THE PROBLEM WITH GREECE: ECONOMIC AND SOCIO-POLITICAL CHALLENGES

Kenneth Matziorinis
McGill University & John Abbott College

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EPOK
Hellenic Progressive Association of Quebec

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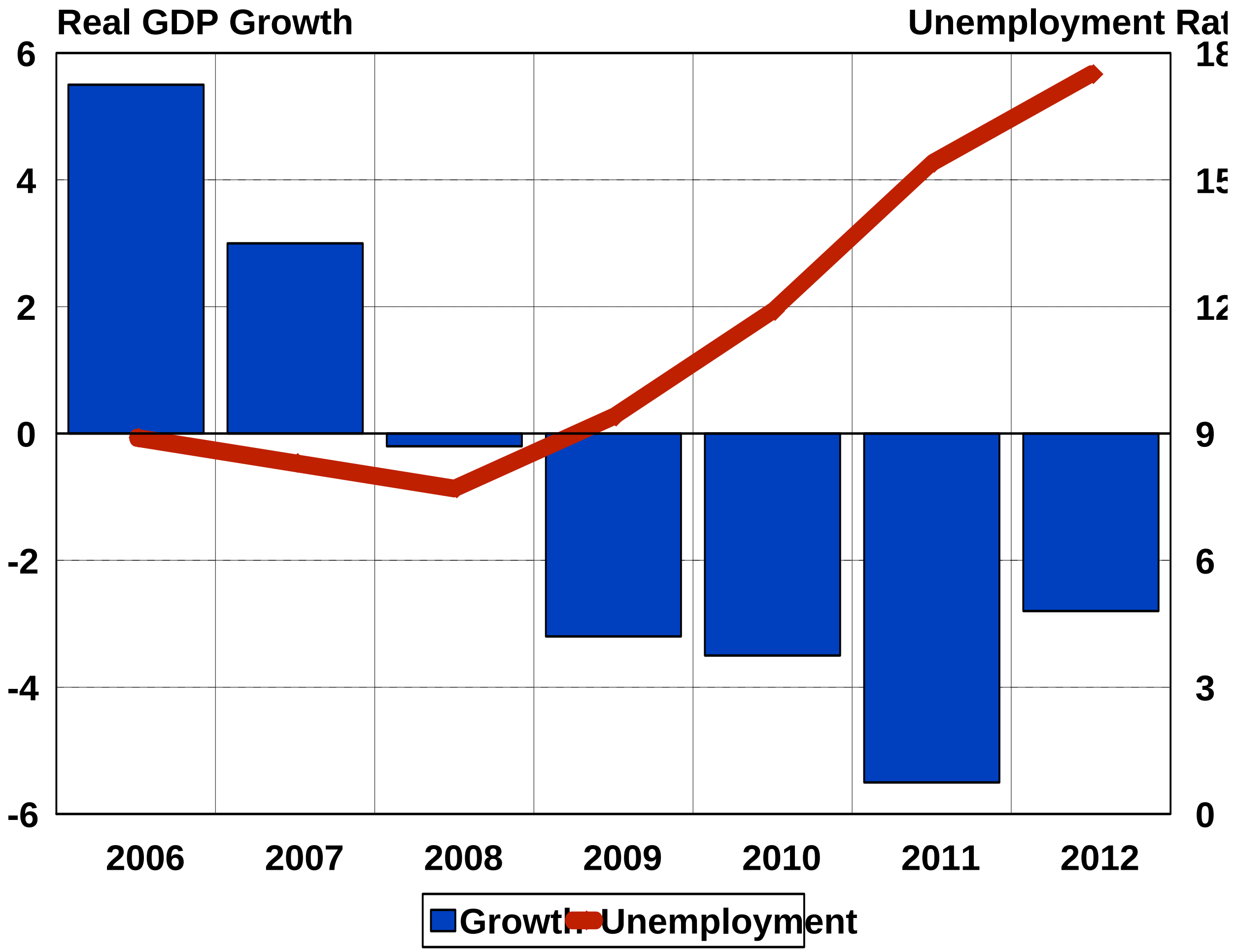
Where Are We Now?

A Hard Economic Landing for Greece

A cumulative decline exceeding 12% and a doubling of the unemployment rate

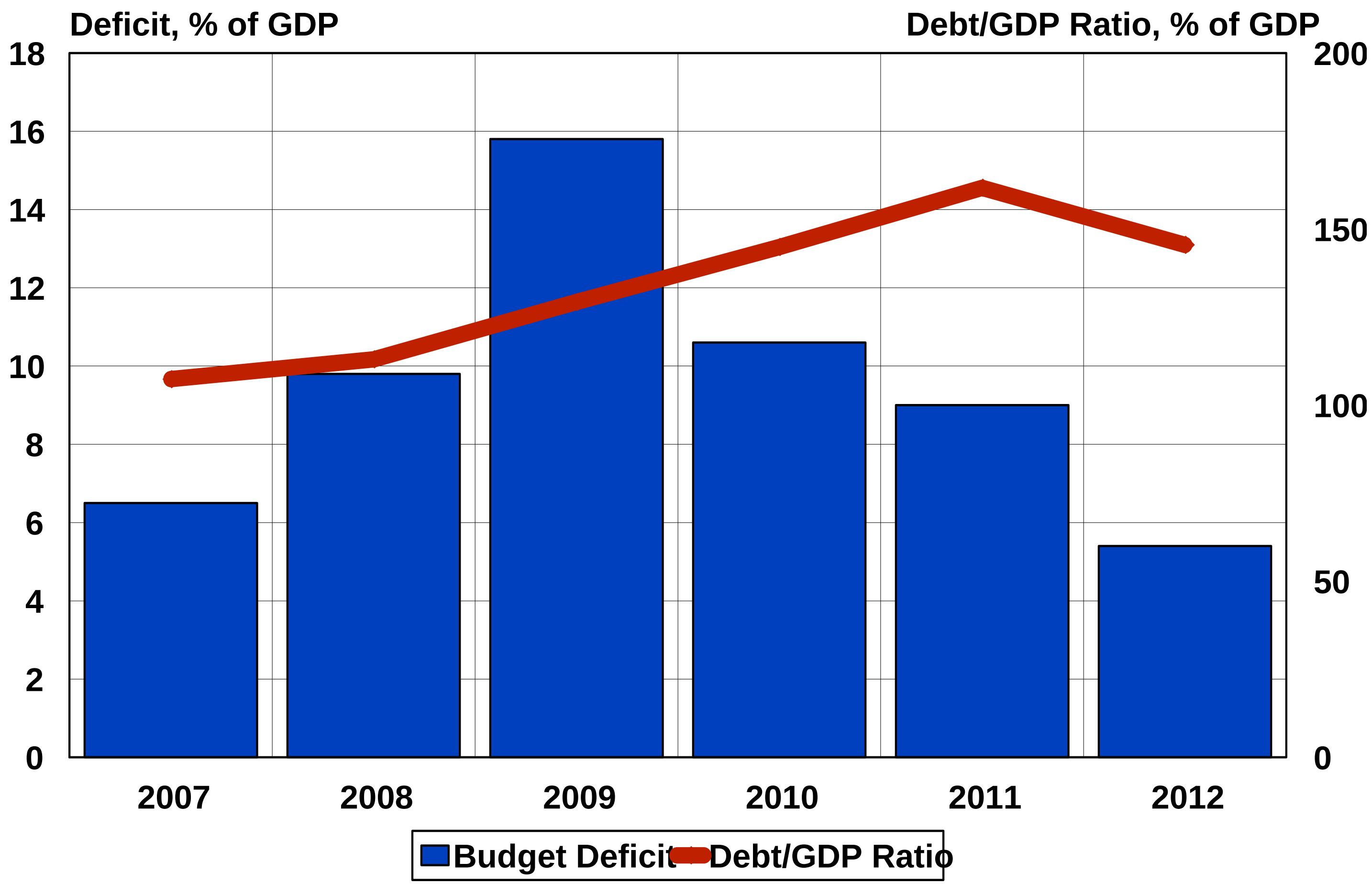


BASIC MACROECONOMIC INDICATORS, GREECE

	2006	2007	2008	2009	2010	2011	2012
GDP (Euros)	208,893	222,771	232,920	231,642	227,318	217,771	212,544
Private Consumption	4.3	3.7	4.0	-1.3	-3.6	-6.2	-4.1
Public Consumption	2.3	7.6	-2.1	4.8	-7.1	-8.0	-7.5
Capital Investment	19.2	10.1	-8.0	-26.6	-13.3	-12.9	-4.0
Exportts	3.1	6.9	3.0	-19.5	4.2	4.5	6.4
Imports	8.2	14.6	3.3	-20.2	-7.2	-5.9	-2.8
Growth Rate (%)	5.5	3.0	-0.2	-3.2	-3.5	-5.5	-2.8
GDP Price Deflator	2.5	3.5	4.7	2.8	1.7	1.4	0.4
Consumer Inflation	3.3	3.0	4.3	1.3	4.7	2.8	0.6
Unemployment Rate	8.9	8.3	7.7	9.4	11.9	15.4	17.1

Source: Hellenic Statistical Service (ELSTAT) and Ministry of Finance, 2012 Budget

Surging Budget Deficits and Upward Revisions to Public Debt



Latest and More Accurate Figures on Greek Economy

- The figures presented here on Greece’s GDP and public finances are the latest figures available: October 5, 2011 Revised Greek Annual Accounts for period 2005-2010 and October 17, 2011 Revised Fiscal Accounts published by the Hellenic Statistical Authority (ELSTAT) as well as the 2012 Budget submitted to Parliament on November 17, 2011 by National Economy Minister Evangelos Venizelos
- Fiscal Projections for 2011 and 2012 are based on the 2012 budget and **assume** the implementation of a **Private Sector Initiative** (PSI) reduction of **50%** in the privately held debt of the Greek state

PUBLIC FINANCES, GREECE

		2007	2008	2009	2010	2011	2012
GDP	Bil Euros	222,771	232,920	231,642	227,318	217,771	212,544
Receipts		90915	94764	88070	89750	85027	89583
Outlays		106066	117850	124636	114213	105483	100190
Budget Deficit	Bil Euros	**-14475**	**-22822**	**-36624**	**-24125**	**-19683**	**-11427**
	% of GDP	**-6.5**	**-9.8**	**-15.8**	**-10.6**	**-9**	**-5.4**
Interest Costs	Bil Euros	10684	11937	11915	13205	15873	12787
Public Debt	Bil Euros	239300	263131	299537	329351	352050	309300
	% of GDP	**107.4**	**113**	**129.3**	**144.9**	**161.7**	**145.5**
Primary Balance		-3791	-10885	-24709	-10920	-3810	1360
			232920	232920	232920	232920	232920
Income Effect			113%	129%	141%	151%	133%
Interest/GDP Ratio		**4.8%**	**5.1%**	**5.1%**	**5.8%**	**7.3%**	**6.0%**
Aver Interest Rate		4.5%	4.5%	4.0%	4.0%	4.5%	4.1%

Source: Hellenic Statistical Service (ELSTAT) and Ministry of Finance, 2012 Budget

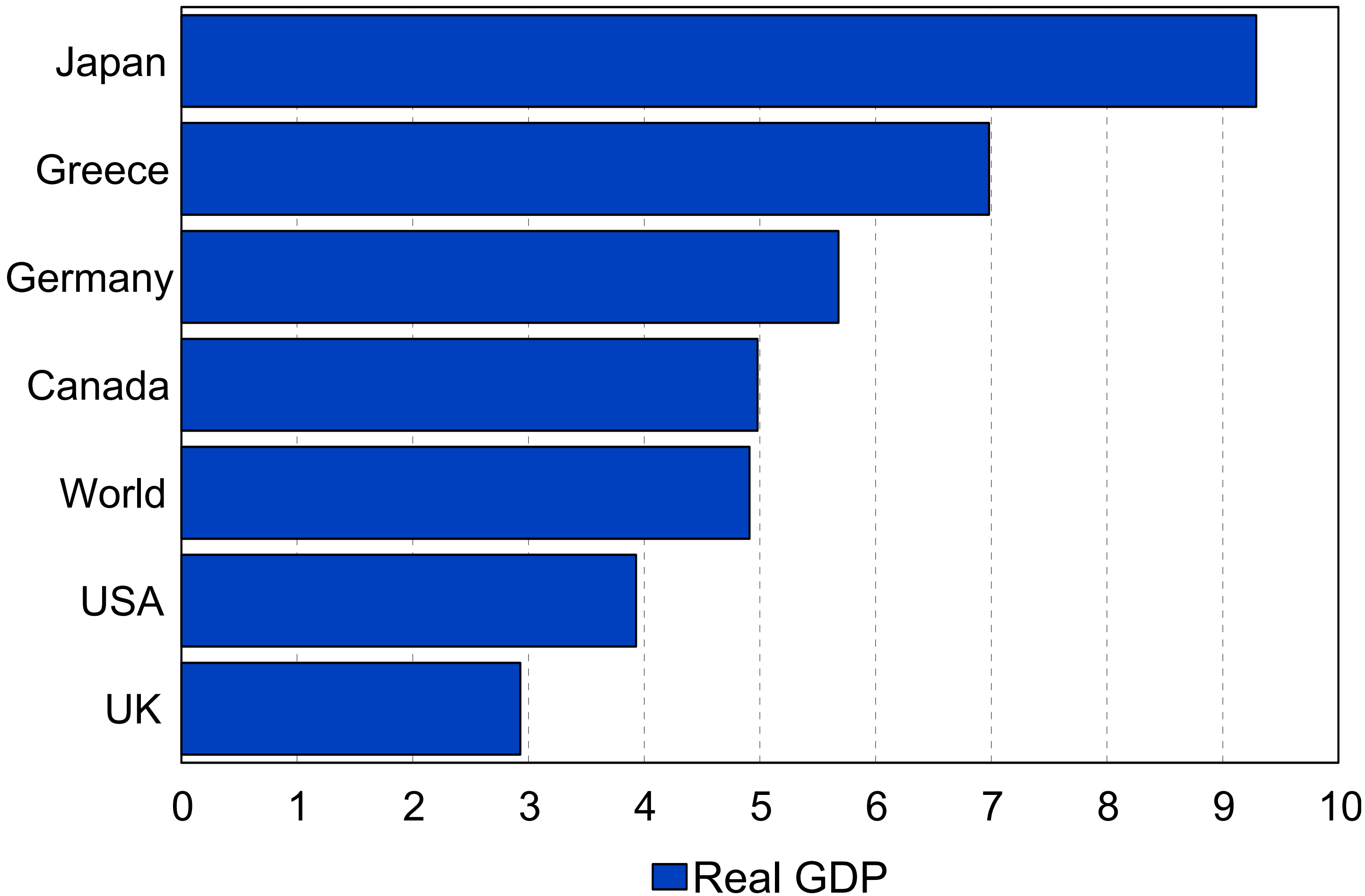
INDEBTEDNESS AND LEVERAGE				
Gross Levels, % of GDP	**USA**	**UK**	**EURO**	**GREECE**
Government Debt	100	83	87	150
Household Debt	91	107	72	68
Corporate Debt	76	128	142	71
Financial Debt	97	735	148	21
Gross Debt/GDP	**364**	**1053**	**449**	**310**
Bank Leverage	13	24	26	17
Debt/Equity Ratio	105	89	72	218
External Govern Debt	32	27	29	61
Net Int Invest Pos. NIIP	19	14	13	99
Source: IMF, Financial Stability Report, April, 2011				

Has Greece Always Done So Badly?

