In October 2011 European leaders reached a deal on a second 130 billion Euro bailout package for Greece which entailed in return for more fiscal austerity and reform measures which also included a 50 percent cut in the face value of Greek bonds held by private investors. When Prime Minister George Papandreou had the fateful idea of calling for a referendum on the latest bailout agreement, this led to a furious reaction by senior Eurozone members, his resignation and the appointment of a caretaker coalition government under the ECB board member Loukas Papademos. Papademos was able to seal an agreement with the troika in March 2012. Double parliamentary elections in May and June 2012 raised the fear of a disorderly default and exit from the Eurozone (Grexit). Yet these fears abated when the June 2012 parliamentary elections produced a coalition government that declared its intention to implement the terms of the agreement. As the immediate risk of a Grexit abated, the roots of the crisis remained anything but addressed.

<sup>1</sup> PIIGS stood for Portugal, Ireland, Italy, Greece and Spain.

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It would be wrong to reduce the Greek crisis to its economic dimensions. What the economic crisis exposed was not just the fiscal profligacy of consecutive Greek governments but the failure of a socio-political model that had shaped Greece since the early 1980s. A public debt-driven model of economic development was reinforced by the influx of billions in European money transfers, structural aid and subsidies. The emergence of a bloated and inefficient public sector crowded out crucial resources needed by the private sector. This turned the relationship between the public and private sector into a breeding ground for corruption, nepotism and clientelism. The gradual loss of competitiveness of the Greek economy meant that a growing number of factories had to shut down or be relocated abroad. A series of favorable developments such as the disbursement of copious EU funds, the end of the Cold War and new business opportunities in Eastern and Southeastern Europe, the arrival of about one million immigrants and Greece's entry into the Eurozone delayed but could not prevent the outbreak of the crisis. Greece's entry into the Eurozone implied a commitment that old practices had to be forgotten, government performance had to be improved and economic competitiveness had to be protected by means other than devaluation. This commitment was never observed. The viability of this socioeconomic model reached its limits in late 2009, but not before having decimated Greece's productive infrastructure.

Coming to terms with the fact that Greece had lived for long beyond its means was difficult. Fiscal austerity measures including new taxes and sharp cuts in public sector salaries and pensions were not only obligations of the Greek government emanating from the bailout agreements. They were indispensable moves to avoid a disorderly default and an exit of Greece from the Eurozone. Yet under these extraordinary circum-

stances, populism and extremism soon increased their appeal. Their recipe was easy. Instead of looking for solutions, culprits for the ills of the country were sought abroad. Accusing European institutions for the economic and social failure of Greece, insisting that the extent of the crisis was exaggerated or that a painless path towards recovery existed but was deliberately not taken by the country's government. A culture of anonymity that became one of the most intrinsic features of Greek society ever since the 1980s contributed to the outbreak of periodic riots that cost and gave the impression that Greece was becoming ungovernable. As the country's economy was caught into a vicious circle of recession and growing unemployment, social cohesion was collapsing and political stability was put into question. At the same time the crisis rekindled an identity debate that most thought settled since the 1980s. "We belong to the West" was the slogan with which Konstantinos Karamanlis rallied support for his EEC membership application in the 1970s. The famous response of the PASOK leader Andreas Papandreou "Greece belongs to the Greeks" –as if the two are mutually exclusive– became a banner of the opponents of Greece's EEC membership. While Andreas Papandreou himself became an advocate of Greece's EEC membership when he rose to power in 1981, a sharp increase of anti-Western and anti-European sentiment in the context of the crisis and the emergence of parties advocating Greece's exit from the European Union indicated how populism could still complicate Greece's relationship with the European Union and the West.

The political ramifications of this crisis were inevitable. The Panhellenic Socialist Movement (*Panellinio Sosialistiko Kinima*-PASOK), the party that had dominated Greek politics since the 1980s and came to power just before the crisis winning 43.92 percent of the vote and a comfortable majority in the October 2009 elections col-

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lapsed to 13.18 percent in the May 2012 elections and 12.28 percent in the June 2012 snap elections. New Democracy (*Nea Dimokratia*-ND), the party which brought Greece to the European Economic Community in 1981 but whose rule in the 2004-2009 years was linked with the most profligate administration of public finances fell from 33.47 percent to 18.85 percent before rising to 29.66 percent in the June 2012 elections. As the cornerstones of the Greek political system were rocking, who were the beneficiaries from this crisis?

