EFFECTS OF AUSTERITY ON GREECE:

Financing of government debt and Troika intervention

by

Jane Lethbridge

j.lethbridge@gre.ac.uk

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Why government debt?

In 2001, Greece entered the Economic and Monetary Union (EMU). Part of the conditions of entry required adhering to the 1997 Stability and Growth Pact, which set limits on government spending and debt of not more than 3% GDP. EU Member States who joined this Pact effectively forfeited their financial independence. This immediate impact of this loss of independence was not obvious until the 2008/9 global financial crisis, when global banks were in crisis and national governments had to bail them out. Greek banks lacked capital and faced liquidity problems. By 2010, Greece was unable to repay or re-finance its government debt without help.

On 23 April 2010, the Greek government requested an initial loan of €45 billion from the EU and International Monetary Fund (IMF), to cover its financial needs for the remaining part of 2010. Three international organisations, the European Commission on behalf of the EU, the European Central Bank and the International Monetary Fund, together known as the "the Troika", started to have a powerful influence on Greece's independence. In exchange for a loan, the Greek Government had to draw up a programme set out in a 'Memorandum of Economic and Financial Policies' and a 'Memorandum on Specific Economic Policy Conditionality', detailing the austerity measures that it had to implement. These measures were voted into law by the Greek Parliament on 5 May 2010. The extent of the loss of sovereign control can be seen in the Memorandum of Agreement with the "troika" in which the Greek government stated:

> *"We will consult with the Fund before modifying measures contained in this letter, or adopting new measures that would deviate from the goals of the program, and provide the European Commission, ECB and the Fund with the necessary information for program monitoring. We will also consult and provide information to the European Commission and the ECB in the same manner."* [1]

"Troika" intervention

The €110 billion emergency loan was made up of an €80 billion loan from the Eurozone states and €30 billion from the IMF. The Greek government was required to introduce a series of austerity measures, designed to reduce government spending. The austerity measures included cutting wages and pensions, reducing the costs of public utilities through privatisation, imposing extensive labour reforms and making cuts to health and welfare services. The "Troika" set targets for the Greek government which were to:

- Achieve 4.5% surplus GDP;
- Make spending cuts of 1.5% GDP (€3.3 billion) in 2011;
- Make additional spending cuts of 5.5% GDP in 2013-4;
- Reduce public sector jobs by 150,000 between 2011-2015;
- Cut the minimum wage by 20%. [2]

Impact of austerity measures on Greece

The austerity measures had an immediate negative impact on the Greek economy. The level of GDP fell in 2011 by more than 6.9%, as a result of a fall in internal demand and exports. The fall in internal demand was caused by the impact of rising unemployment, public spending cuts, and reductions in social security benefits, which affected both consumption and investment. This led to reduced government revenues because of lower tax incomes and higher benefit payments. Additional measures were adopted to reduce government expenditure, which included reductions in the cost of buying drugs for hospitals, increasing co-payments for drugs of €3-€5 and reductions in doctor's overtime, which affected the delivery of health services.[3] There were reductions in defence spending, local authority staffing and wider reductions in public investment, all of which contributed to the deterioration of the Greek economy. The "troika" also de-

manded that the Greek government reform the public sector, particularly reducing public sector employment.

The austerity measures weakened the Greek economy further. Although the "troika" monitored the implementation of the austerity measures, some of them were resisted by social movements, which led to a change in government. By February 2012, the Greek government had to ask for an additional loan, which meant that Greece had become even more dependent on the "troika". The second loan of €164.5 billion will continue until the end of 2014, with Eurozone countries, through the EFSF contributing €144.7 billion and €19.8 million from the IMF.[4]

Reports and reviews published by the EU and the IMF show the power that the "troika" has had over the Greek government and illustrate how austerity was considered the only solution for Greece. One example of this attitude was the dismissal of a social dialogue agreement between Greek social partners because it 'was not commensurate with the needs of the Greek economy, and did not deliver a strategy to quickly address the large challenges Greece is faced with'. [5] As a result, a programme to reduce labour costs by 15% was imposed.

The EU was also critical of the slow rate of reducing public sector employment and targeting social programmes, inviting OECD to provide advice. Part of the terms of the loans involved the use of technical assistance which was considered crucial for the success of the programme. This included advice on tax administration and reducing tax evasion, public financial management, public sector reform and projects to improve the business environment. For example in pension reform, the government had not progressed as fast as the "troika" demanded and so the reform of the secondary and supplementary schemes will be designed in consultation with the European Commission, ECB and IMF staff, and its estimated impact on long-term sustainability is validated by the EU Economic Policy Committee.[6]

Conclusion

The impact of the austerity measures on the Greek economy and Greek society has been devastating. There has been little evidence that the "troika" has been aware of the failure of its measures although the IMF in a report in May 2013, indicated that there had been some consideration of how damaging austerity policies had been but not enough to change the loan conditions. Greece is still being pushed to further increase the 'flexibility' of its labour market in order to make it more competitive. Consumption and government expenditure have continued to fall and government debt has increased. Meanwhile the social costs of austerity are affecting the whole of Greek society. Young people are leaving the country or remaining unemployed, thus reducing the potential for future economic growth.

Table 1: 2009-2012 Greece

	2009	2010	2011	2012
GDP (growth rate)	-3.2	-3.5	-6.9	-4.7
Employment growth rate	-0.7	-1.9	-6.3	-4.8
Current account balance (% GDP)	-14.3	-12.3	-10.3	-6.9
General Government debt (% GDP)	129.3	144.9	165.3	161.4

Source: www.imf.org

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[3] Karanikolos et al (2013) Health in Europe 7 Financial crisis, austerity, and health in Europe The Lancet 27 March 2013

[4] http://ec.europa.eu/economy_finance/assistance_eu_ms/greek_loan_facility/

[5] EC Directorate Economic & Financial Affairs (2012) The Second Economic Adjustment Programme for Greece Occasional Paper No 94 March 2012 p.38
http://ec.europa.eu/economy_finance/publications/occasional_paper/2012/pdf/ocp94_en.pdf

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