Actually, NO

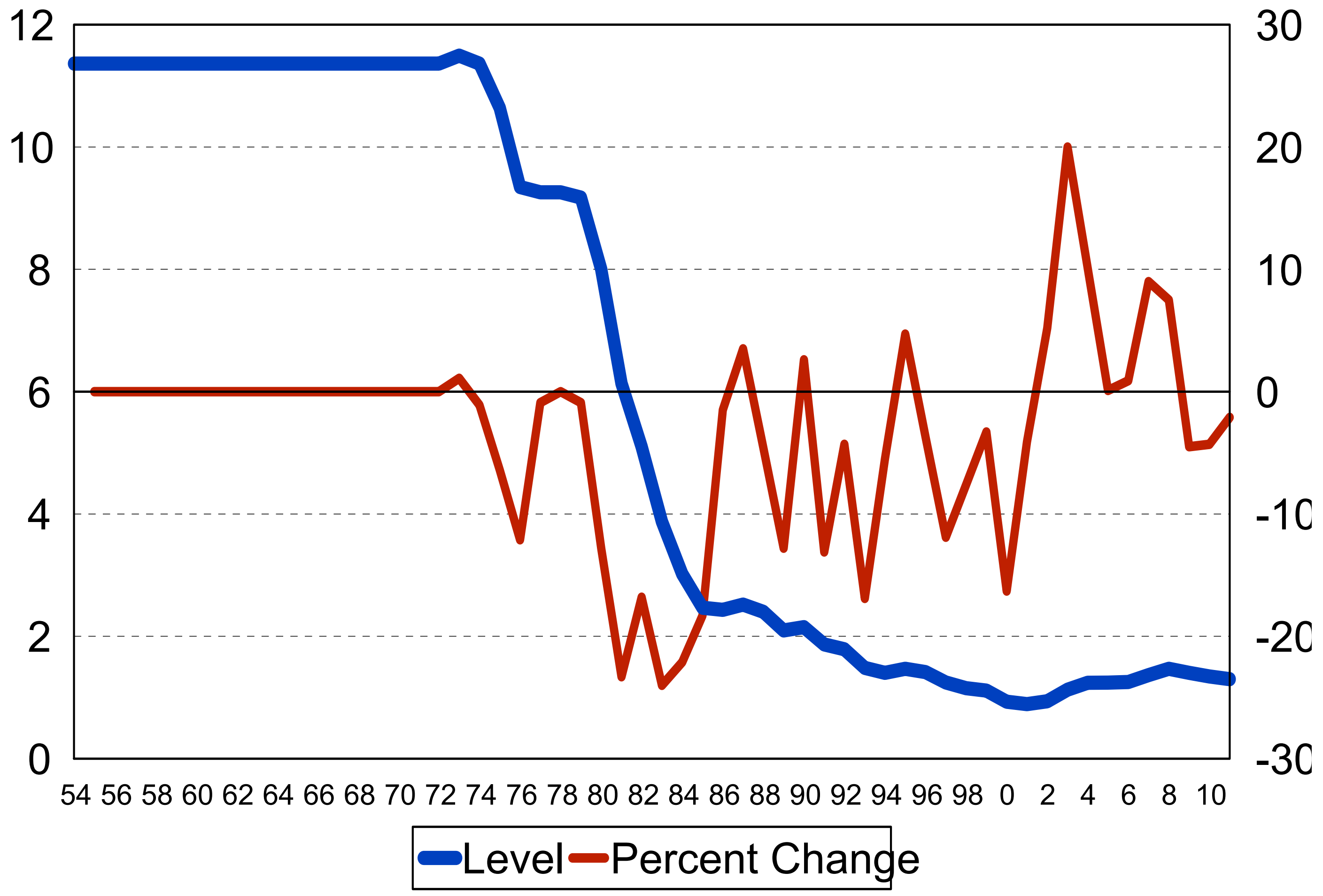
GDP Growth Rates, 1950-1973

OECD, The World Economy: A Millennial Perspective, Angus Maddison, 2001



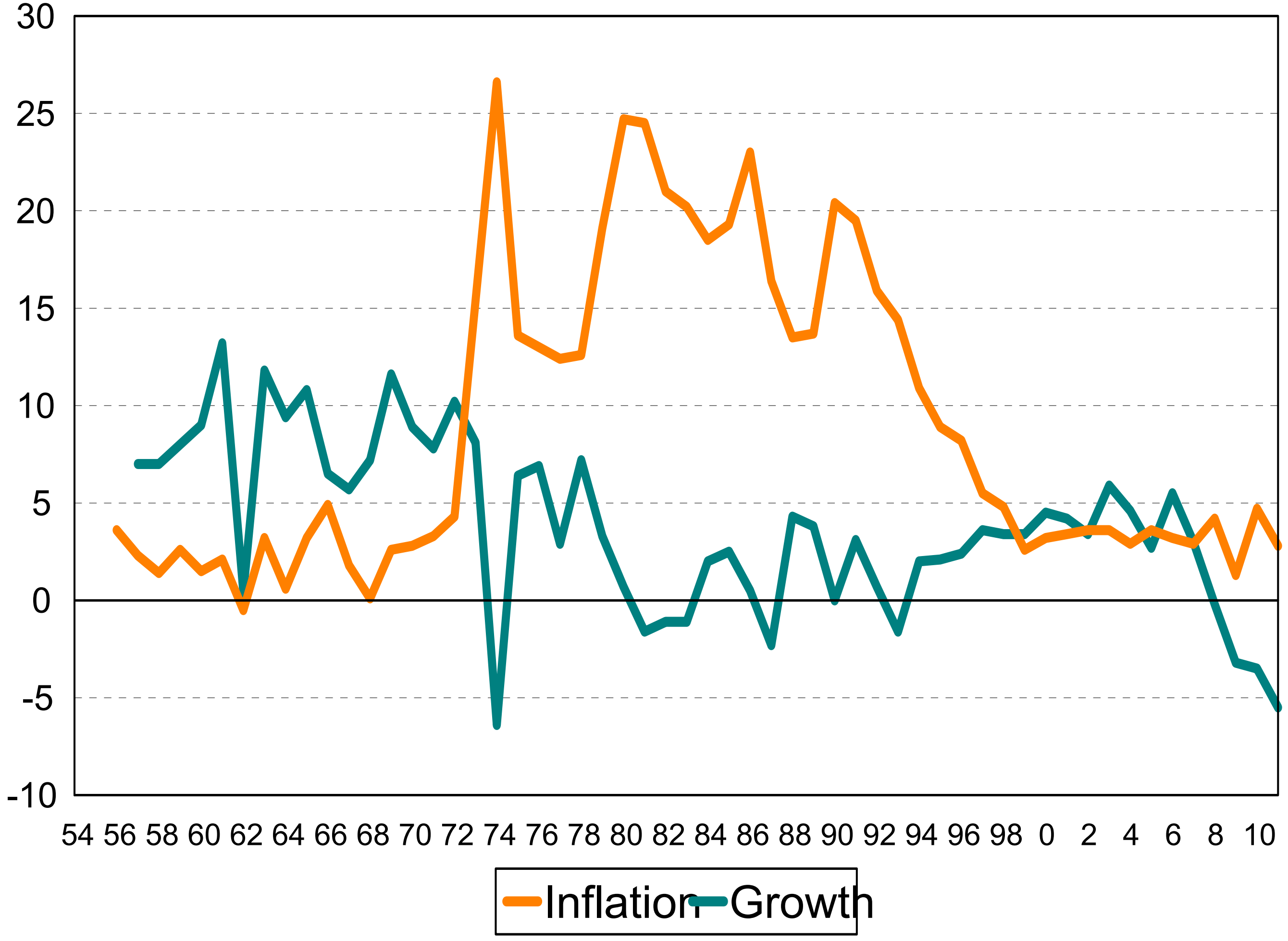
Greek Drachma USD Exchange Rate: 1954-2011 ,Euro since 2001

Greece experienced its fastest growth and lowest inflation under the Bretton Woods system of fixed exchange rates (1954-73)



Inflation & Growth Rates Greece: 1956-2010

There is an inverse relationship between growth and inflation, monetary discipline encourages prosperity



What Went Wrong?

- The breakdown of the Bretton Woods system of fixed exchange rates in 1971-73 unleashed a period of monetary instability, high inflation and low growth, Greece was no exception
- By the early 1980s most countries brought inflation under control, economic growth increased, but that was not to be the case for Greece
- With the election of PASOK in 1981, there was regime change in Greece, good for democracy but bad for the economy
- PASOK took a highly populist path appealing to peoples' weaknesses and bad habits, i.e. responded to financial insecurity by providing government jobs, increasing pensions and introducing social entitlements that were alien in Greek society, they expanded the power of unions and made the private business and industrial class subservient to the politicians and the unions, they set up a system of entitlements, monopolistic privileges and government regulations that undermined the work ethic, discouraged private business initiative, increased dependence on politicians and petty bureaucrats and fostered corruption, sloth, and kakistocracy. Breaking or by-passing rules and values became the norm rather than the exception.

What Went Wrong?

- Many of Greece’s top industrial enterprises were nationalized, putting politicians and labour unions in charge; the government borrowed huge amounts to fund massive losses
- The debt to GDP ratio reached 100% of GDP by 1993 and the central bank resorted to printing money to pay the bills, unleashing 20% inflation
- The only bright spot in the PASOK record was Kostas Simitis, as Finance Minister in the 1980s he made great efforts to remove the excesses and restore stability to the economy, again as Prime Minister after 1996 he did the same and was successful enough to enable Greece’s entry into the Eurozone in 2001
- Greece attained macroeconomic stability, growth accelerated, it entered the Euro-core of nations and won the bid to host the Athens 2004 Olympic Games.
- By 2004, Greece’s stature, credibility and geopolitical importance had reached the highest point in its modern history. The UEFA Euro 2004 soccer victory, coupled with the Athens 2004 Olympic Games were some of the beneficial outcomes of reforming the economy and changing its attitudes

What Went Wrong?

- Greece's image in the world had changed. For the first time in its modern history, Greece was viewed as a successful advanced industrial country, the envy of its neighbours.
- At the same time the self-image of Greeks changed, they started thinking of themselves as a prosperous people who could expect the same standard of their Northern-European peers.
- To brake the stronghold on the political power that the PASOK had achieved, the conservative New Democracy (ND) party of Kostas Karamanlis decided to outdo the PASOK's populist strategy when it came to power in 2003. Although it started with good intentions by 2007 started giving in on the populist demands and started cutting taxes and raising spending
- Instead of using the opportunity of the reduction in interest rates that entry into the Eurozone had brought to Greece and reducing the debt, by 2007 the ND started doing the opposite. In light of Greece's high public debt/GDP ratio and the large budget deficits, it should have been cautious and exercise restraint. Instead, it did the opposite. The run-up in public spending and surge in the budget deficit can only be described as patently irresponsible.

What Went Wrong?

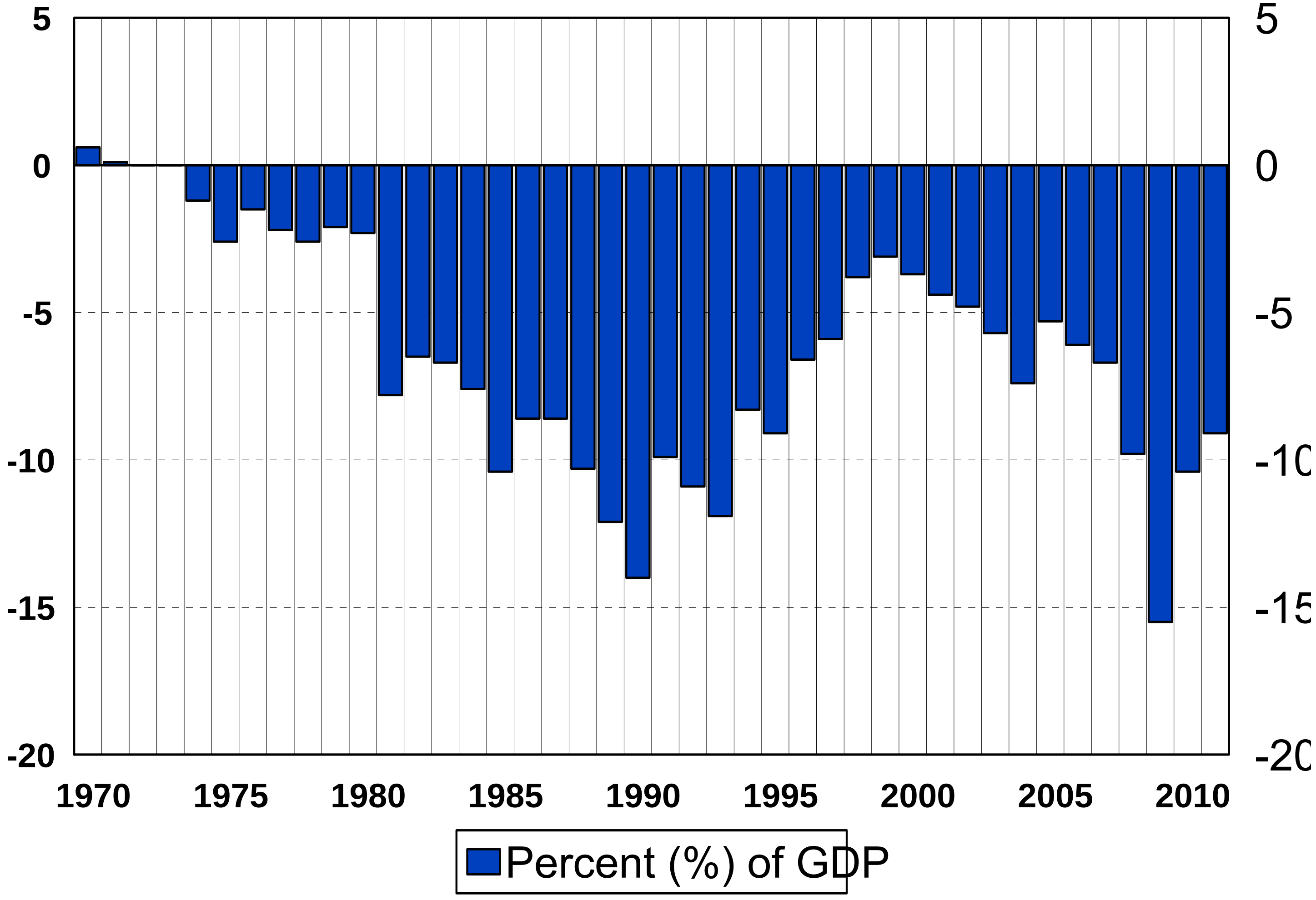
- Membership in the Eurozone brought Greece enormous benefits but also enormous responsibilities
- Greece had to stay within the Maastricht Treaty rules of maintaining budget deficits below 3% and reducing the debt/GDP ratio over time to 60%
- Greece’s competitiveness would have to increase over time by increasing productivity (output per worker) and ensuring that salaries did not rise faster that productivity
- Between 2001 and 2008 Greek productivity rose by 2.2%, one of the highest rates in the Eurozone, but it allowed wages to rise even faster which increased unit labour costs and reduced its competitiveness
- At the same time, despite repeated calls to reform its economy and political institutions from the EU Commission, the OECD, the IMF, the central bank and its business leadership (SEV), the Greek political establishment failed to heed the calls because of opposition from the powerful unions and fears of the political cost this would entail. Politics tramped common sense.

What Went Wrong?

- Then came the inevitable. The external shock of the 2008 global financial crisis and the global recession that followed in 2009 and the new risk averse environment of global financial deleveraging
- True, Greece is not to blame for the global recession, and true, entry into the Eurozone made its position more difficult to sustain.
- But it is also true that Greece went way out of its way to ask for trouble. It had not used the early years to reform its institutions and enhance its competitiveness.
- Instead of increasing its saving and investment to 20% of its GDP, it went on a spending spree of titanic proportions
- Every society needs to save at least 20% of its annual income and invest in factories, equipment, buildings and infrastructure at least 20% of its output.
- To raise salaries you need to raise productivity, you can’t ask your employer to pay you more than you give to him.
- To increase competitiveness, you need to work smarter, be innovative, increase productivity and reform your institutions in order to make all this possible. Otherwise, tragedy awaits you and this is what happened to Greece.