The crisis did not lead to a reconfiguration of Greece's reformist forces that were unevenly distributed among Greece's established political parties, but to a rise of political extremism. Passing the blame for Greece's ills to European institutions and major EU member states has been a key theme among Greek populists. . In their view, the crisis was a ploy set by Greece's enemies in order to crush Greek sovereignty and independence with the willing support of some Greek "collaborators." No austerity and reform measures were necessary, as Greece had only to tap on its unexploited resources in order to achieve economic recovery and even prosperity. Speculation about the existence of immense oil and natural gas fields in the Eastern Mediterranean off the Greek shores were hyped by Greece's nationalist and populist press. Pressure mounted on the government for the unilateral declaration of Greece's exclusive economic zone (EEZ) in the Eastern Mediterranean notwithstanding possible reactions by other littoral states in the region, most importantly Turkey. In addition, as anti-German sentiment was on the rise, parties raised the issue of demanding from Germany to pay reparations for the occupation in Greece during the Second World War or the repayment of a loan which the government of occupied Greece had made to Nazi Germany.

On the left of the spectrum, the Coalition of Radical Left (SYRIZA), an alliance of radical left parties, saw its fortunes to rise from 4.6 percent in the 2009 elections to 16.78 percent and 26.89 percent in 2012. SYRIZA's popularity rose steeply, as it objected to all painful fiscal austerity and structural reform measures and promised to denounce the bailout agreements and restore the *status quo ante*. How it could finance Greece's current account deficit and service its debt never became clear. In their view, Greece was a victim of rapacious international capitalism and was not responsible for its own sufferings. The threat for a Greek disorderly default was seen as a key bargaining tool, while exit from the Eurozone was not seen as taboo. Some SYRIZA members even saw the Eurozone crisis as the harbinger for a terminal crisis of global capitalism and a socialist transformation in which Greece would play a vanguard role. Athens' Syntagma Square, focal point of demonstrations against austerity and reform measures, was hoped to play an equivalent role with the role of Cairo's Tahrir Square in the "Arab Spring."

On the right, two new parties aimed to represent rising discontent against the fiscal and structural adjustment program. The first party, the "Independent Greeks" (*Anexartiti Ellines*) was founded by New Democracy delegates who objected to the moderate shift that their party took following its participation in the Papademos government in November 2011. It advocated a populist, nationalist anti-Western agenda and got 10.61 percent of the vote in the May 2012 and 7.51 percent in the June 2012 elections. The second party, the "Golden Dawn" (*Chryssi Avgi*) was not a newcomer in Greek politics. One of Europe's numbered unequivocally pro-Nazi political parties, the "Golden Dawn" moved from the far margins to the main stage of Greek politics. Increasing its vote twenty-four times between the October 2009 and the April

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2012 elections and garnering 6.97 percent in the May 2012 and 6.92 percent in the June 2012 elections, the "Golden Dawn" was linked not only with opposition to reform and austerity measures, but also with a wholesale rejection of the democratic regime and its values. Departing from an anti-Western and anti-Semitic agenda, the "Golden Dawn" blamed the international community as responsible for Greece's crisis and scapegoated immigrants as responsible for rising unemployment, as well as existential threats for the Greek nation. The party developed its strongholds in some of Athens' run-down neighborhoods where resident immigrants were accused by popular media of increasing crime rates. An increase of violent attacks against immigrants by party thugs was met with indifference if not tacit support by a small but growing part of Greek public opinion. Cynicism and wholesale rejection of the current political party system facilitated the increase of the political appeal of a party whose legality according to the Greek Constitution became a highly debated issue among experts. The changing fortunes of the "Golden Dawn" were ample evidence that public finances were not the only and even not the most alarming aspect of the Greek crisis.

Pessimism reached a peak on the eve of June 2012 elections, as the prospect of a hung parliament or a SYRIZA-led government that would denounce the bailout agreements raised fears about an economic collapse and Greece's eventual exit from the Eurozone and even the European Union. Nonetheless, New Democracy, which until the end of 2011 had vehemently objected to fiscal austerity and reform measures, won the plurality of votes on a pro-bailout agreement agenda and formed a coalition government under its leader Antonis Samaras with the support of PASOK and DIMAR (*Dimokratiki Aristera*-DIMAR) that also lent their support for the bailout agreements. Meanwhile, in Brussels and Eurozone capi-

tals, there was mounting consensus that keeping Greece within the Eurozone would be the optimal solution for all parties. The uncertainty that Greece's exit from the Eurozone would bring about, the fear of contagion in European economy similar to that of the default of Lehman Brothers in September 2008, and the threat that such a development could comprise for the stability of the Eurozone sidelined views arguing in favor of insulating Greece from the rest of the European economy and letting it default and exit the Eurozone.

