

The Political Origins of the Greek Crisis: Domestic Failures and the EU Factor

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ABSTRACT

This article argues that the origins of the Greek malaise are primarily political rather than economic and rooted in the delay, postponement, and half-hearted implementation of public policy reforms that preceded the crisis. The 2007-08 global economic crisis triggered market scrutiny over Greece, as it brought to an end a period of abundant liquidity and a relaxed attitude by global markets *vis a vis* Eurozone members. Greece's impossible fiscal position was brutally exposed, and a downward spiral began. The article also argues that although Greece set itself up for failure, the Eurozone's inability to act swiftly and early, to diagnose the problem correctly and to combine a policy mix consisting of budgetary consolidation *and* policy reform further exacerbated the problem. Despite the fact that disorderly default has been avoided and a sense of normalcy has returned, Greece has to move swiftly on the reforms front to avoid disaster.

The 2008 financial crisis led to a rapid downturn of global output. The collapse of Lehman Brothers set in motion dormant forces in the lightly regulated financial sector and led to a series of bank mergers, nationalizations and takeovers in the US, the UK and elsewhere. The failure of subprime mortgages was followed by pressure on the official banking sector, and governments felt compelled to intervene so as to rescue the banking system from a dangerous and unpredictable collapse. For a while, the neoliberal orthodoxy of the preceding 30 years came under fire. This time, it was not only die-hard socialists who fired at the banks and their profit-motivated "greed." As the crisis moved further into the real economy, civil society took up the case of income inequality and launched the "99 percent" campaign, highlighting how the economic spoils of the present economic

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system are distributed so unevenly as to threaten the stability and reproduction of the capitalist system.

In no other country have the last few years been more traumatic and at the same time more revealing than in Greece. An EU member since 1981 and one of the world's thirty richest countries until recently, the Hellenic Republic has hit the world's headlines in an unprecedented manner. The main reason is the fact that Greece became the weakest link in the Eurozone chain, with both debt and deficit levels at record highs and a record of fiscal imprudence that makes it susceptible to collapse. That would have been of little importance to the world's media and markets had Greece not been a Eurozone member; the fact that it does makes its possible default an event of severe consequences for the Eurozone as a whole, and thus for the global economy.

In May 2010 and after it had become obvious that the country would be unable to keep on borrowing in the open markets on punitive interest rates, Greece received a €130 billion rescue package from the IMF and the EU. The goal was to bring down public debt levels and consolidate public finances. The program's failure became apparent by late 2011 and a new agreement for a second loan worth €110 billion was reached in February 2012. By early March, a bond swap deal between Greece and its creditors was successfully concluded, wiping out more than €100 billion of Greek debt.¹ Meanwhile, the country's social, political and economic system came under severe pressure as EU-IMF conditionality imposed drastic cuts on public expenditure, tax rises and flexible labor laws to facilitate 'fire-and-hire' policies, all in the name of enhancing the country's competitiveness.

In this paper I will advance two main arguments: first, the origins of the Greek crisis are primarily political rather than economic and rooted in the delay, postponement and half-hearted implementation of public policy reforms that preceded the crisis. Second, although Greece set itself up for failure, its downward spiral was exacerbated by the Eurozone's inadequacy to act swiftly and early, to diagnose the problem correctly and to combine a policy mix consisting of budgetary consolidation *and* policy reform led to a disastrous situation by early 2012. Following the successful bond swap deal and signs that the EU is now willing to combine fiscal consolidation with pro-growth policies, the next few months will be crucial in determining whether the Greek economy will be able to recover, however modestly, in the next few years.

In what follows, I will first describe the Greek malaise by use of basic data and some facts so as to place the subsequent analysis into context. I will then outline the root causes of why past reform failures have now come to bear their bitter fruit on the Greek population. To illustrate the argument I will use the case of successive failures to reform the pension system, as this policy area is broadly

representative of the problem. In the next section, I will link the Greek malaise to the EU handling of the crisis since 2009, and the conclusion will summarize the main arguments.