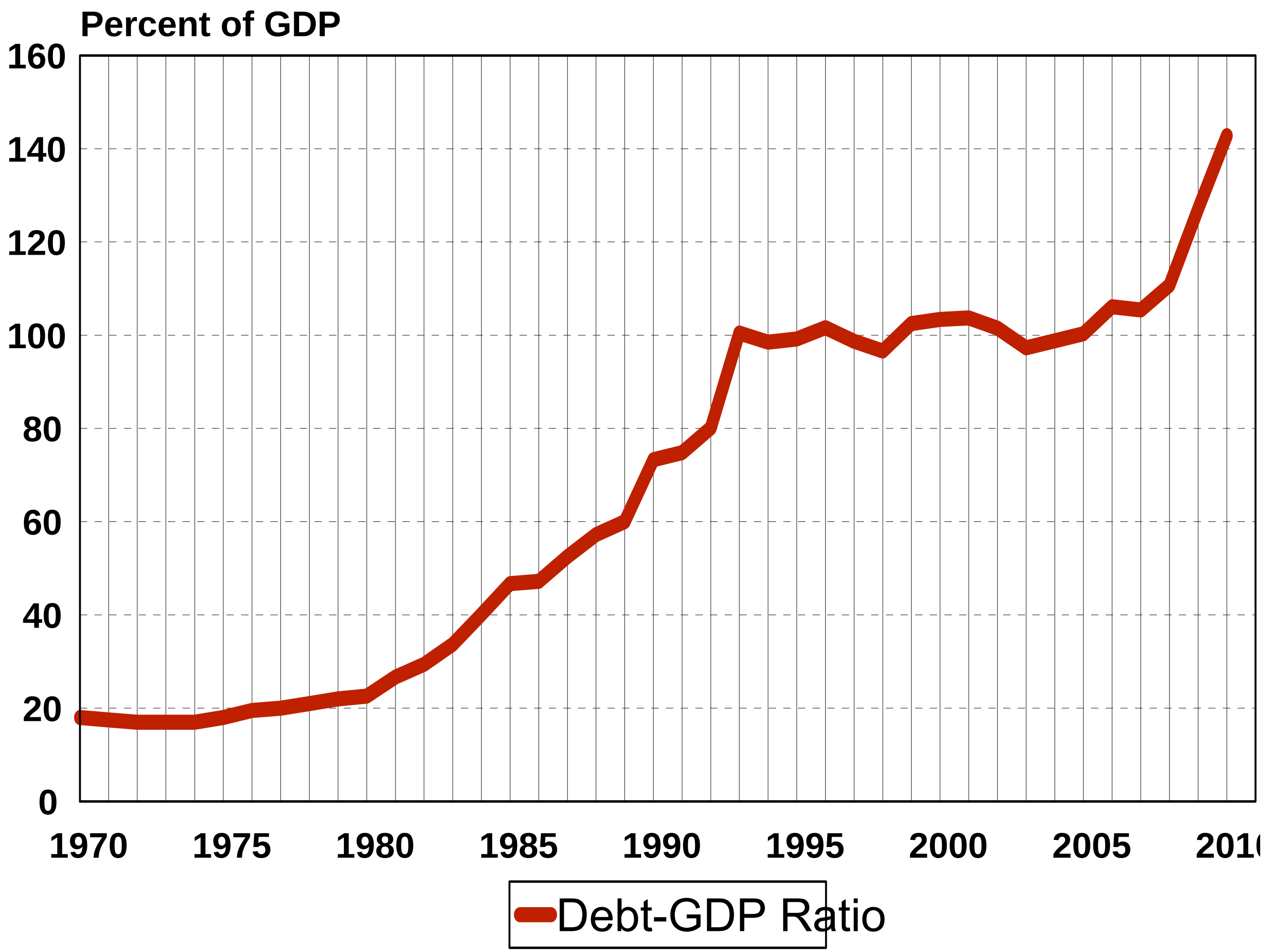
Budget Deficits, Greece: 1970-2011

Greece has not balanced a budget since 1973



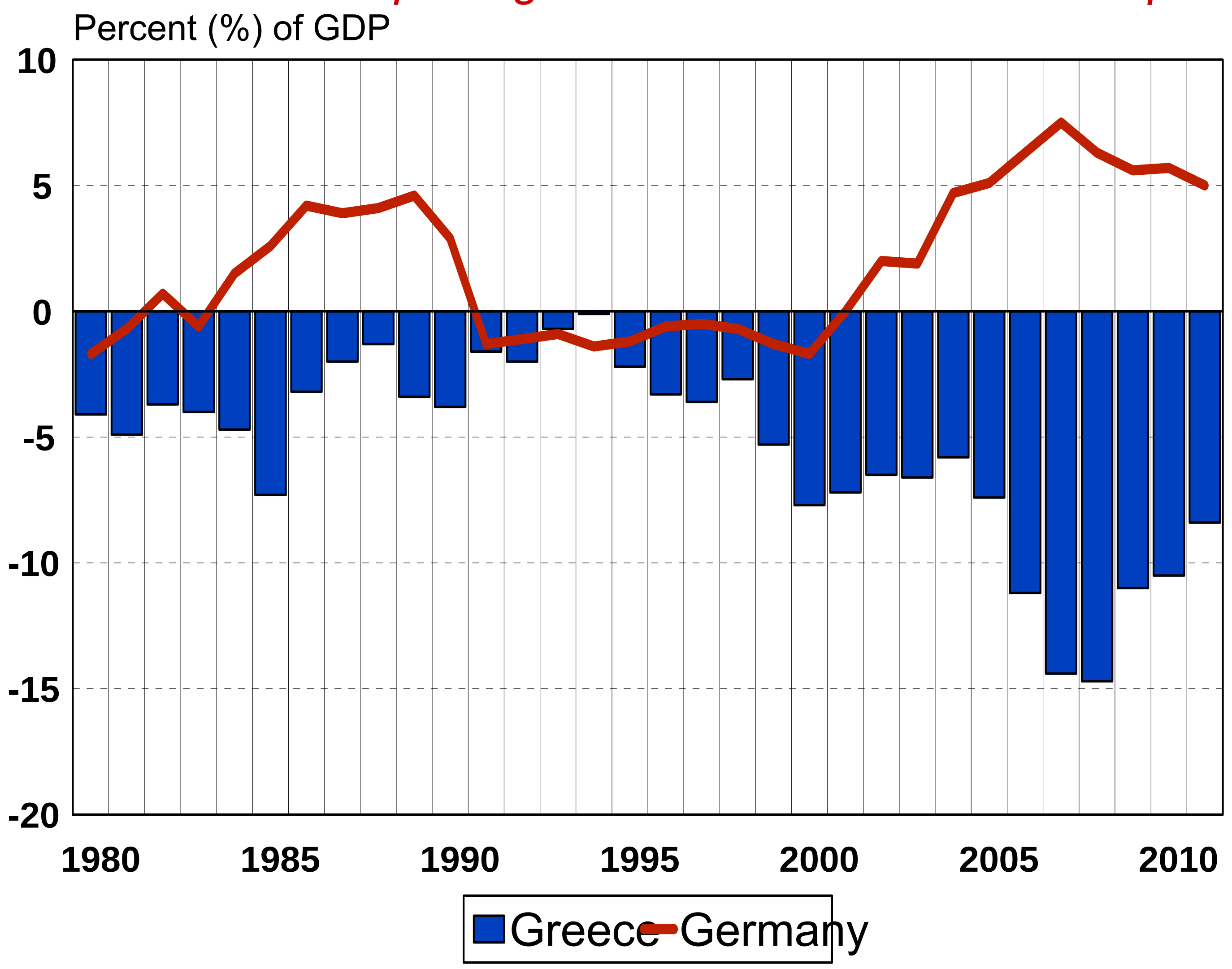
Debt-GDP Ratio, Greece, 1970-2010

Between 1980 and 1993 public debt rose fivefold from 20% to 100% of GDP

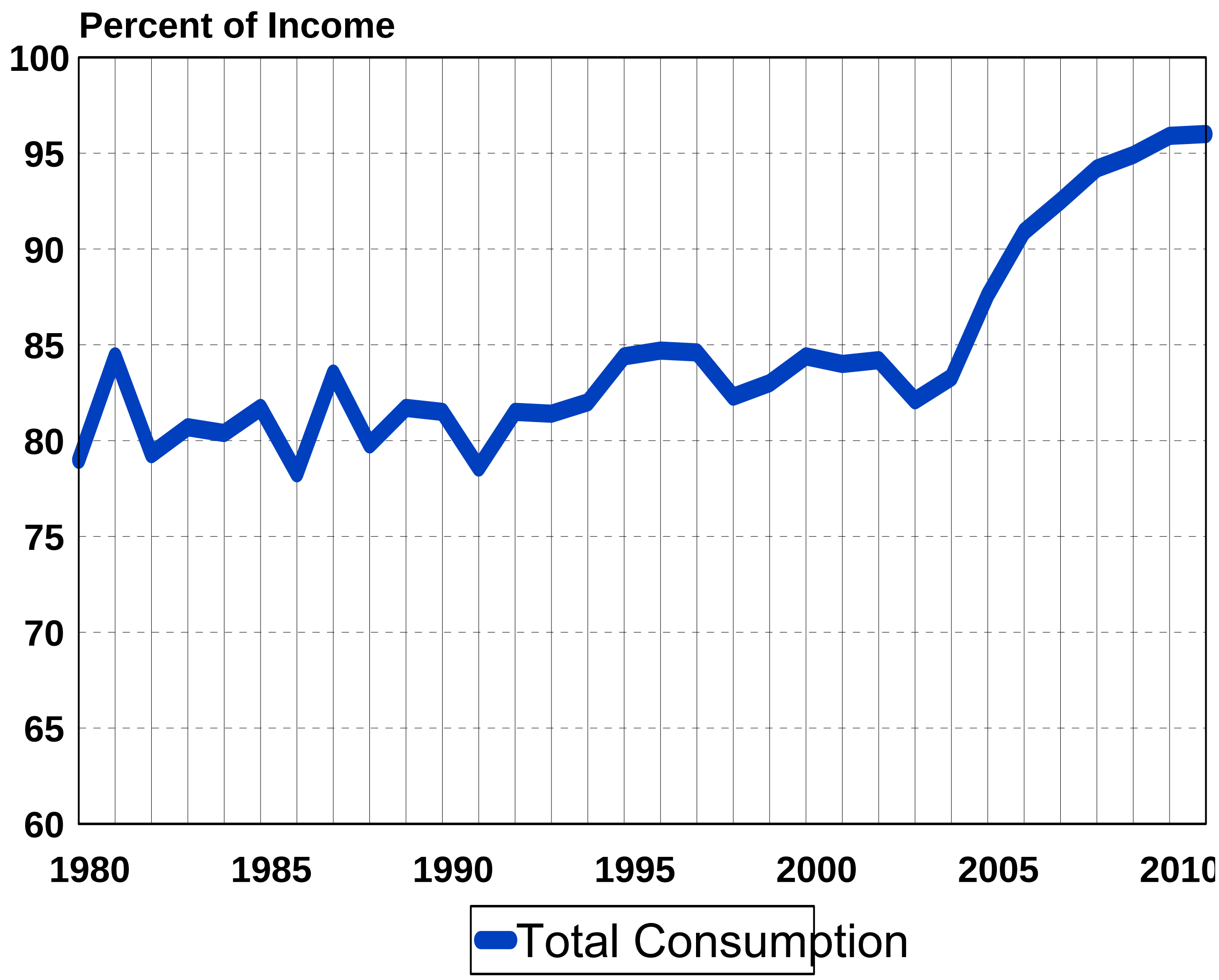


Current Account Deficits: Greece vs. Germany, 1980-2011

Greece has been importing far more than it has been exporting

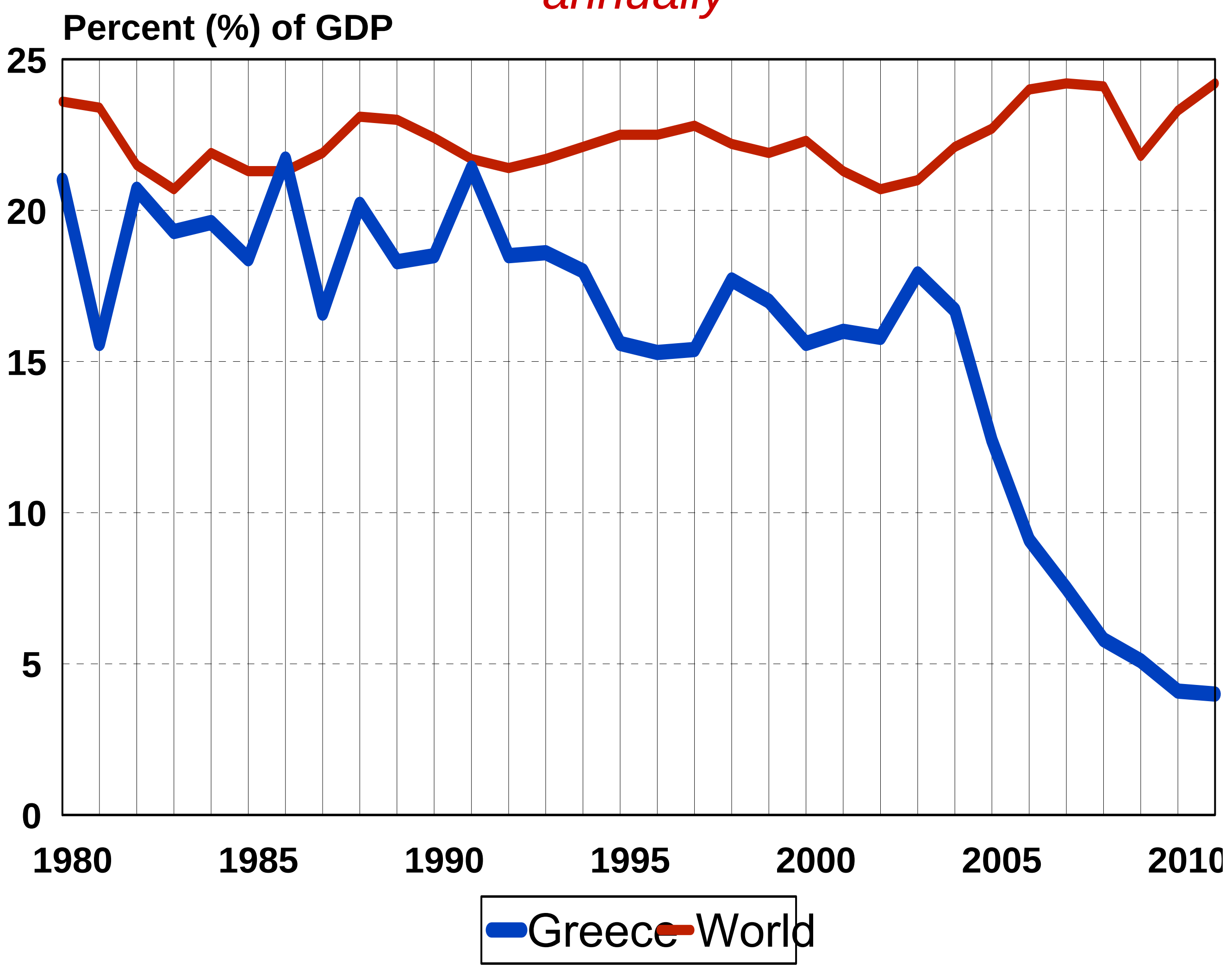


Private & Public Consumption as Percent of GDP, Greece 1980-2011



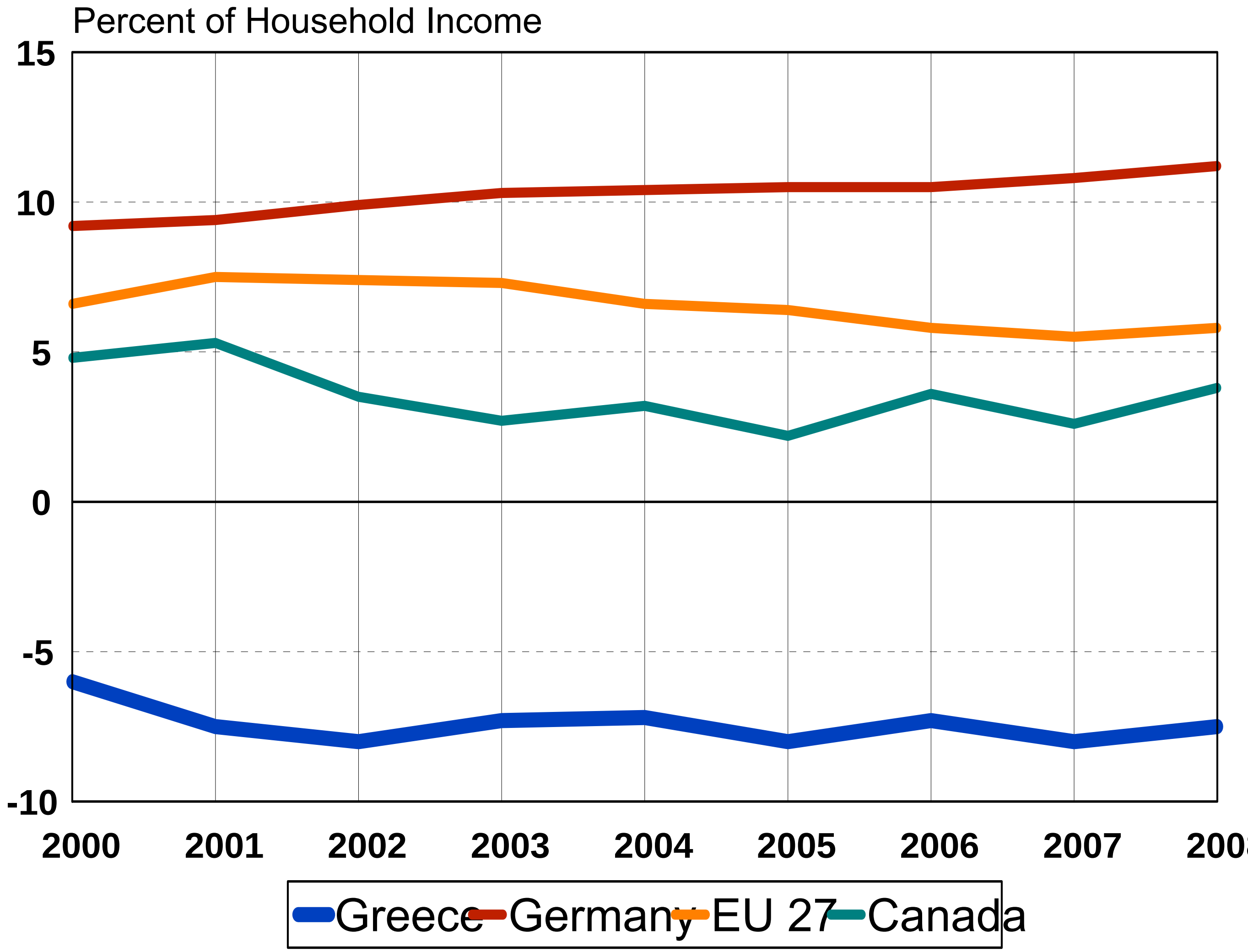
National Saving Rates: Greece vs. World, 1980-2011

