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GREECE IN THE TIME OF MEMORANDA

1. In 2001, when Greece joined the Economic and Monetary Union (EMU) and adopted the single currency, omens were good and expectations were great. At the time, it was thought that joining the hard core of European economies would act as a catalyst that would accelerate effective convergence with the advanced European countries on both the economic and the social level.

Unfortunately, these expectations did not materialise. In the years that followed, the economy grew, but not on the basis of a productive model that would ensure sustainable progress. Society demonstrated a clear preference for consumption instead of savings and investments, while strongly reacting to any attempts to change established structures. The political system paid excessive attention to the political cost and was reluctant to take decisive reform initiatives. The country enjoyed the benefits of the single currency, but did not try to respect the obligations that its adoption entailed.

2. In particular, economic growth has been fast, but it exclusively relied on domestic demand, fed by public and private borrowing. The productive basis did not adapt accordingly and competitiveness rapidly slackened, thus causing an increase of the trade deficit. Public expenditure increased, while revenues could not follow, thus creating large deficits and driving public debt to unprecedented high levels.

3. These problems had been repeatedly pointed out by the Bank of Greece, the European Commission, and international organisations. However, their warnings were not taken into account and the country continued in its course insouciant, borrowing to consume increasingly more products and services that it did not produce. When the global financial crisis hit in 2007-2008, the international environment underwent dramatic changes. Under the new prevailing conditions, countries with large structural imbalances suffered the most. In Greece, the international financial crisis soon evolved into a public debt crisis. Markets, re-evaluating credit risk in a manner including the likelihood of the country's default, imposed new and more onerous terms on borrowing, which gradually became prohibitive.

4. Already in 2008 it became apparent that, for the economy to survive, a multi-annual programme should be adopted to reduce public deficit, control the debt dynamics, and implement extensive structural reforms. In the beginning of 2010 it became clear that it was no longer possible to cover the deficit through financing from the markets.

5. It should be recalled at this point that the financial crisis evolved into a public debt crisis for some countries of the Eurozone, directly threatening the stability of the Economic and Monetary Union. Greece found itself at the heart of the crisis, being the weakest economy in the Eurozone, with large (government and current account) deficits, and serious structural problems. Since early May 2010 it had become clear that one country's problem had become an issue for the entire Eurozone. European leaders adopted important decisions to deal with the crisis and to prevent its recurrence, which represent the beginning of the most important attempt to reform the EMU since its establishment.

6. In April 2010, the Greek government applied to the Eurozone countries and to the IFM for financial support, and the following month the Memorandum of Economic and Financial Policies was signed. This launched a course of abrupt economic adjustment to prevent default and to lay the foundations for allowing the economy to return to a balanced state. This course has neither been straight forward nor painless. Besides, it was not certain from the beginning that the country could adjust in an orderly manner, while exit from the Eurozone has often been put forward as imminent and, at times, unavoidable. In addition, there have been critical fluctuations to the economic policy implemented, which oscillated between consistent implementation of the necessary measures and hesitancy – due to the political cost – culminating in mid-2011 and reappearing during the period of the dual election in mid-2012.

7. Furthermore, the initial agreements with Greece's partners were also significantly amended in order to deal with the consequences of the delays from time to time in implementing the programme, or to correct erroneous initial forecasts.

In the end, collapse and exit from the Eurozone, that appeared to be very likely, have been prevented through the continuous support on the part of Greece's partners and through the efforts of consecutive governments. Today, therefore, we can trust in a better future and expect that the economy will recover and, under certain conditions, enter into a new, virtuous, upward cycle.

The economic and social cost of adaptation has been considerable. The citizen's sacrifices have been particularly painful. Nevertheless, the problems of those past years and the losses in terms of production, employment, and revenue was the price that was paid to prevent the collapse of the economy, to which the wrong choices of the past were inevitably leading.

<u>Therefore:</u> Greece should have made and should continue to make every effort in order to remain in the Eurozone and avoid defaulting, something that would have immeasurable economic and social consequences.

• The Adjustment Programmes and the agreements with Greece's partners ensure financing of the Greek economy. Without them, defaulting would be inevitable. This is why they should be implemented in a resolute and consistent manner. Besides, the terms of the Programmes involve, to a very large extent, changes that should have been made many years ago.

• For the country to return to growth, safeguarding its European perspective, it should eliminate fiscal imbalances, improve competitiveness and foster an export-oriented economy, modernise the State administration, make the operation of markets competitive, and limit the burden of the public debt. Greece needs a new development model.

• Fiscal adjustment should rely, first and foremost, on reducing expenditure. Revenue should be reinforced by limiting tax evasion and extending the tax base, so as to make subsequently possible the necessary reduction of tax rates.

• Implementing audacious structural reforms will limit the amplitude of the recession and then support and accelerate the course to recovery.