The Greek Crisis: Some Data and Figures

Greece is not the only country suffering from high debt levels, it is not the only country with high public deficit and it is not the only country whose economy is contracting.² Yet it is the *only* country in which both debt and deficit are at record highs, and whose GDP is contracting at record levels.

To start with, Greece is now going through its 5th consecutive year in recession and its GDP has shrunk by 13 percent since 2008. The consequences of such a dramatic fall in output are stark. Unemployment is now hovering around 22 percent and is above 50 percent for the young.³ Salary cuts for public and private sector workers alike are estimated between 10-30 percent, excluding the effects of punitive taxation and tax rises imposed on VAT rates (now at 23 percent for most goods and services). Pensions have been cut by 12 percent in 2011 and larger cuts are planned for 2012 and the years to come.⁴ Meanwhile, excise duties and special levies on firms, individuals and real estate have been imposed a number of times over the last three years on an *ad hoc* basis, with no obvious financial result for state coffers.

These measures had some positive effect on some macroeconomic indicators. The country has managed to reduce its current account deficit from 14.9 percent of GDP in 2008 to 9.8 percent in 2011.⁵ The European Commission suggests that the country has recovered around half of the competitiveness lost in 2009-2011, not least through the reduction in labor costs.⁶ Note, however, that this success was almost entirely due to wage reductions and not any systematic effort to reduce the non-wage element in labor costs. Finally, the country's export rate has risen since 2010 and "closed professions" are now liberalized *en masse*, a measure which in theory will offer new employment opportunities and by enhancing a more level-foot competition will bring down prices.⁷

Nevertheless, the country's debt ratio to GDP has been rising since the crisis began, and moved from 116 percent in 2009 to more than 150 percent by 2012. The constantly rising debt level totaled more than €360 billion and had become unsustainable. In March 2012, the Greek government successfully negotiated a debt write-down worth €105 billion, a total of 53 percent reduction of its debt to private creditors. This came as part of a package deal that also included the second €110 billion bailout, the creation of a special account to deposit debt repayments, and an austerity package that alongside privatizations and tax rises foresees cuts in pensions, civil service salaries and bonuses, minimum wages, and tax-free

thresholds. The goal is to reduce Greece's debt-to-GDP ratio to 120 percent by 2020,⁸ a level which itself is not necessarily sustainable in the long run.

Greece's Political Economy: Avoiding Change

The Broad Context

Will the second bailout package work? The fact that the transitory coalition government formed in late 2011 and headed by former ECB Vice-President Papademos managed to successfully conclude both the debt write-down deal and tough negotiations over a second bailout plan inspires some confidence. Yet successive failures by the country's political elites to address the root causes of the crisis in the past mean that Greece's future remains uncertain.

Severe crises have knocked on Greece's door in the very recent past, but were averted due to a combination of low interest rates, especially after the country's entry in the Eurozone in 2001, liquidity-rich and fairly benign international markets and the belief that the Maastricht Criteria of 1992 would lead to economic convergence across the Eurozone. When the tide turned in 2008 and a lack of political leadership in Europe exposed individual member-states' weaknesses, Greece could no longer avoid being singled out as a problematic case. Long-delayed reforms would now have to be introduced from outside, would not be subject to social dialogue or negotiation, and would have to be introduced immediately to reassure markets that the Eurozone remained in control and would not break up. In other words, change that should have occurred gradually over the last 30 years, in an equitable and preferably progressive manner was continuously blocked, delayed or not implemented. Examples include broadening the tax base, tackling sky-high tax evasion and simplifying bureaucracy to enable law implementation and efficient service delivery. A brief discussion of the evolution of Greece's post-war political economy will help illustrate the point better.