A mature developed economy needs to save at least 20% of its income annually



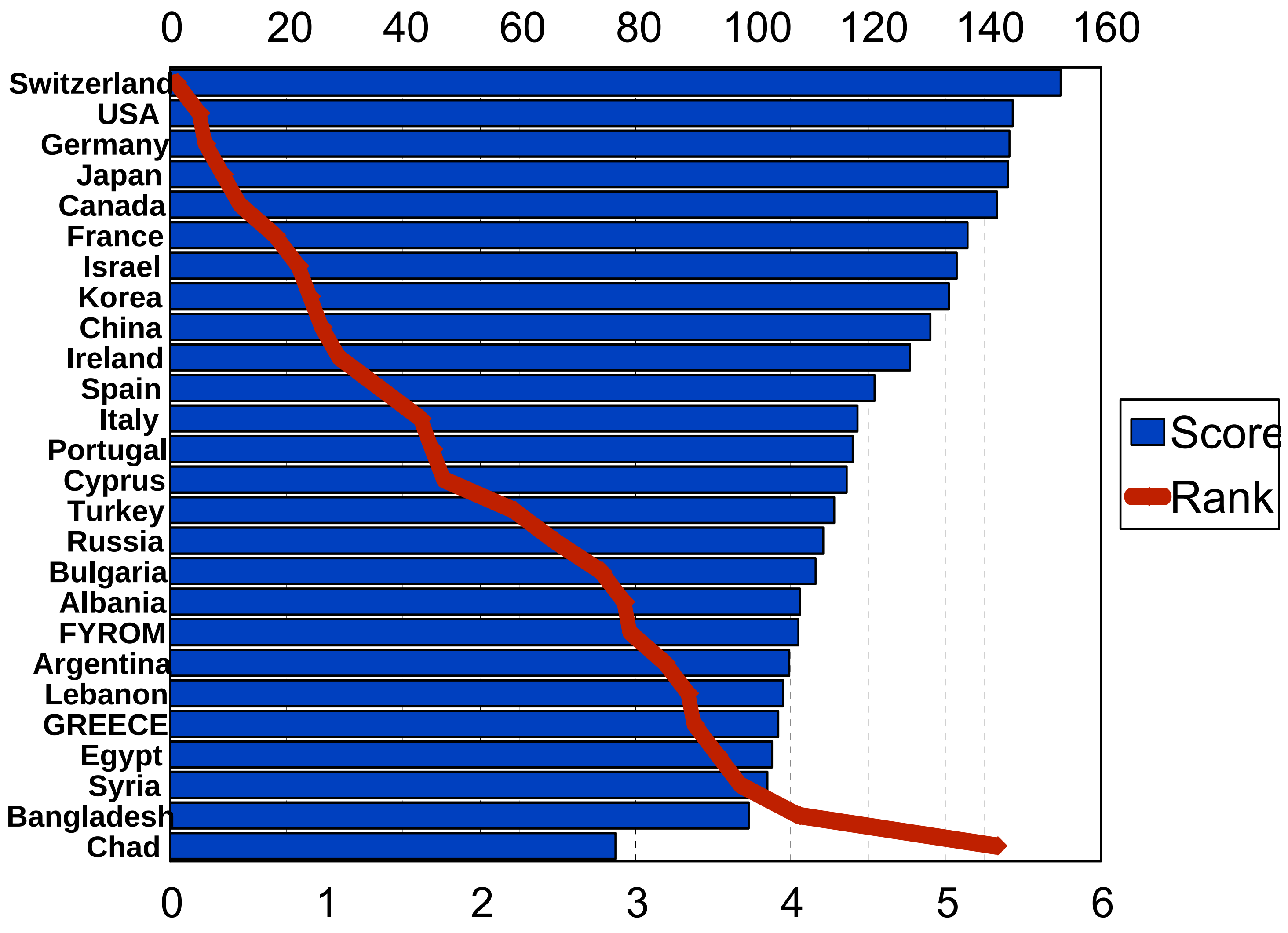
Household Net Saving Rates: 2000-2008

Hard to believe, Greeks have been consistent dis-savers



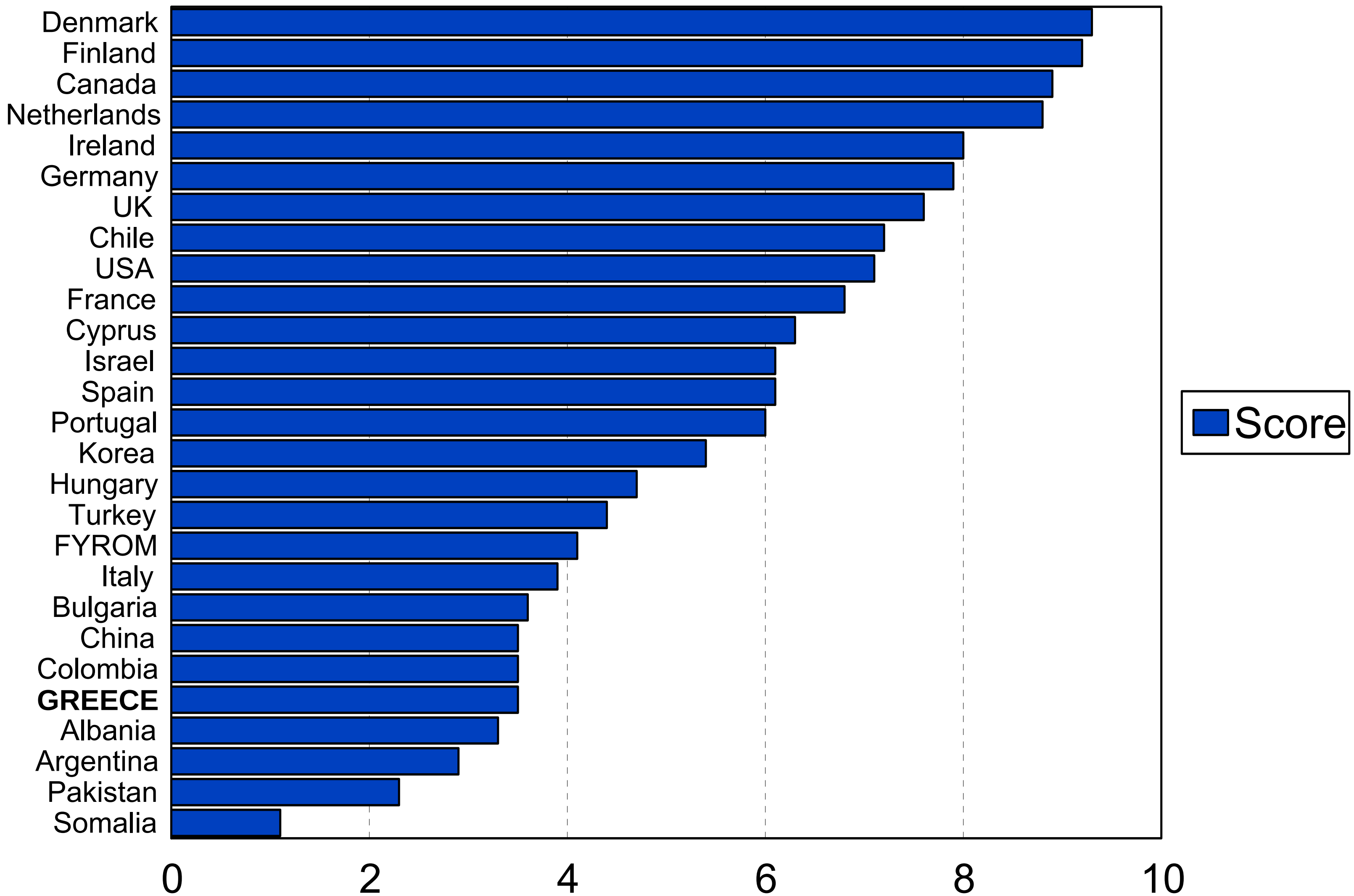
Global Competitiveness Index Rankings, WEF, 2011-12