• The historical challenge facing the country requires the broadest possible coalescence of political and social powers, national understanding, and convergence.

• Adjustment programmes are a necessary condition for exiting the crisis, but not a sufficient one. The economy's drastic reorientation towards a new model requires an integrated National Plan for development, having long-term targets, which will be consistently implemented.

8. The most significant among the developments in the period from 2011 to 2016 have probably been the great recession of the economic activity, much larger than initially anticipated, and the **outbreak of unemployment**.

The great recession was mostly due to the contraction of domestic demand. However, it would appear that the uncertainty regarding the outcome of the stabilisation exercise also had a considerable impact on the great recession. Uncertainty arose to a large extent from the manner in which stabilisation was pursued, at least during the second year of implementation of the initial programme. Instead of moving forward with the front-loaded policy that had been decided, a hesitant approach was opted for, hoping that part of the adjustment cost could in the end be prevented or, in the worst case, be paid later. Deferrals and delays constantly led to revisions of the agreements with Greece's partners and to new measures, resulting, on the one hand, in the adjustment cost being much higher than it would have been had the measures been adopted timely and, on the other hand, in the manifestation of the expected positive effects to be postponed until later in the future. This consolidated a perception that the adjustment programme had failed and that what was occurring was the adoption of a series of painful measures, without any visible effect. This has had serious consequences:

• It reinforced expectations that the future would be increasingly bleaker, which led to systematically postponing consumer and, especially, investment decisions. This in turn has led to a greater recession than the one that would have been justified by the tight policy, a fact which undermined fiscal adjustment and further worsened the vicious cycle.

• It undermined the credibility of the support agreement which was viewed in a negative manner and was considered by a large part of the public to be the main cause of all evil. The actual reasons that led to the crisis have been obscured.

• It intensified social unrest for a long period of time, the public discourse continuously revolving around the cost of the measures at issue, the implementation thereof being constantly postponed.

• It unsettled government cohesion and undermined political stability. The risk of such effects had been pointed out from the outset by the Bank of Greece.

All the above have broadened the loss of trust and, during negotiations with its partners, Greece was constantly required to furnish stronger assurances that it would implement the terms agreed upon. The loss of trust originated from the appreciation that political will for implementing the programme had weakened, since the necessary minimum basis of consent among political forces to implement the changes Greece had committed itself to implement could not be achieved. This appreciation led to mistrust in the country's ability to ensure continuity of the implementation of the programme and fed into all kinds of speculation and predictions about possible scenarios.

9. The European Union has been studying the crisis experience and has been looking for new governance orientations, which will define a new operational framework for the EMU and the economies of the Member States, a new institutional architecture. For Member States in the Eurozone, the emerging environment requires greater consistency regarding compliance with fiscal obligations and the establishment of new rules for economic policy, aside from fiscal policy.

The crisis appears to be leading the EU and the Eurozone into a new path, its main pursuit being convergence of the Member States' economic policy. This entails long-term commitments to achieve fiscal balance, improve competitiveness, and harmonise the rules of operation of markets and the banking system.

The crisis has resulted not only in adopting longer-term goals for the structural changes but also in a basic choice: the financial support for countries faced with problems. This choice has not been easy or self-evident. This is why it was met with severe resistance. However, it has prevailed in the end, because it was based on European criteria – i.e. the appreciation that the default of any Member State would have very serious side effects for the entire Eurozone.

10. Lastly, the book of Giorgos Papakonstantinou, former Minister of Finance in the Giorgos Papandreou government, entitled "GAME OVER", allows us to draw some important conclusions: first, the causes of a state's default are almost always internal. Second, the European path for the bail-out may not be the best option, but it is the best possible option. Third, it has been confirmed once more that the EU advances only through the crises it faces, but it does advance and does not

disintegrate. Fourth, in difficult times, Greece was supported by the responsible stance of supposedly “evil” bankers, such as M. Draghi and G. Stournaras.

11. If Europe has changed since the onset of the crisis, Greece has been literally transformed. When the crisis hit, the country was living beyond its means and was suffocating under its weak institutions and a sick political system. In 2010, Greece managed to avoid the “sudden death” of default and the devastation it would bring, particularly for the most vulnerable groups in Greek society. It entered into an unprecedented adaptation process and has undergone during all this time a transformation on many levels, albeit at a great cost for its citizens.

This was a necessary transformation and this is why it has had results; even if this is hard to admit, few things would have occurred in Greece, had it not been for the “damned” Memorandum. Its elaboration may have been problematic and its implementation has often been below what was necessary or desirable – but it was the first time that the country has had a business plan, with deliverables and deadlines, as well as sanctions. However, the fact that all this included coercion is the reason why it has not actually changed the country in depth. If one does not believe in change, change will remain superficial.