Greek post-war policy was primarily oriented towards rapid economic development whilst seeking monetary stability. The 1953 currency devaluation and trade liberalization amidst a relatively stable international economic environment were very helpful.⁹ The Greek economy grew on average by 6.5 percent between 1950-1961, while growth during the period 1961-1979 was even more impressive, 7.4 percent.¹⁰

However, this period is also the one in which high rates of economic growth were for the first time accompanied by structural economic problems. First, inflation averaged 16 percent between the two oil crises in the 1970s, thus offsetting growth rates. Secondly, worsening balance of payments difficulties resulted from the slowing down of foreign currency inflows. Thirdly, the commitment to monetary and fiscal stability that had underpinned the Greek post-war eco-

conomic paradigm¹¹ came to an end in the immediate post-dictatorship (post-1974) period, as democratic transition made expansionism the preferred pathway to legitimize the new regime. The politics of expansionism was enthusiastically adopted by the centre-right New Democracy (ND) governments of the 1970s (1974-1981), accompanied by nationalizations of select industries.

The 1980s is the defining decade of modern Greece. The civilianization of the regime and democratic consolidation¹² went hand in hand with rising aspirations by the middle classes that emerged following the economic upturn of the 1950s and 1960s. On the political level, new actors made a powerful entry through the 1981 electoral victory of the Socialist Party (PASOK). The latter's call for politics to benefit the "non-privileged" resonated strongly with the vast strata of self-employed craftsmen, tradesmen, agricultural laborers and low- and middle-ranking state officials.¹³ However, the economy entered a period of high inflation and low growth. Loss of competitiveness in the international market was accompanied by the emergence of "ailing industries" bailed out by the state for electoral purposes. While the EU sought to encourage liberalization reforms in line with its professed plans for a Single Market, the government avoided electorally painful economic restructuring.

To avert disaster, the second PASOK government elected in 1985 briefly experimented with a program of fiscal consolidation to control a ballooning public deficit and rising debt. The consolidation program lasted for only two years and was reversed the moment its unpopularity became obvious to the party's leading echelons. Their re-election at stake, they opted for more expansionism, i.e. for more public sector expenditure with (in essence) borrowed money. Since EU membership guaranteed financial support and contributed to rising living standards, deficit-financed social policy continued unabated. Meanwhile deindustrialization continued and an inefficient services sector grew instead.

Greece met with political instability in the late 1980s amidst corruption allegations and successive electoral contests produced short-lived coalition governments. The European Community warned the country that its deteriorating economic situation worried Europe, and that measures had to be adopted quickly to avert economic catastrophe. It was argued that the Economic and Monetary Union (EMU) project could be derailed if Greece's economic performance did not improve.¹⁴ In 1990, Greece had an inflation rate of 20.4 percent, a public deficit of 15.9 percent and an unemployment rate on the increase standing at 7 percent.¹⁵ At the same time, interest payments by the end of the 1980s had quadrupled compared to 1981.

The seeds for future destruction were sown. By the 2000s, Greece was producing little, and even less of its produce was internationally competitive. Its product, service and labor markets were ossified and its entrepreneurial spirit

hidden underneath a large, bureaucratic monster fed by successive center-right and center-left governments. It taxed labor income at punitive rates, while its labor productivity was in decline. It had failed to invest in education and R&D, thus artificially maintaining healthy growth rates through a construction boom fuelled by the 2004 Olympic Games.

Data confirms this. The country ranked 78th in Transparency International's 2010 annual report,¹⁶ squeezed between Colombia and Lesotho.¹⁷ Moreover, it ranked 100th for 2012 in the *Doing Business Data* released by the World Bank Group. Note that the average rank of states in the same group as Greece ("OECD High Income") was 29.¹⁸

Perhaps more importantly of all, its civil service lacked the digitalization, organization and infrastructure to deliver adequate and efficient services to its citizens. To illustrate, state authorities had to conduct a survey to find out the exact number of civil servants gainfully employed only after the Memorandum of Understanding was signed between the Greek state, the EU and the IMF in 2010.¹⁹ This revealed stark discrepancies in civil servants' salaries, most of who were completely arbitrary and did not reflect objective qualifications, such as the employee's education level, IT skills, and so on. When the EU/IMF-Greece Memorandum was signed in the spring of 2010, the European Commission set up a Task Force for Greece. The EU argued that its establishment was a 'strong gesture of solidarity' with Greece.²⁰ That is only part of the story, however. The formation of the Task Force, whose primary purpose is to offer technical assistance to the Greek authorities so as to boost the country's ability to benefit from EU funds and accelerate the pace of administrative reform, is also an institutional framework underscoring EU pressure to introduce reforms that have been postponed or cancelled for decades.