Almost a year after its rise to power, the record of the Samaras government is rather mixed. On the one hand, painful and deeply unpopular fiscal austerity measures were passed through the parliament, and this led to significant improvement of public finances. The current account deficit reached 2.1 percent of the GDP in the first ten months of 2012, and a current account surplus in the near future appears to be a target within reach. On the other hand, structural reform which would eliminate inefficient public spending and support the country's real production base was still looming. Despite verbal support for privatization, no major project was implemented between June 2012 and January 2013. Any measures intended to rationalize public spending and to contract the country's inefficient and bloated public sector were met with determined opposition by public sector employee unions. While it turned out, for example, that Greece had one of the highest teacher-per-student ratios and yet one of the worst education systems in the developed world, no discussion was made on how to introduce evaluation methods, better reward the efficient public sector employees and get rid of the inefficient ones. Instead, the discussion was focused on how to provide maximum job security to all and ignored the question of how to improve performance. Privileges of semi-public organization employees accumulated during the "good old

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days" through clientelistic relations with governments were not abolished. Despite repeated assurances to the troika, lifting all barriers to entry into a number of "closed professions" proved impossible. Government parties were apparently aware that the abolition of the complex network of clientelistic relations in the public sector, which would be an inevitable result of structural reform and privatization, would likely bring about their own demise at the polls. Hence they appeared unwilling to lend full support for structural reform, even though this meant that the distribution of the cost of the adjustment process would be unfair against the private sector. While the Greek government pledged not to fire a single redundant public sector employee and avoided rationalizing public expenses, hundreds of thousands of private sector employees were losing their jobs as a result of the recession. Despite lofty statements about the elimination of tax evasion, one of the key chronic diseases of Greek public finances, very little was achieved, due to both lack of political resolve as well as the dismal state of Greek tax authorities. Meanwhile the key question of recapitalizing the Greek banking sector, once one of the locomotives of the Greek economy, that suffered a heavy blow due to the haircut imposed on Greek bonds, was not dealt as a key step towards restarting the Greek economy, but in terms of protecting clients. The demolition of the clientelistic state is unlikely to be achieved by the very actors who contributed to its consolidation. This was a painful reminder of the complex nature of the Greek crisis, as well as of existing barriers to recovery.

The threat of a "Grexit" may not be looming as it did in June 2012, yet addressing structural deficiencies of the Greek state and economy is imperative in order to consolidate Greece's position in the Eurozone and facilitate the recovery of its economy. The course of Greek recovery will also be af-

ected by domestic developments in key Eurozone states. The extent to which European solidarity can remain strong and justify the continuation of the bailout plan and the possible introduction of an equivalent of a "Marshall Plan" will be instrumental for the expedition of Greek recovery. On the domestic front, whether corrupt structures that were among the triggering factors of the crisis will be allowed to survive in the new era or not will be of critical importance. These include the old political party system. The transformation of New Democracy from a virulent anti-reform opposition party between 2009 and 2011 to a pro-reform senior coalition government partner ever since may have contributed to the prevention of a "Grexit" but has still harmed the credibility of the Greek political party system. Similarly, the early 2013 attempt of SYRIZA's leader Alexis Tsipras to soften his rhetoric and build a more moderate profile through visits to Berlin and Washington DC, while possibly questioning the cohesion of the party, was likely to reinforce mistrust towards political parties and support for anti-systemic parties, such as the "Golden Dawn". A paradigmatic shift is necessary in order to shift the focus of attention from the clients of the pre-2009 order to the social and economic forces that can become the locomotives of Greek recovery. This shift will also rehabilitate social values that were left into oblivion or tarnished, such as fair competition, honesty, entrepreneurship and citizenship. As current political parties have proven unable to address these new challenges, it is likely that their administration would promote some *ad hoc* reform measures, which would prevent a disorderly default but would fail to address the underlying causes of the crisis. A formidable and ambitious reform agenda can only be promoted by new political parties without the heavy burdens and habits of the recent profligate past. These parties could host existing reformist groups that have been kept outside politics or exist in disparate form

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within the existing political party system. Restoring trust in political parties will be a formidable task given the lower than ever incidence of social capital in the country. As adjustment costs are unevenly distributed among different segments of the Greek, questions related to the absorption capacity of the economic and social shock will be central. The vicious circle of growing cynicism and mistrust against politics in a substantial segment of Greek public opinion needs to be carefully addressed, as well as domination of a populist and nationalist discourse. The introduction of a new political discourse which escapes from the pitfalls of exceptionalism and victimization and does not avoid addressing uncomfortable truths about the roots of the crisis is of paramount importance. This discourse will also raise the question of fair distribution of adjustment costs, highlight the unfulfilled potential of the country and focus on endorsing its productive forces. Building-up trust is essential not only for accelerating Greece's recovery but also for the restoration of its links with the European community and the elimination of "Golden Dawn"-like challenges to its democratic political regime.

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