Greece ranks 90th out of 142 countries



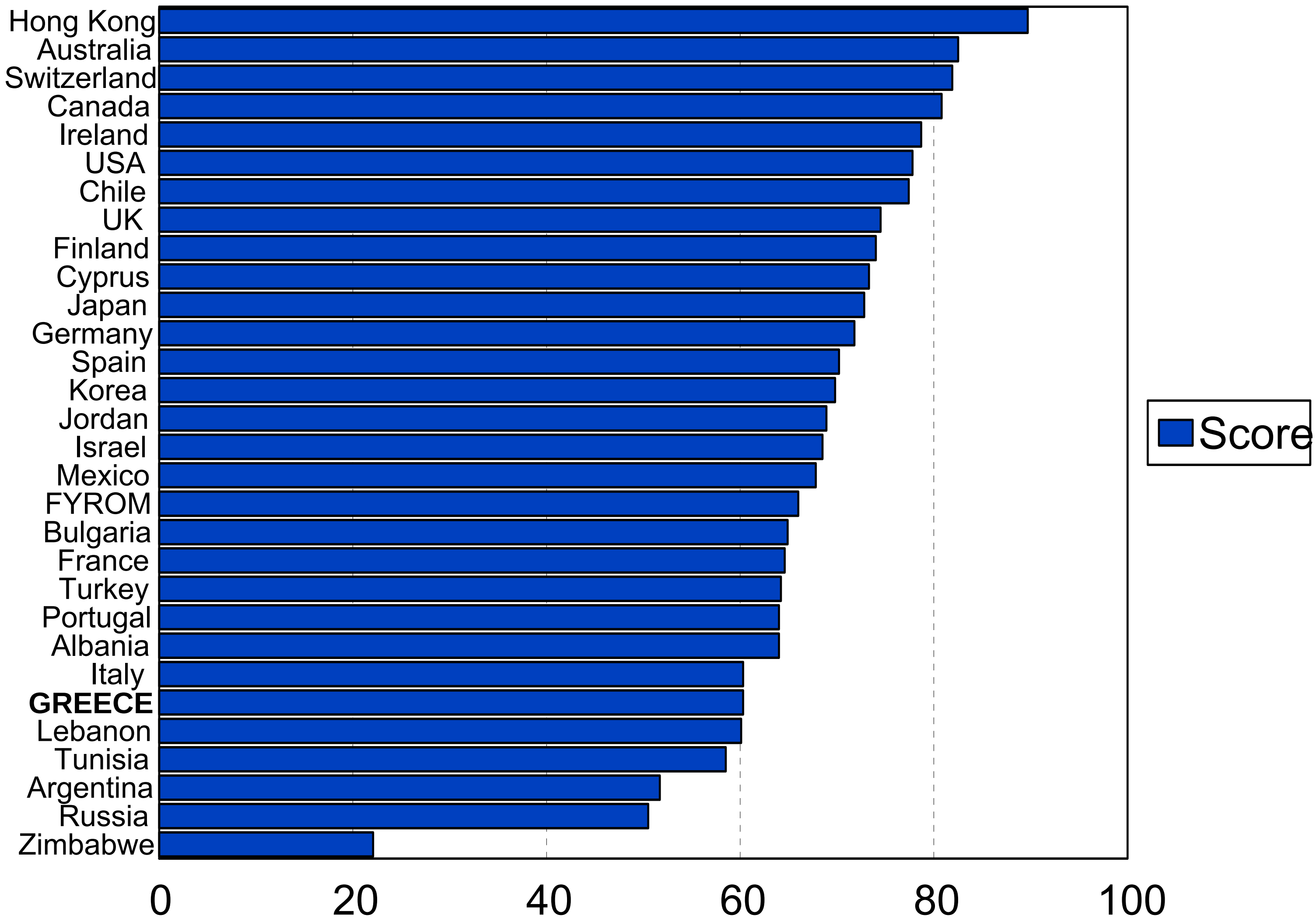
Corruption Index, 2010

Greece scores 78th out of 178 Countries



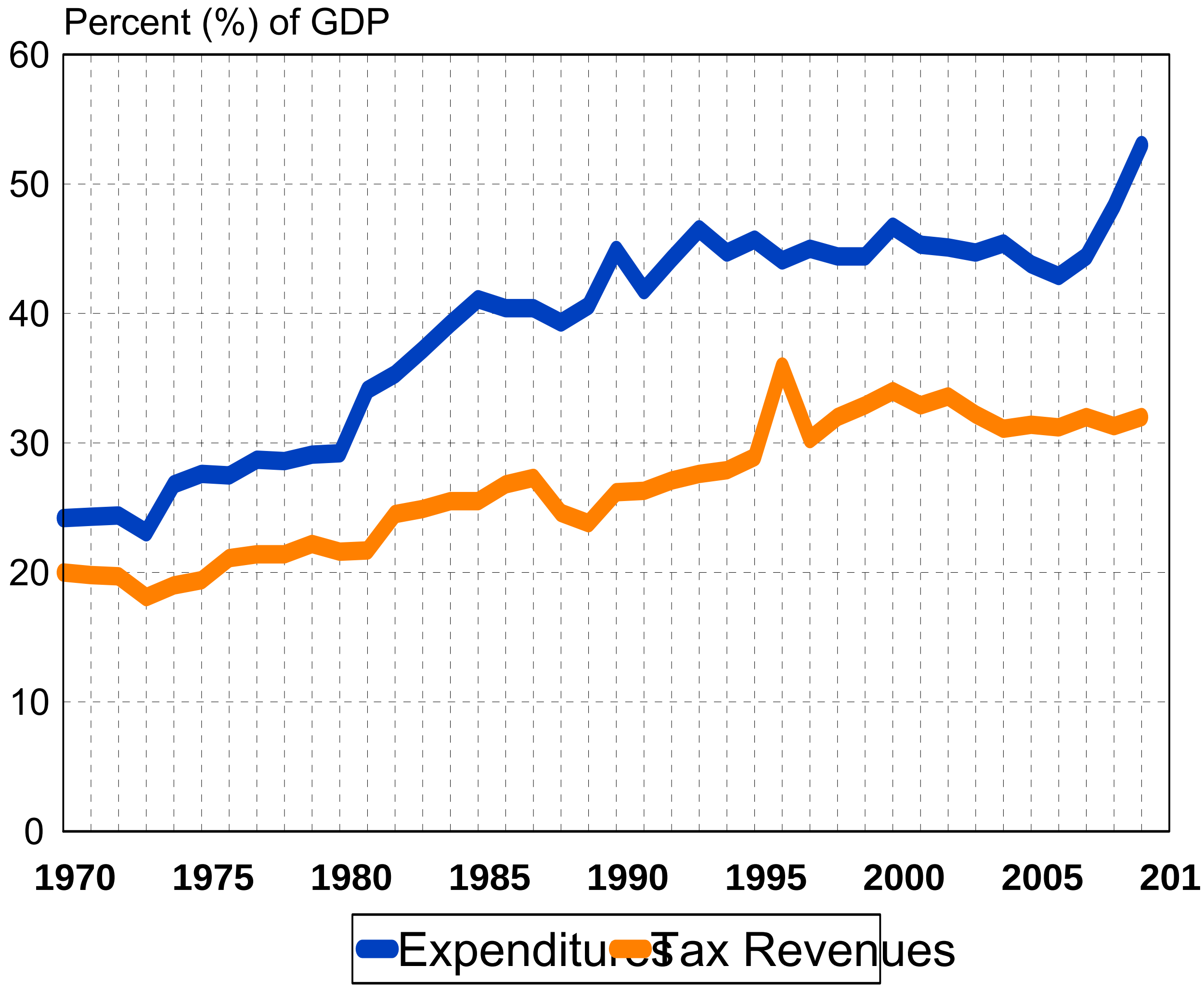
Economic Freedom Index, 2011

Greece scores 60.3, 88th out of 179 countries



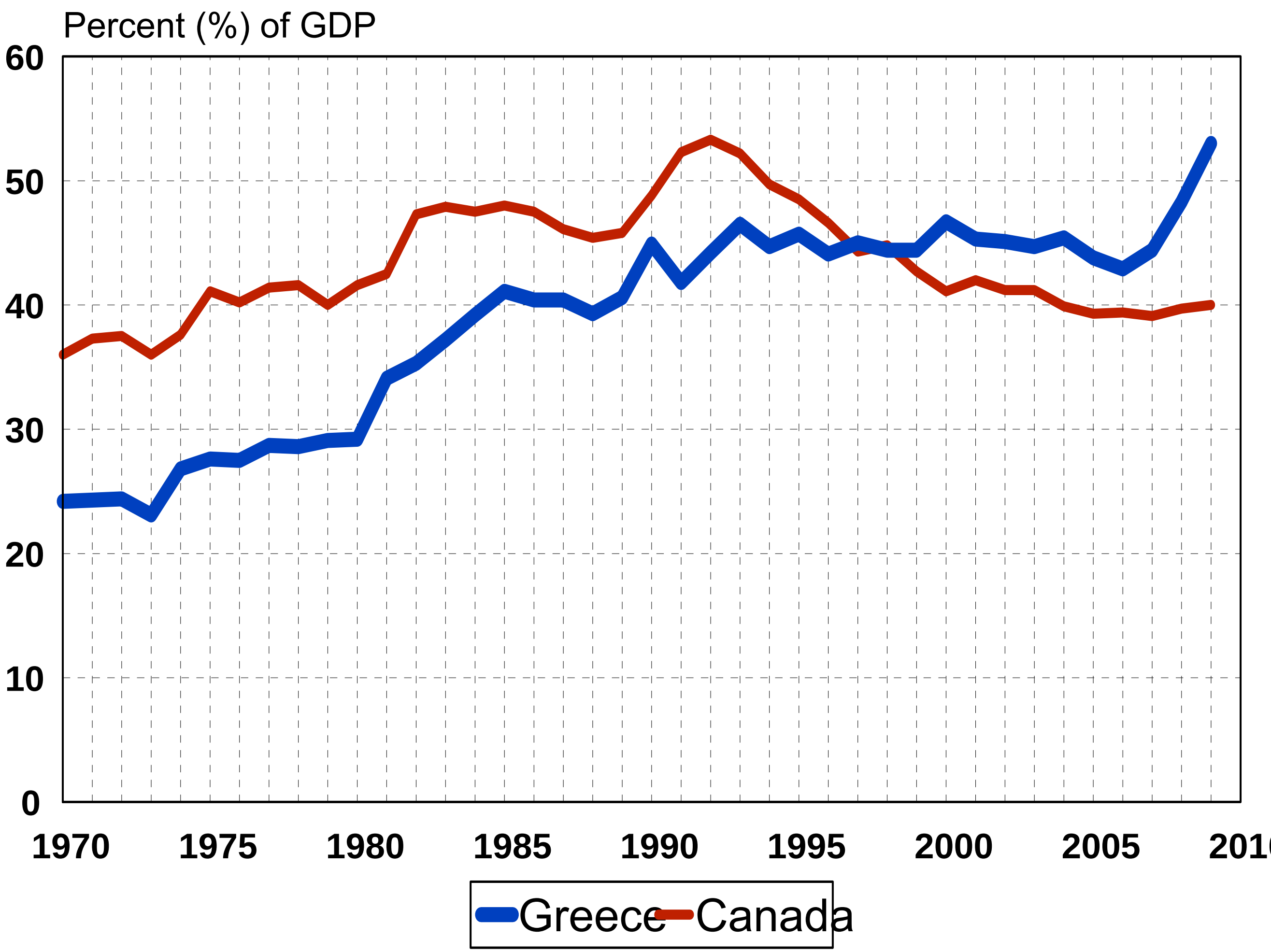
Government Spending & Tax Revenue as a Share of GDP, Greece 1970-2008

Government spending exceeds 50% of economy



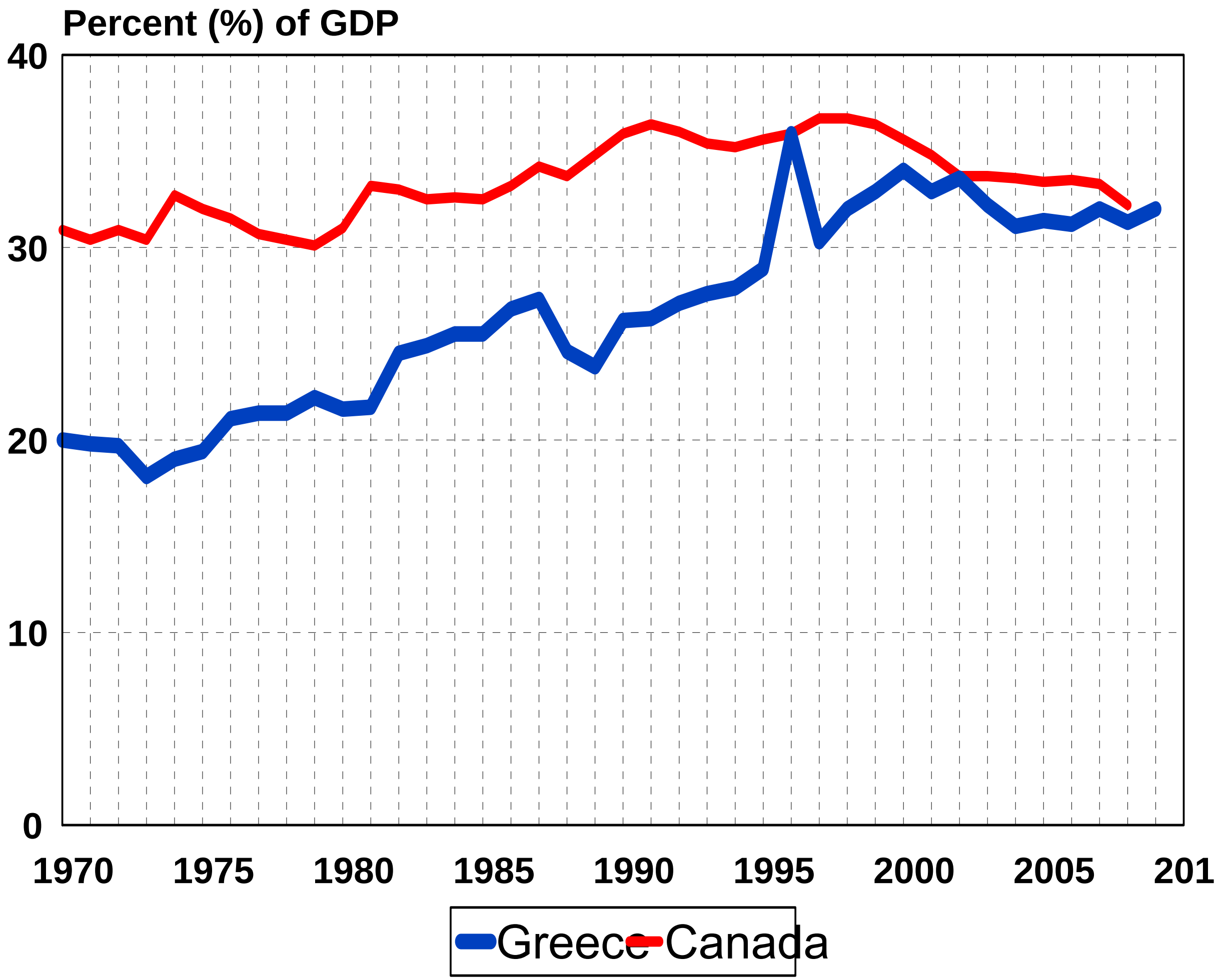
Government Spending Shares: Greece vs Canada, 1970-2008

Can a less affluent country afford to spend more?



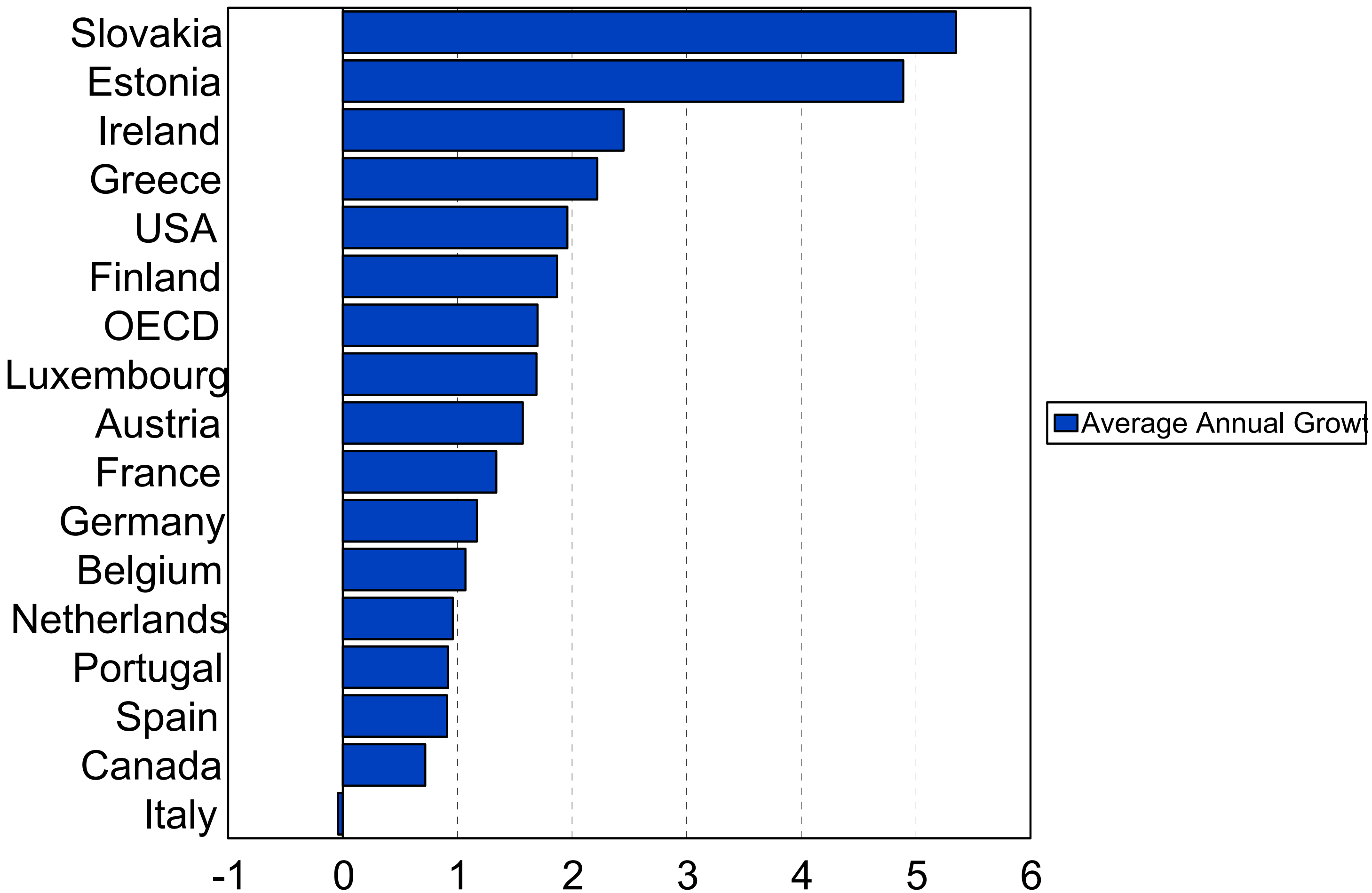
Tax Shares, Greece vs Canada: 1970-2008

There is a limit to how much you can tax your people!



Labour Productivity Growth: 2001-2008

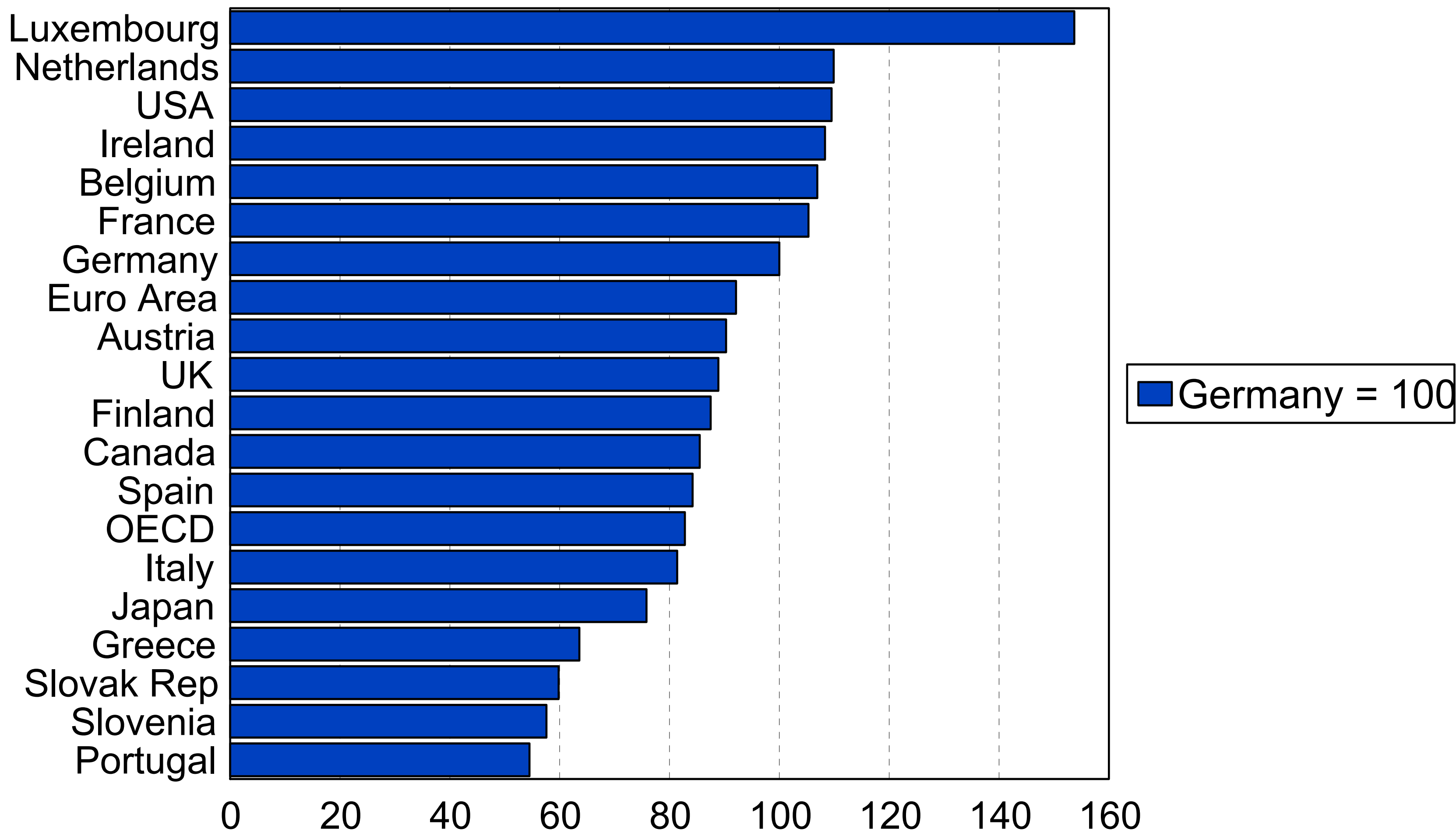
Greek productivity growth has been very good, it averaged 2.2%