A meritocratic public service ethos was never developed, and party political favoritism grew enormously over successive governments, meaning that top officials were replaced whenever elections led to a change of government.²¹ In some cases, a change of guard would occur with a reshuffling, as Ministers would seek to work with their "own." The result was a dispirited body of civil servants, occasionally marred in corruption and never properly assessed in terms of its service delivery.

The democratic achievements of the post-1974 era, such as the democratization of the trade unions and the restoration of their legitimate rights and freedoms, lost their original meaning through time. Instead they became a symbolic point of resistance to all kinds of reform, from serious to hasty, from sensible to unjust. The positive changes that were introduced in labor relations over the 1980s and 1990s did not lead to some form of Europeanization of social dialogue and negotiated solutions to policy problems.²² Instead, trade unions became an

obstacle even to progressive reforms and declined invitations by governments, particularly in the late 1990s and early 2000s, to find coordinated answers to labor market problems.

The Greek trade unions have for long perceived reform along the lines of the “insider-outsider” dichotomy they have helped to sustain, and refused to undertake responsibility for employees outside their core clientele, such as private sector employees (unions speak almost exclusively in the name of civil servants) women, immigrants, and part-timers. Their approach has offered a perfect alibi to a political class addicted to a patron-client relationship with the electorate and a reluctance to move ahead with bold change. Often, unionized employees in public utility corporations (DEKO), in alliance with party apparatchiks in the public sector secured extraordinary privileges for themselves in complete disregard for the average employee, and by use of their party connections at the highest echelons of the state. There was the odd attempt to remove some of their privileges but it was countered by the trade unions’ leadership ability to mobilize few but highly influential supporters within the two major parties.²³

This is not to suggest that political parties or the business world were innocent bystanders: the desire to avoid political cost characterized the former and a timid approach complicated by entrepreneurs’ close and often murky relations to the state characterized the latter. The end result was a *société bloquée*,²⁴ where sensible policy solutions were rejected until the crisis hit home.

Reform Failure: The Pension System

To illustrate the source of the country’s inability to change I will use the representative case study of the pension system. This is a policy area whose challenges (demographics, workers/pensioners ratio, and new patterns of employment and social security contributions) are common to all advanced economies, and the need for reform dates back to at least the 1990s. Furthermore, the Greek pension system is characterized by gross inequities in coverage and benefits, an incoherent decision-making structure, fragmentation and weak budget constraints.²⁵

The ND government that came to power in 1990 promised to reform the pension system that was responsible for half the cost of public deficit and absorbed 15 percent of the country’s GDP.²⁶ Pressure from the EU played into the hands of leading government functionaries and could act as a source of empowerment in an attempt to entrench a new political economy agenda. In fact, the establishment of the Maastricht criteria led to a broad consensus on the need for EMU entry. Yet the ND government failed to introduce radical reform, save for a few changes in the retirement age to push the can further down the road. The structural deficiencies of the Greek pension system were not addressed²⁷ and the changes introduced in the pension system in 1993 amounted to little more



Photo: REUTERS, Yorgos Karahalas

A poster depicting German Chancellor Merkel and the IMF head Lagarde hangs in front of the Greek parliament during an anti-austerity demonstration in Athens' Syntagma square.

than cosmetic modifications. Instead, the government appeased the trade unions by watering down its changes and passed the buck to its successor to avoid the political cost associated with radical change.

The re-election of PASOK in 1996 under a new Prime Minister, Kostas Simiitis, meant that “modernization” became synonymous with the need to Europeanize (i.e. reorganize, rationalize, and improve according to west European standards) various facets of public life. During that eight-year period some progress was achieved in containing rising debt and deficit levels, and growing prosperity combined with sensible management of the economy offered the illusion of long-term prosperity. Yet the issue of substantial policy reform never went away, as the few attempts made to radically alter the country’s stifled political economy failed to bear fruit.

Although the government received expert advice on the need for reform, no change was introduced during the 1996-2000 legislative period. Stagnation was no longer an option following PASOK’s narrow re-election in 2000. Its manifesto called for social security reform, and concurred with the Bank of Greece’s warnings of a pension “ticking bomb” threatening to derail the country’s finances and undermine its ability to compete effectively in the context of the Economic and Monetary Union (EMU). In 2001, the government came up with a policy package that tried to deal with some of the pension system’s more structural problems and, more importantly, tried to redress some of its

gross inequities. The Trade Union Confederation (GSEE) immediately attacked the proposals and strikes began. Opinion polls took a turn for the worse, while the responsible Labor Minister Giannitsis²⁸ could count on no support from his colleagues. The minister himself sought to defend his proposals by appealing to rationalist arguments but to no avail; he was removed soon after the proposals were dropped.²⁹ The law that was passed once Giannitsis had seen the door was a significantly “softer” version of the original proposals. Massive resistance to change had been manifested yet again and comprised an unusual alliance of party traditionalists, trade unions and the highly populist and influential media.

In the spring of 2008, the ND government unveiled plans to reform the social security system following its chronic failure. The most significant changes included increasing the retirement age, reducing “supplementary” pensions to a maximum of 20 percent of basic pension, abolishing early pensions schemes for mothers of children under 18 and those employed in public enterprises and banks, offering financial incentives for retirement after 60 and merging social insurance funds from 133 to 13.³⁰ The social dialogue attempted by the government prior to the reform failed to engage the trade unions, as the GSEE accused the government of ignoring the financial side of the problem and declined to participate.³¹

From the description above it becomes obvious that one of the fundamental reasons for policy failure that led to a deep crisis was the vulnerability of Greek governments to the granting of exemptions to privileged groups. These groups follow the rhetoric of trade unionism and “workers’ resistance to injustice,” while their practice points to an inner-circle group of privileged functionaries with direct links to both major political parties and the capacity to block much-needed change in the country’s pension system.

From Crisis to Tragedy: Slow Responses and Wrong Priorities

How is it that the Eurozone and its political handlings also share part of the Greek tragedy? After all, the financial generosity of Greece’s partners cannot be doubted, at least with regard to its volume. Greece is benefiting from a financial aid facility and credit line that totals €450 billion: €240 take the form of direct loans to the state, €107 billion is worth the haircut deal agreed in March 2012, and Greek banks have benefited from €100 billion worth of ECB credit. Additionally, the EU has set up credit and rescue mechanisms in the form of the European Financial Stability Facility (EFSF) and its successor, the European Financial Stability Mechanism (EFSM), both of which have been used to assist the Greek state.

Yet there are a few fundamental issues at fault in the EU response to the crisis and they ought to be part of the attempt to explain what has gone wrong

thus far, specifically in Greece and more generally at the EU level. These could be summarized as timing, policy choice and policy content.

Timing

A new PASOK government was elected in Greece in October 2009. A month later, it announced that the budget deficit for that year would be 12.7 percent, a staggering nine percentage points higher than the previous estimate of 3.7 percent. The market reaction was swift and severe, with Greece being downgraded by all major credit rating agencies and eventually reaching “junk” status. Banks and other financial institutions started dumping Greek bonds *en masse* and turbulence in the Eurozone began in earnest. A Eurozone debt crisis erupted soon afterwards, as members with similar debt levels such as Ireland, Portugal, and Spain saw the cost of ensuring their debt against eventual default rise quickly. By 2011, the crisis had hit such proportions that both the Greek and Italian governments had to resign, and were replaced by administrations headed by Papademos and Monti respectively, both of whom were trusted in Brussels as former EU insiders. The cost of having to bail out Italy alongside Greece, Ireland and Portugal was prohibitive for the Eurozone.