Labour Productivity, 2008

GDP per hour worked, current prices & PPPs

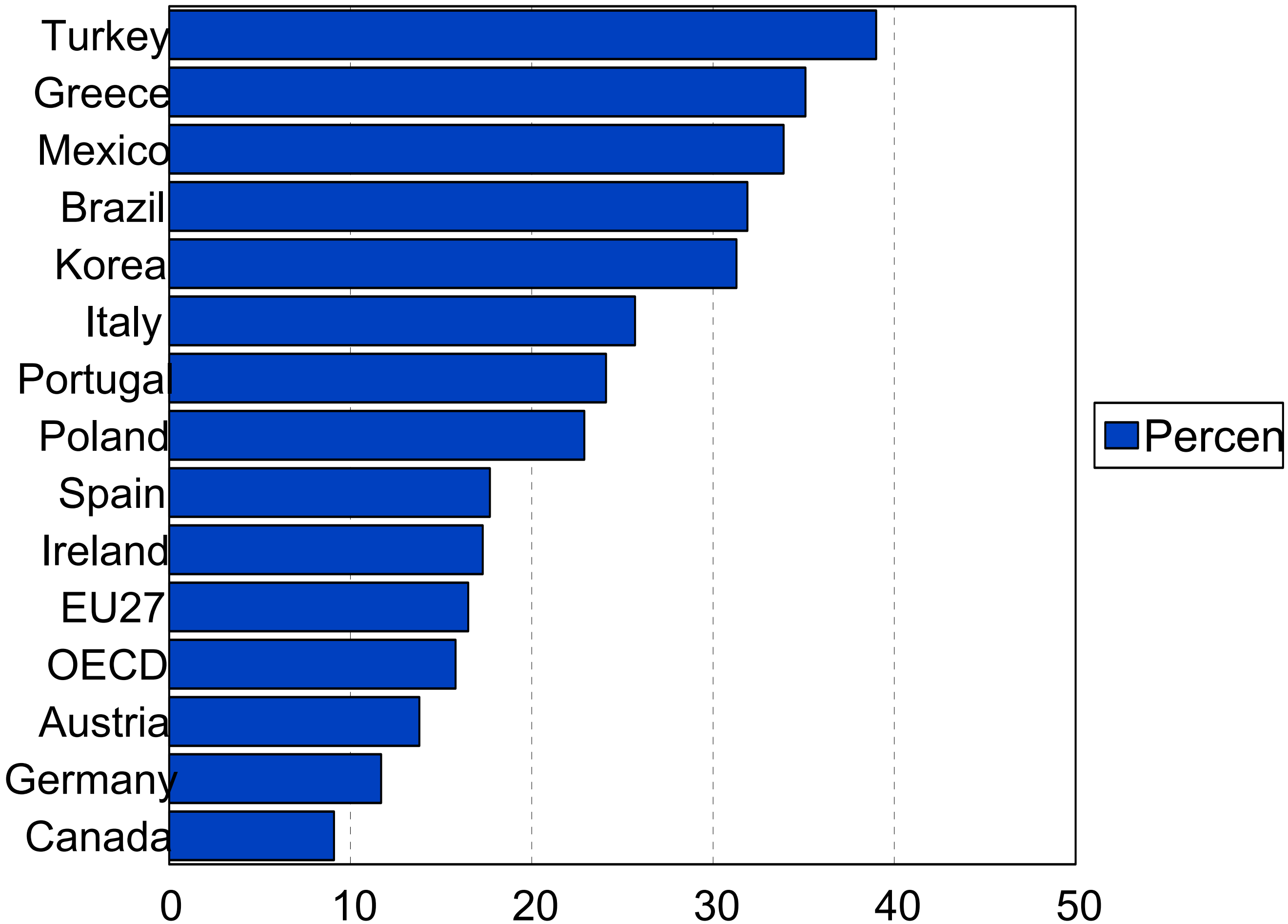
Yet it still 63.6% of that of Germany



Self Employment Rates

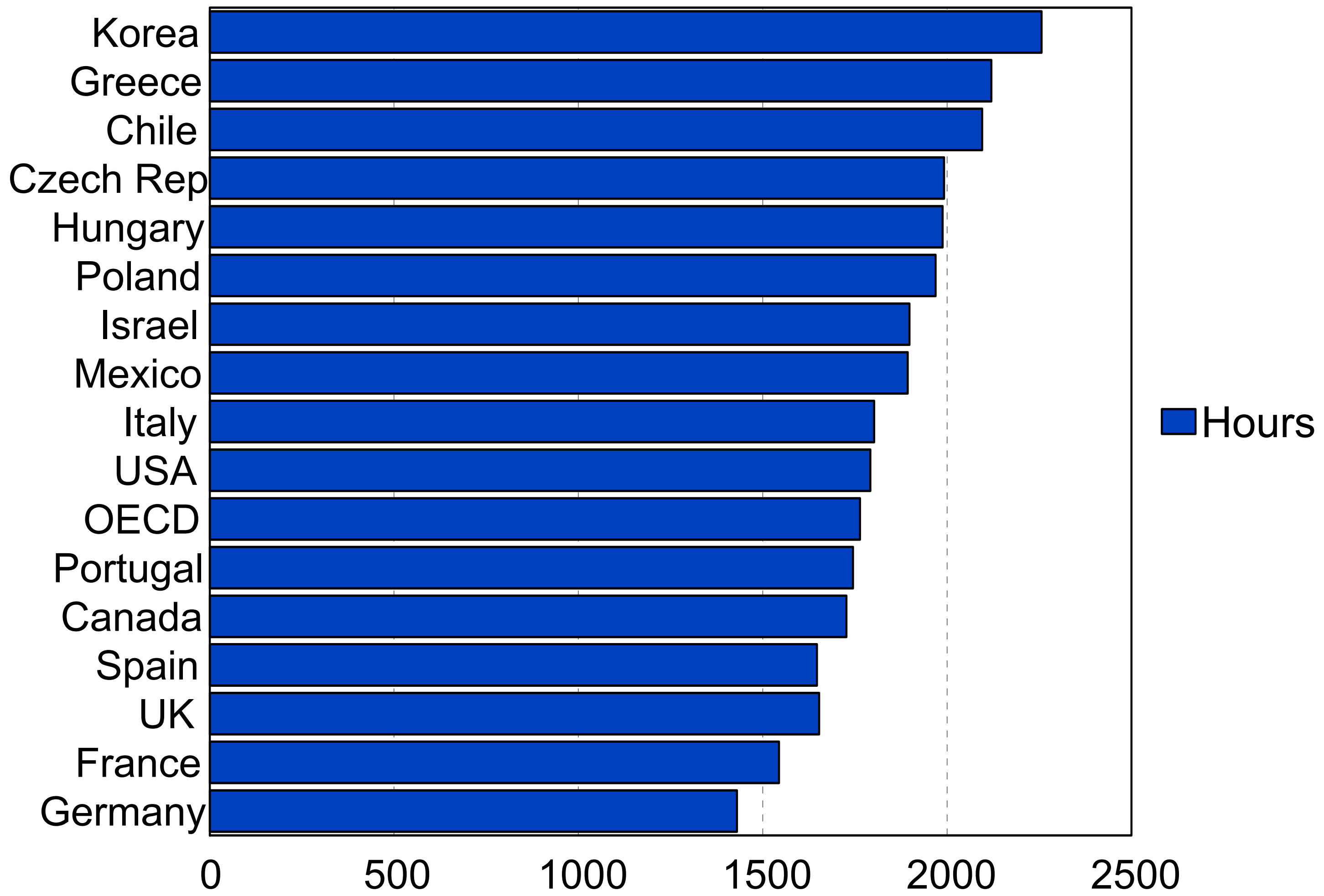
As a percentage of total employment, OECD

It is much harder to collect taxes when self-employment rates are so high



Average Hours Actually Worked, 2008, OECD

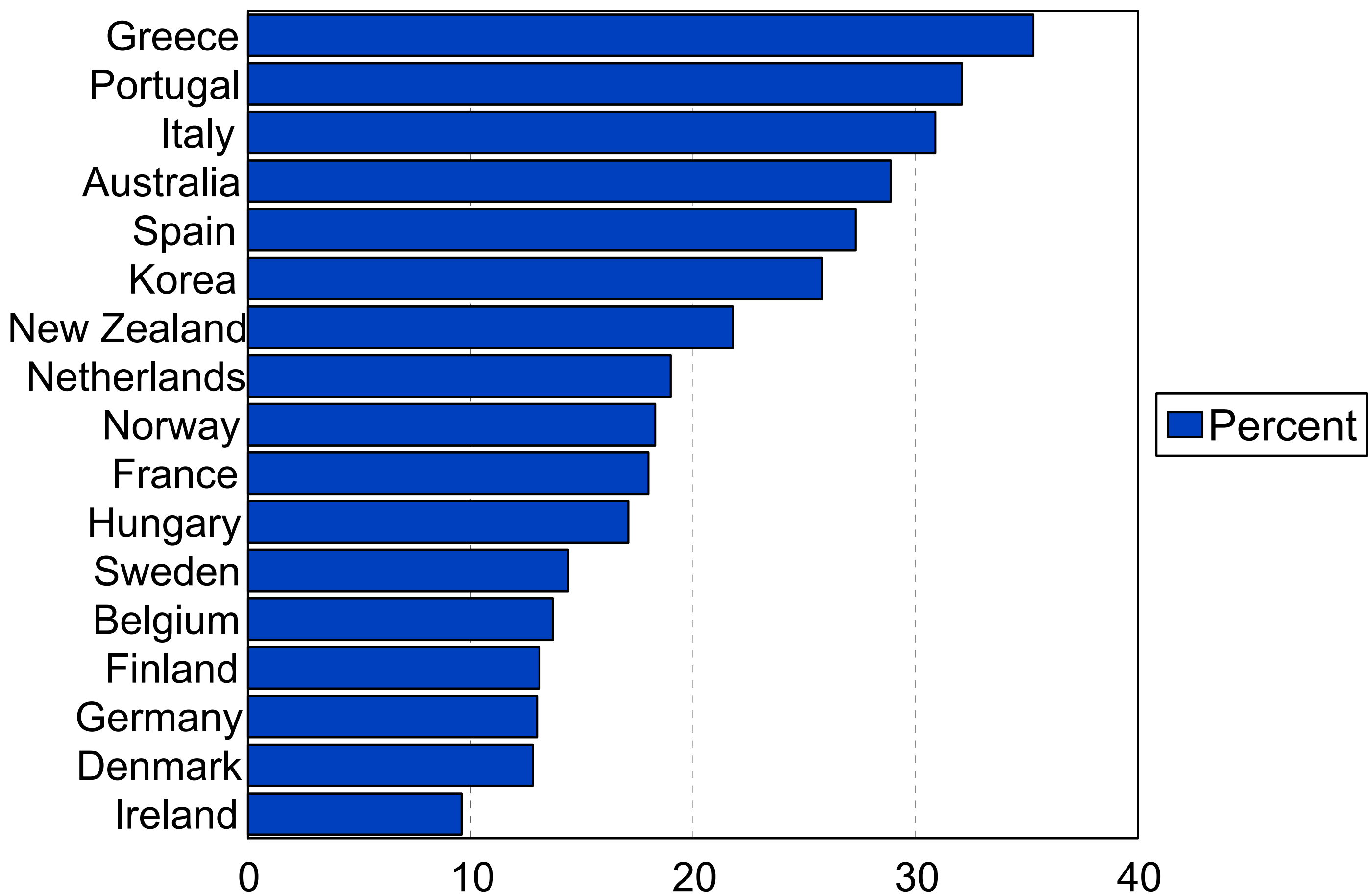
Greeks may work hard but need to become more productive