Yet the European Council reacted slowly and for a while seemed to think that no contagion effect would take place, and that the Greek situation could be managed in slow motion. Although in February 2010 the European Council asked Greece to “remove the risk of jeopardizing the proper functioning of Economic and Monetary Union,”³² no mechanism was put in place to reassure the markets that the Eurozone had a credible solution to the rapidly emerging contagion problem. Markets sensed the lack of policy direction and contributed to the escalation of the crisis. By the time that Greece officially requested a rescue package in April 2010, the situation was threatening to get out of hand. It was at that moment that the EFSF was formally put in place.³³ Yet even institutional innovation was not enough to stem the crisis and the lack of confidence in the Eurozone’s determination to deal with the problem. Measures are taken in the last possible moment and only after it has become obvious that unless something happens quickly the Eurozone may not survive. Last-minute rescue packages have had a detrimental effect to the extent they gave the impression that Eurozone did not take the problem seriously enough, and was driven to a solution only after its very existence came into doubt.³⁴ By the time more decisive action was taken, the crisis was firmly implanted and refused to go away.

Policy Choices

Slow action was a problem, but is also understandable. First, this was an extraordinary crisis experienced for the first time in the context of the Eurozone.

Second, Greece was in many respects an unusual case, since it suffered record high debt and deficit levels at the same time, while its political class was reluctant to commit to long-term reform and restore even part of its lost competitiveness. Finally and more importantly, political time is a lot slower than market time. Eurozone states and the EU in general need to take collective, consensus-based decisions and work out the details of their action in a way satisfactory to everyone concerned. Markets, in contrast, decide in seconds in a decentralized and often chaotic manner.

If timing is therefore an understandable weakness, the policy choices underpinning the handling of the Greek crisis are less so. Already in 2010, it was obvious that Greece had a mountain to climb and that the combination of very high debt and deficit levels called for one of two actions. The EU could have decided either to reduce the country's sovereign debt through early restructuring, or mutualize its debt to make sure that the Eurozone would remain immune from contagion.³⁵

But Germany and France chose to go along both routes with disastrous results. Until the last rescue package was agreed upon in February 2012, they pretended that Greece was essentially solvent, while the markets looked at the numbers and foresaw that the country would soon not be able to meet its obligations. As austerity started to "bite," strikes and protests caused further havoc to an already paralyzed administration and social unrest started to spread throughout the country.³⁶ An early restructuring of the debt would have prevented its continued rise after 2009.

Debt mutualization could have been another option. Issuing Eurobonds in a careful manner entails a series of advantages. First, it makes borrowing more credible as it pools the risk that sovereigns now have to bear individually. Second, it overcomes the current fragmentation in borrowing practices within the Eurozone and offers a political answer to the ability of the markets, exploited to the full until now, to pick off the weakest link in the Eurozone chain and attack it ferociously. The Eurozone has debt and deficit levels that compare favorably to those of the United States, the UK or Japan. Finally, Eurobonds strengthen liquidity and offer a potential rival to US Treasury bonds for creditors willing to look beyond Washington and branch out their portfolios.³⁷ In addition to Eurobonds, the EU could have acted decisively to make the European Central Bank (ECB) a lender of last resort to finance state debt. Finally, a European Monetary Fund would signal Europe's determination to tackle the crisis in a systematic rather than *ad hoc* manner.

Thus the problem here is one of political rather than economic logic. Debt mutualization means taking a decisive step towards fiscal union, and that is a step too far for the EU. Although new institutions have been created in the midst

of the crisis and there is speculation that Eurobonds will have to come sooner rather than later, moving towards some kind of economic federation is anathema for Europe's leaders and for many of their constituents. This is particularly true for Northern European euro zone members, who have reaped the strongest benefits from the Euro's creation and have augmented their competitive edge, not least through labor market reforms in the early 2000s.³⁸ Southern Europe, on the other hand, has seen its unit labor costs go up over the last decade and the gap between its own performance and that of countries like Germany widen further. The latest Commission growth forecast illustrates the point: the Euro area is forecasted to contract by 0.2 percent in 2012 but this hides the fact that recession will be deep in Greece (around 5 percent), Portugal (around 3 percent) and Spain (around 1.5 percent) while Germany and Finland will grow at about 1.5 percent.³⁹

Policy Content

The most important failing of the EU is its policy choice, and to be more precise, its policy mix. Over the last few years, belt-tightening in the form of sharp tax rises and deep cuts in public expenditure have been chosen as the only way out of the crisis. This is most obvious in countries like Greece, where belt-tightening *is* necessary and a level of austerity *was* unavoidable considering the delays and policy failures outlined above.⁴⁰ Still, using the need for reform to introduce measures that lead to social despair and doubtful economic wisdom is no way to exit the crisis.

A good example is labor relations: in Greece, government has been forced to reduce the minimum wage so as to allegedly enhance its competitiveness.⁴¹ Similar reforms have been introduced in Portugal, Spain and Italy. Further reducing the purchasing power of people living on low and very low income does little to reignite the economy and foster much-needed growth, as it is doubtful that companies will hire more faced with lower labor costs. What it certainly does is squeeze the lower-middle and middle classes, sharpening socio-economic inequalities in the midst of record-high unemployment and low labor mobility. The same policy recipe is used across the EU and is pursued with vigor and determination, even where its necessity is doubtful and its results are causing distress and further economic problems. As the Eurozone unemployment rate reaches 10.8 percent,⁴² its highest ever, it is clear that the European economic and social model, on which the EU prides itself, is in danger.

This policy has led to social reaction and causes continued political instability in those countries where the economic situation is worse. Social reaction is understandable and very much justified. In most countries, the debt crisis was not a debt crisis to start with: it was a private debt crisis that later on be-

came a public debt crisis through the policies of nationalizations and successive bail-outs touched upon in the introduction. Salaried workers and employees see their living standards fall without any serious contribution of their own to this crisis. Moreover, the arguments in favor of continued austerity and successive bank bail-outs only worsen the situation, considering that vast strata of the EU population are convinced that politicians and bankers have formed a “rich men’s alliance” to protect their own.

The consequences of this are far deeper than lower popularity ratings or a change in government. First, they go to the heart of our democratic societies to the extent that they help legitimize dangerous generalizations about “corrupt politicians” and the “inept political class.” A lack of trust towards democratic institutions had already become evident before the crisis began, and had resulted from the *de facto* immunity that politicians have enjoyed until now. The politics of austerity (what is more, unjust and indiscriminate austerity) fuels this resentment further and threatens the democratic system of popular representation. It does so by allowing people to reach for easy scapegoats as they fail to maintain their standard of living. When the scapegoat is not “politicians,” they are often the “other,” defined in ethnic or religious terms. Signs of rising xenophobia and racist attacks are multiplying in Greece as well as across the EU. The strong opinion poll support that far-right parties enjoy is the most obvious piece of evidence.

Secondly, the politics of austerity sharpens divisions within the EU between the north and south and reproduces unfounded stereotypes about the “lazy” southerners. Thus, one of the consequences of the current crisis in the Eurozone is to widen the gap of perceptions between Europeans and reinforce pre-existing stereotypes that harm the values of respect and tolerance that underpin the EU project. The unacceptable and ludicrous portrayals of Chancellor Angela Merkel and other senior German politicians in Nazi uniforms by the Greek populist tabloid press follows repeatedly aired complaints by northern European politicians for “the Greeks” and other southern Europeans to get their house in order and behave “responsibly.”⁴³ The fact that France and Germany were among the first to violate the terms of the Maastricht Treaty in the mid-2000s amidst sluggish growth and high unemployment is thus conveniently brushed aside.