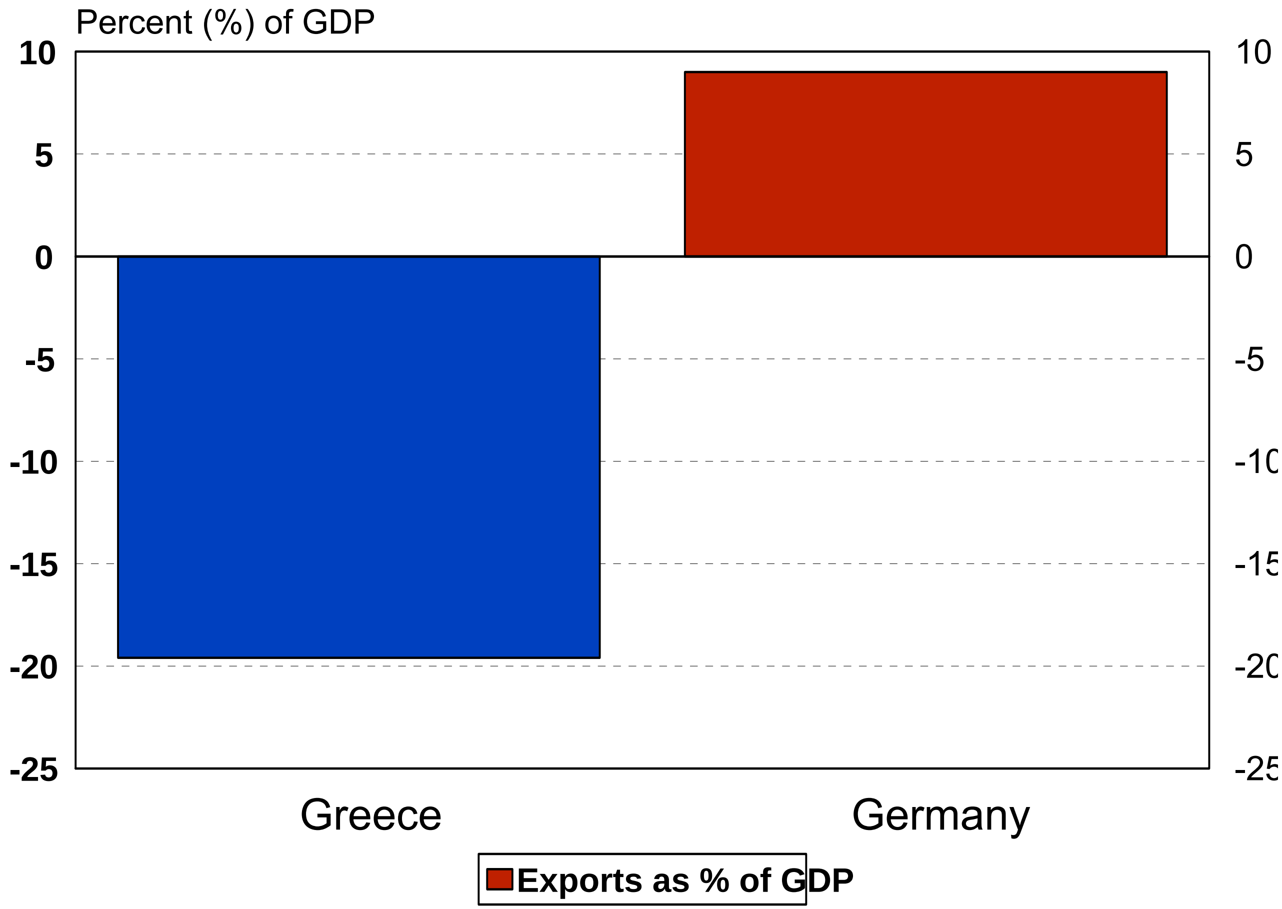
Structure of Manufacturing Sector, 2006

Number of Employees in Manufacturing in Enterprises With Less than 20 Employees

Percentage of total number in manufacturing

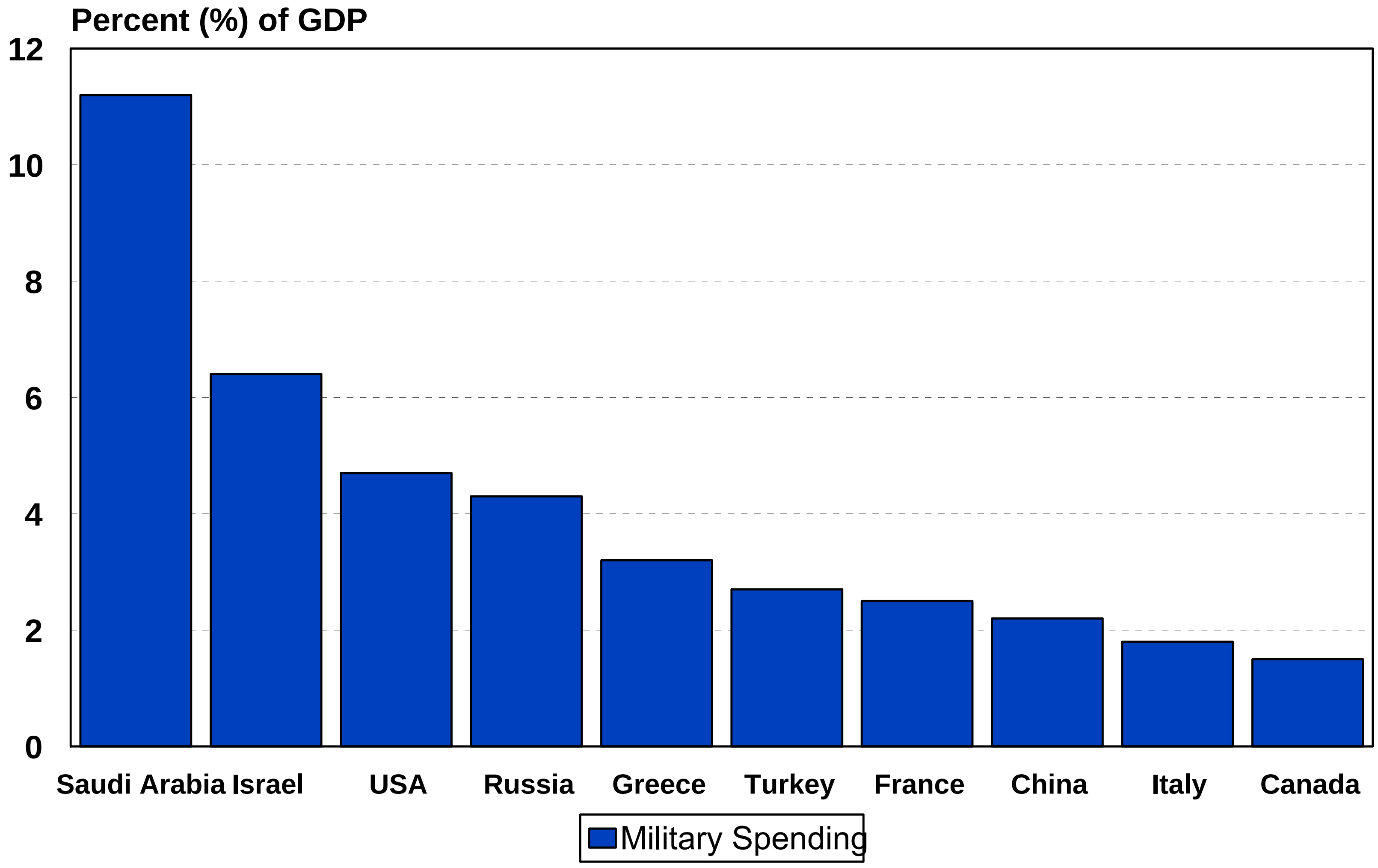


International Competitiveness Deficit, Greece vs Germany, 2008



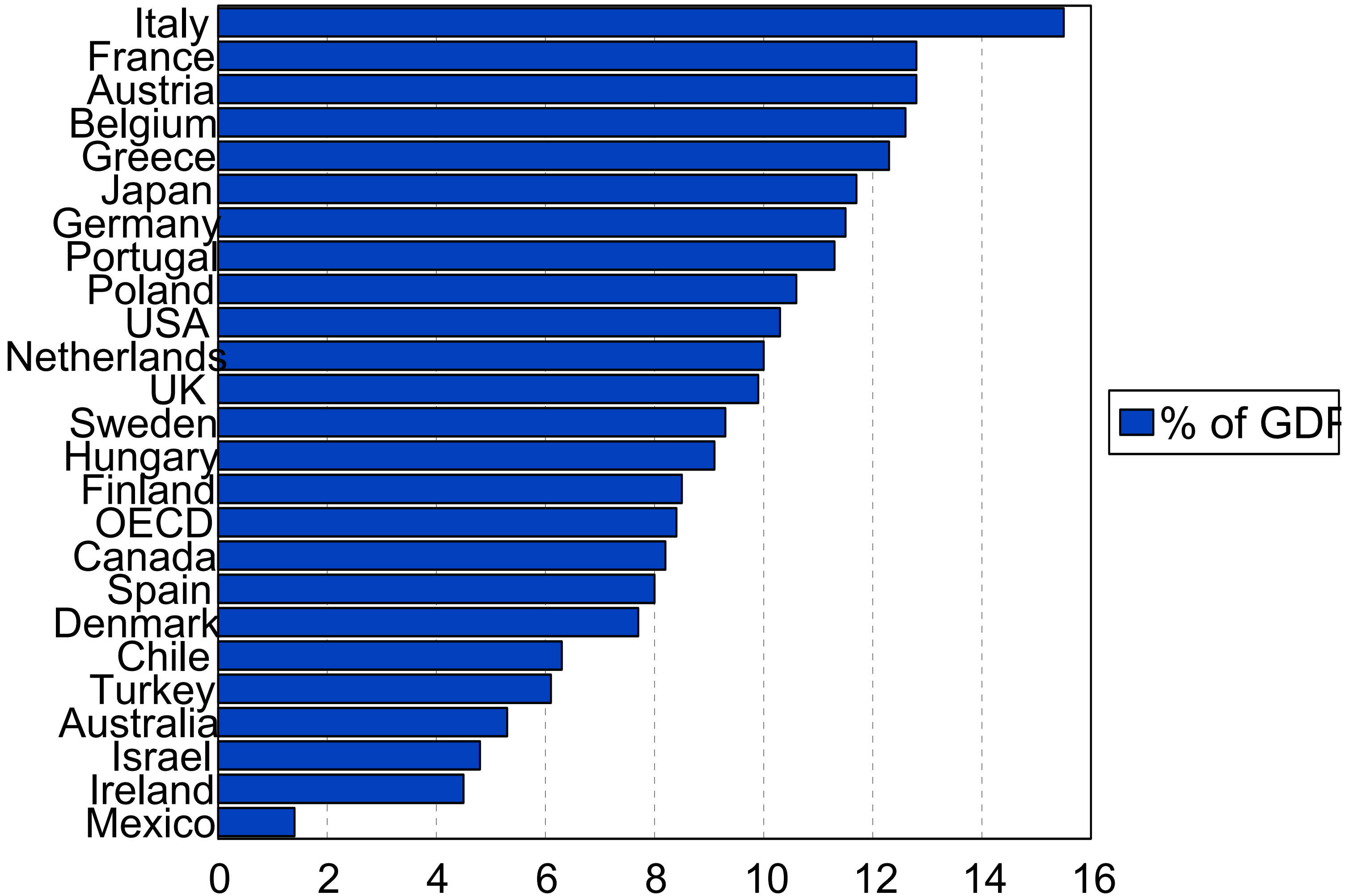
Military Spending as Percent of GDP, 2009

Greece is obliged to spend more on defence since it is situated in a dangerous neighbourhood



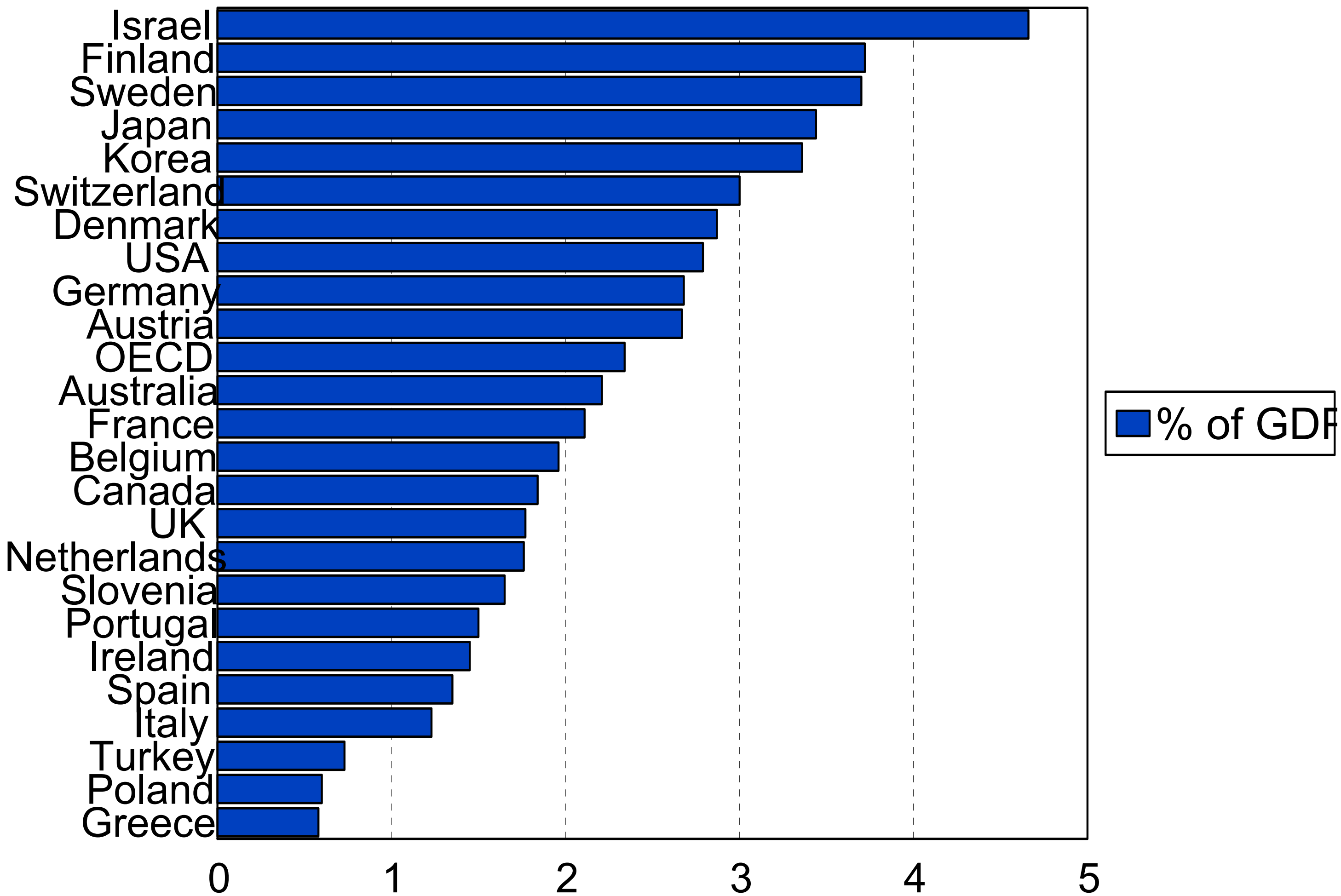
Public and Private Pension Benefit Spending, OECD, 2007

Greece is a champion when it comes to paying people for not working, i.e. pensions, but …



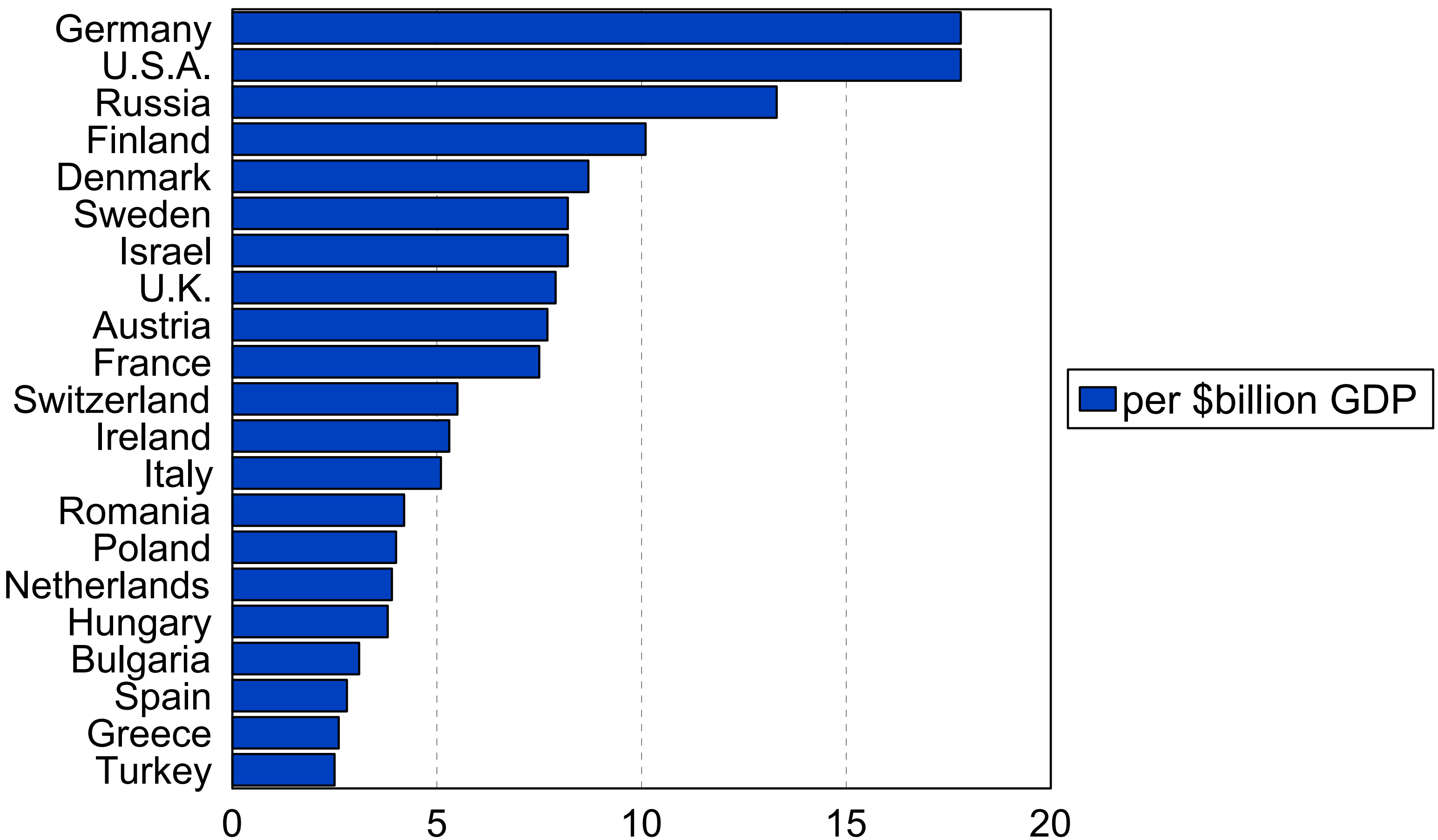
R&D Expenditures as a Percentage of GDP, OECD, 2008

When it comes to R&D it is in the bottom!