Conclusion

The Greek crisis is a multifaceted phenomenon. The economic aspect of it is obvious and due to the country’s Eurozone it has attracted the world’s attention. Yet it would be a mistake to think that if the country overcomes its financial difficulties it can afford to go back to its old ways. Rather, the debt and economic

crisis is a reflection of much deeper, structural problems relating to the country's malfunctioning political economy. Its stifling bureaucracy, the absence of a sizeable, state-independent entrepreneurial class and factionalist, inward-looking trade unions and a political class addicted to patron-client relations have combined to bring the country to the brink of collapse. Although Greece did not have high levels of private debt when Lehman Brothers collapsed, its public debt levels revealed a political class that got used to financing its way through debt accumulation. It is now struggling to come to terms with a harsh reality imposed from outside.

This will have far-reaching political consequences. The next elections, scheduled for late April or early May, will be unlike any other in recent memory. They will underscore popular frustrations with the two major parties and especially PASOK, whose former leader and Prime Minister George Papandreou has received the bulk of the harsh criticism directed at his handling of the crisis. They are also likely to lead to an increase in the number of parties represented in Parliament, and are very likely to hinder the winner from forming a single-party majority government. Single party majority governments have been the norm since 1974, but a new culture of consensus-based politics will have to be implemented in earnest if the country is to recover. Pro-reformist elements exist today across the political spectrum. Their ability to overcome factionalist divisions and work in good faith with one another has today become a precondition to exit the crisis in a relatively short period of time.

As the second section of the article sought to make clear and despite the fact that Greece is the victim of its own deeds, the political handling of the crisis by the Eurozone has been inadequate. Moreover, a one-sided preoccupation with budget cuts intensified social tensions and threatened Europe's social and economic model. The good news for Europe is that it has not run out of time; focusing on growth and jobs as opposed to one-sided austerity is still feasible as well as necessary.

Endnotes

1. Valentina Pop, "Greece clinches do-or-die bond swap deal," Euobserver, March 9, 2012. Retrieved March 12, 2012, from <http://euobserver.com/19/115534>

2. In 2010 the UK had a deficit of 10.4 percent (Greece: 10.5 percent) and Ireland surpassed them both with the astonishing deficit level of 32.4 percent. Yet both Ireland and the UK scored way below Greece when it came to their debt levels. Athens was reporting 143 percent compared to 96 percent and 80 percent for Ireland the UK respectively. Spain had a very high budget deficit of 9.2 percent but a perfectly manageable debt level of 60 percent. Finally Italy was on the danger zone debt-wise with 199 percent but with a comparatively low deficit of 4.6 percent.

3. Eurostat, "News release: Euro indicators 31/2012," (Brussels: European Commission, 2012).

4. Official Gazette, “Ρυθμίσεις συνταξιοδοτικού περιεχομένου και άλλες επείγουσες ρυθμίσεις εφαρμογής του Μνημονίου Συνενόησης του ν. 4046/2012. [Regulations on Pensions and Other Urgent Measures for the Implementation of the Memorandum of Understanding of Law No. 4046/2012],” (Athens: National Printing Office, 2012).

5. Bank of Greece, “Νομισματική Πολιτική 2010-2011 [Monetary Policy 2010-2011],” (Athens: Bank of Greece, 2011).

6. European Council “European Council 1-2 March 2012: Conclusions, CO EUR2,” Retrieved March 15, 2012 from http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/128520.pdf

7. Consumer prices in Greece are very high and in many cases high above their equivalent elsewhere in the EU. What is more, prices have not fallen despite the severe crisis, exacerbating an already difficult situation. See Dimitra Manifava, “Consumer prices remain high despite crisis,” *Ekathimerini*, March 6, 2012. Retrieved March 9, 2012 from http://www.ekathimerini.com/4dcgi/_w_articles_wsite2_1_06/02/2012_426423

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40. Note, however, that austerity politics does not need to lead to social despair and a breakdown of the social contract. Public authorities ought to make sure that cuts target the well-off and ease the pain on those in modest incomes. This has not been the case thus far, neither in Greece nor elsewhere in the EU from Spain to the UK. This is the fundamental reason behind the spread of social unrest that Europe experienced in 2011.

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