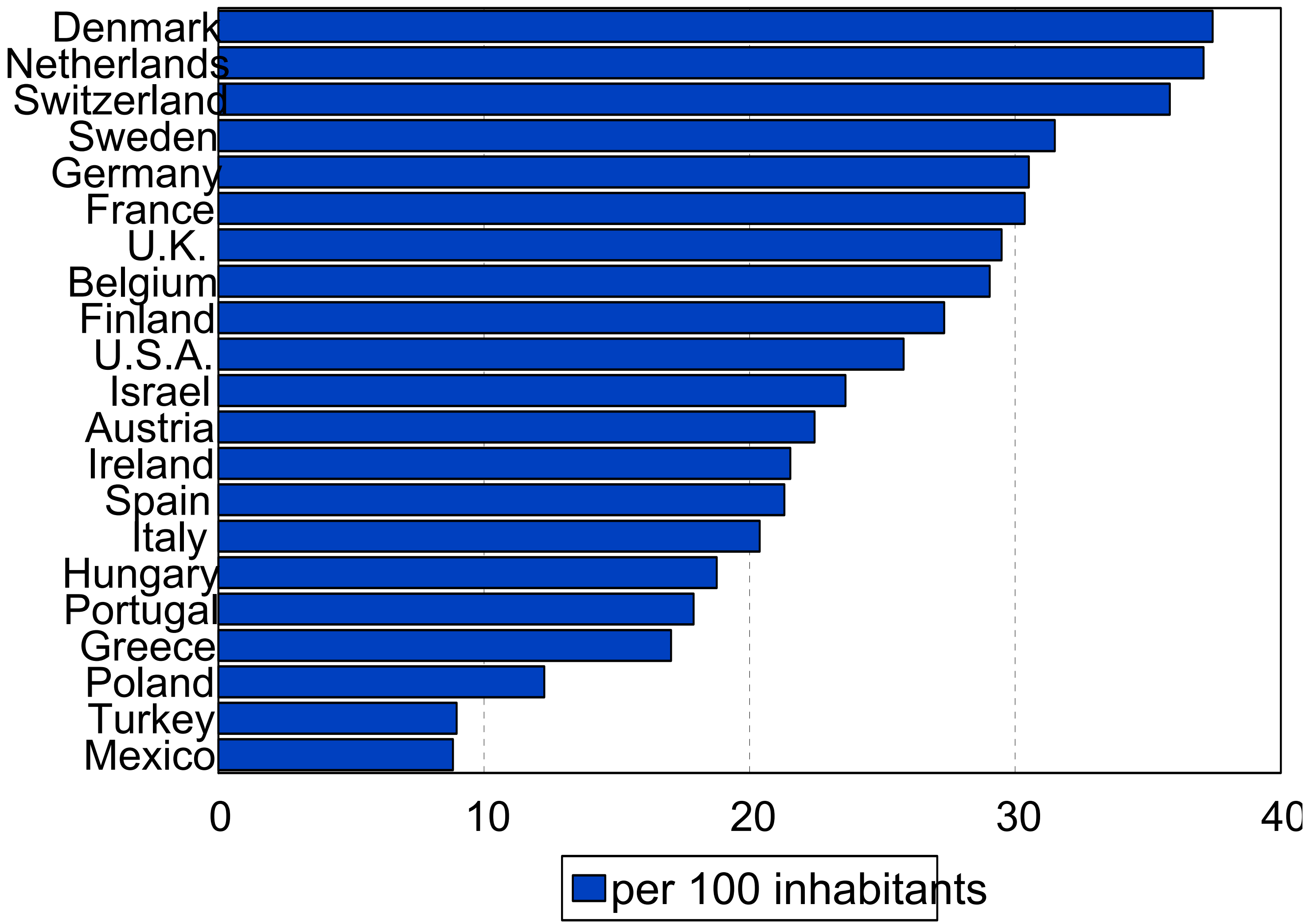
Resident Patent Applications per $billion GDP, 2008, WIPO

…and the same with intellectual creation



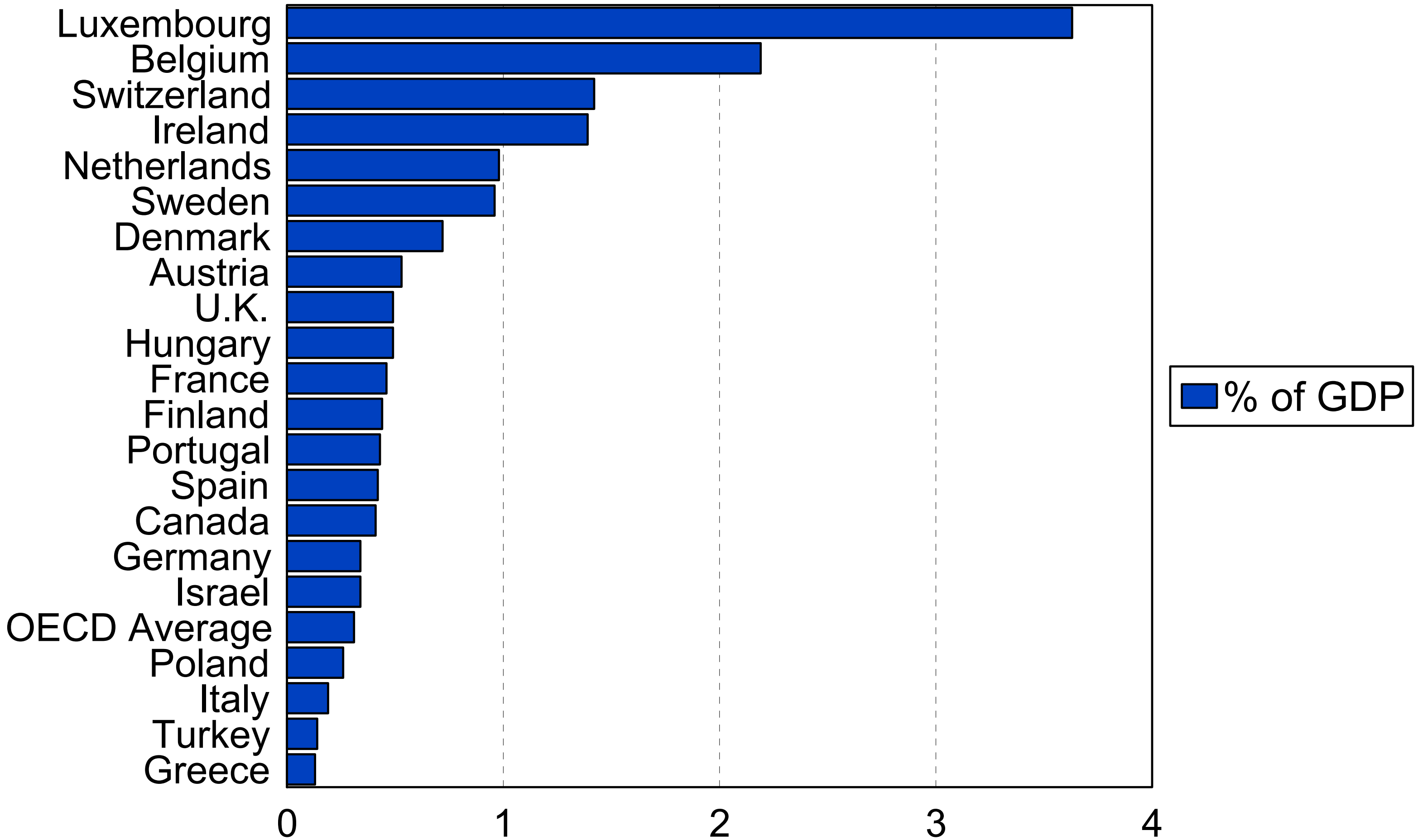
WIPO, World Intellectual property Indicators, 2010

Total Broadband Subscriptions, 2009, OECD

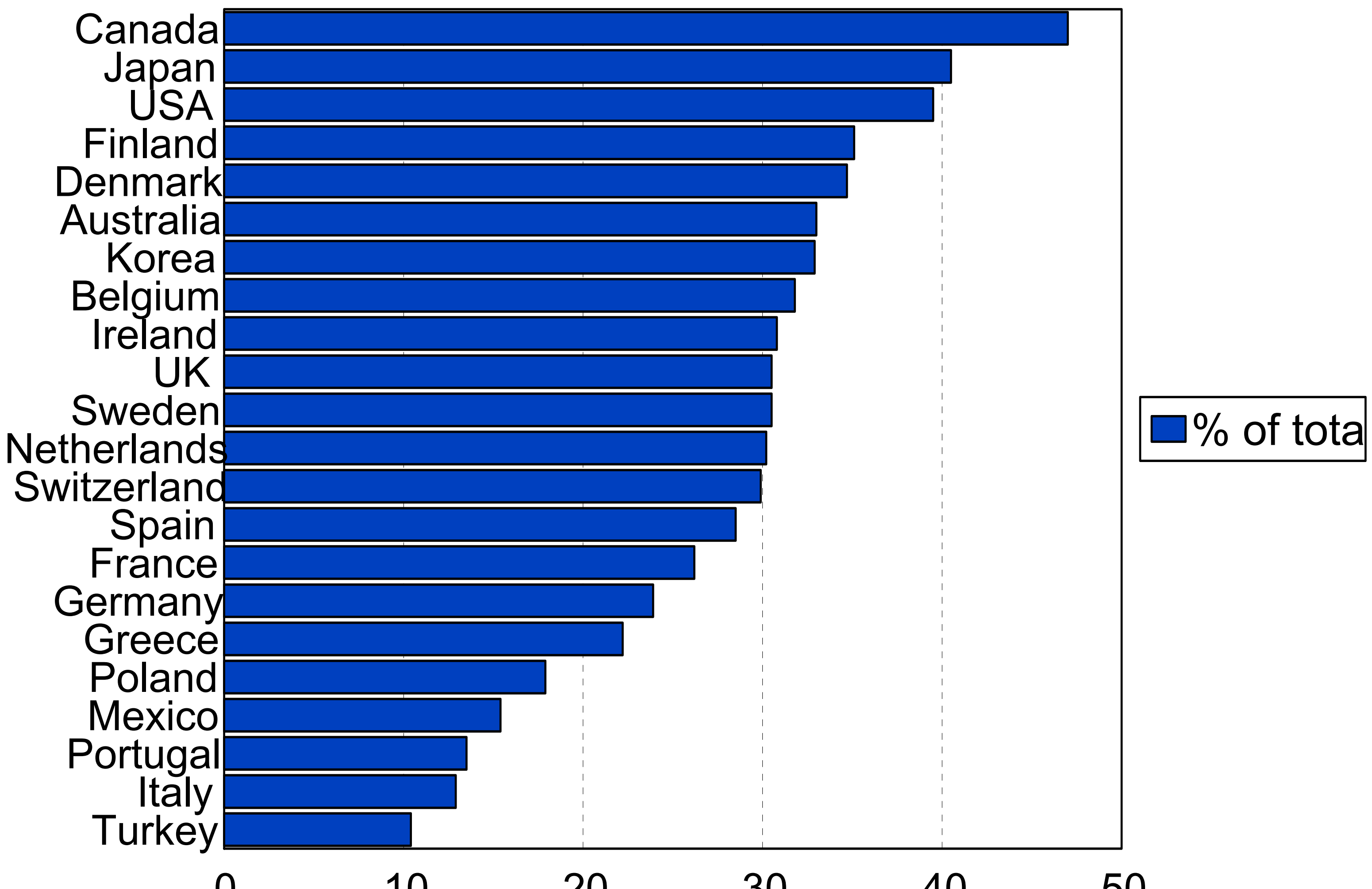


Cumulative Foreign Direct Investment as Percent of GDP, 2009

If Greece attracted the same share as Portugal it would result in an additional US$ 100 billion Investment in the country!
If it became the 'Greek Tiger' of SE Europe, $200 Billion!



Tertiary Level Educational Attainment for Age Group 25-64 (Percent of population of same age group), 2008, OECD



PISA 2009 Where Countries Rank in Mathematics, Science and Reading

- In the 2009 Test results, Greece ranked statistically significantly below the OECD average in all three areas
- Ranked 30th out of 34 OECD member countries in Mathematics
- Ranked 30th out of 34 OECD member countries in Science
- Ranked 22nd out of 34 OECD member countries in Reading

Greece's Problem is Political, It is the Oversized and Ineffectual Public Sector

- The structure of its economy and the public governance institutions cannot support generous social entitlements

- The problem is centered mainly in the public sector of the economy, in 2009 public spending accounted for **54% of GDP** whereas public revenues accounted for **38%**

- It needs to reduce the size of the public sector and make it more efficient, more accountable, more meritocratic and more effective

- It needs to liberalize markets and allow the private sector to regain the upper hand in managing the economy
- Structural reforms will allow for a more efficient use of limited resources that can contribute **15-20%** to country's GDP over a 5-10 year horizon

- Greece's problem is the public sector and the populist political environment that was installed since the 1980s, not its economy.

There are Limits to Big Government
'ΓΝΩΘΙ ΣΑΥΤΟΝ'

- With a productivity and international competitiveness deficit, Greece does not afford a large government sector
- Given the structure of its economy, Greece cannot succeed with very high taxes
- Government spending must shrink to below 40% of GDP
- Taxes should shrink towards 33% of GDP
- Given Greece's geopolitical position in a dangerous neighbourhood, Greece needs to spend less on social programs to ensure its national security
- Greece needs to allow the private business sector to lead, become more entrepreneurial, more innovative and more creative
- Greece needs to accept reality and recognize the limits of its abilities and proceed accordingly

Greece Needs to make Reform the Highest National Priority

- Greece needs to make economic and institutional reforms **urgently**
- Increase productivity
- Reduce unit labour costs and link them to productivity
- Liberalize labour market and make it more flexible
- Remove monopolistic privileges and barriers to competition
- Increase saving rate
- Increase capital investment spending
- Encourage innovation, entrepreneurship and R&D
- Enhance international competitiveness
- Make government more efficient, more effective, more accountable
- Make the distribution of taxes more equitable and restore sense of justice amongst citizens
- Make society more merit based
- Or else, Greece will **<u>not</u>** survive as we know it!

Greece Needs to Make the Right Choice

- The choice facing the Greek political leadership is simple, let’s not hide behind petty excuses
- Either it reduces dramatically the size of its government and cut deeply social entitlements, or
- Expand its economy while holding the size of government and social entitlements constant
- To expand its economy it needs to make drastic reforms and restructure its government apparatus, programs and policies to liberalize markets, empower the business sector, stimulate competition and increase competitiveness
- Reform and restructuring is the key to resolving Greece’s problem: reform stimulates economic growth, growth in GDP increases tax revenues and reduces budget deficits and reduces debt/GDP ratios
- In a bigger, more prosperous economy the relative size of the government sector and public debt shrink automatically
- Public sector jobs and social entitlements are safeguarded

‘Rich Greeks but Poor State’

- Greeks have been known for centuries for their entrepreneurial spirit, innovativeness, willingness to take risks and hard work
- Since the 1980s, this dynamic spirit of Greek people has been co-opted by the populist and self-serving ruling class and the energies of its people have been diverted away from wealth creation to ‘what can I get out of my state’ attitude, which in Greek is called ‘piatsiko’
- No state can survive when its citizens only take and don’t give
- Please note that I have not used the term ‘socialist’. It is not socialism that is necessarily the problem with Greece. Socialist states in other European countries have managed to create wealth and prosperity for their people and thus can afford their socialist programs
- It is the backward populist policies that Greek politicians have pursued under the guise of ‘socialism’ that only feed on ignorance and short-term opportunism. Socialism is a luxury that Greece cannot afford.

Restore Entrepreneurs to the Driver's Seat

- 'Enterprise', 'individual self-initiative', 'private sector' and 'profit' are words that are hated by the Greek labour movement, not to mention Greece's small but vocal Communist Party, and have been forgotten by the average Greek
- No nation's economy can thrive when economic decisions are made by workers and not by entrepreneurs, by politicians instead of scientists and professionals, when a powerful and privileged political ruling class make the most important economic and social policy decisions.
- Politicians are neither economists nor business people, nor professionals, they should know their place
- Unions have a role to play but they also need to be less politicised, less ideological and more pragmatic. There are powerful unions in Germany too, but they work with their bosses to achieve the common good for everyone, and in the long run the state survives and the people prosper.

Some Axioms to Remember and Follow

- The average Greek citizen must realize that they cannot expect the same social benefits from their government as their Northern European neighbours enjoy, unless they make Greece as productive and competitive as the economies of their Northern partners
- Money, does not grow on trees. For the government to spend it, it must either tax someone else or borrow it and tax everyone in the future
- They should not expect to have rich pensions, but have poor schools, poor productivity, poor justice or poor R&D
- Borrowing, unless it is done only for business or investment purposes, has never made anyone rich
- No business partnership has succeeded when one partner puts all the money and does all the work. The Euro Zone, is precisely such a partnership.
- They should learn to give more than they take, if everyone gave more we would all be better off because of it.

Can Greece Do It? Only If it Finds the Political Will to Proceed with Reforms and Change its Attitudes

- Even if Greece achieves 67% success in reforming its economy and institutions,
- The economy will recover quickly and future growth will surprise the sceptics
- The potential wealth creating effects of economic, social and political reforms are enormous for Greece
- The debt-GDP ratio will fall dramatically
- Living standards will start to rise
- Greece needs a new vision, a new strategy, a new economic growth model, and to restore Honour, Integrity, Thrift, Enterprise, Ingenuity and Justice to its daily lexicon.
- By 2021, Greece can emerge much stronger than it is today.

For further inquiries, contact the author:

Kenneth Matziorinis, BA, MA, Ph.D., CMC
Adjunct Professor of Economics,
McGill School of Continuing Studies
Professor of Economics,
Dept of History, Economics & Political Science,
John Abbott College
Senior Partner, Canbek Economic Consultants Inc.

E-mail: **ken.matziorinis@mcgill.ca**

www.canbekeconomics.com

www.hellascapital.com

Tel.: +01 514-884-6962