PROSPECTS AND POLICIES FOR THE GREEK ECONOMY

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The Eurozone Crisis, Greece, and the Experience of Austerity

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LEVY ECONOMICS INSTITUTE OF BARD COLLEGE AND FORD FOUNDATION

GREEK SOVEREIGN DEBT CRISIS

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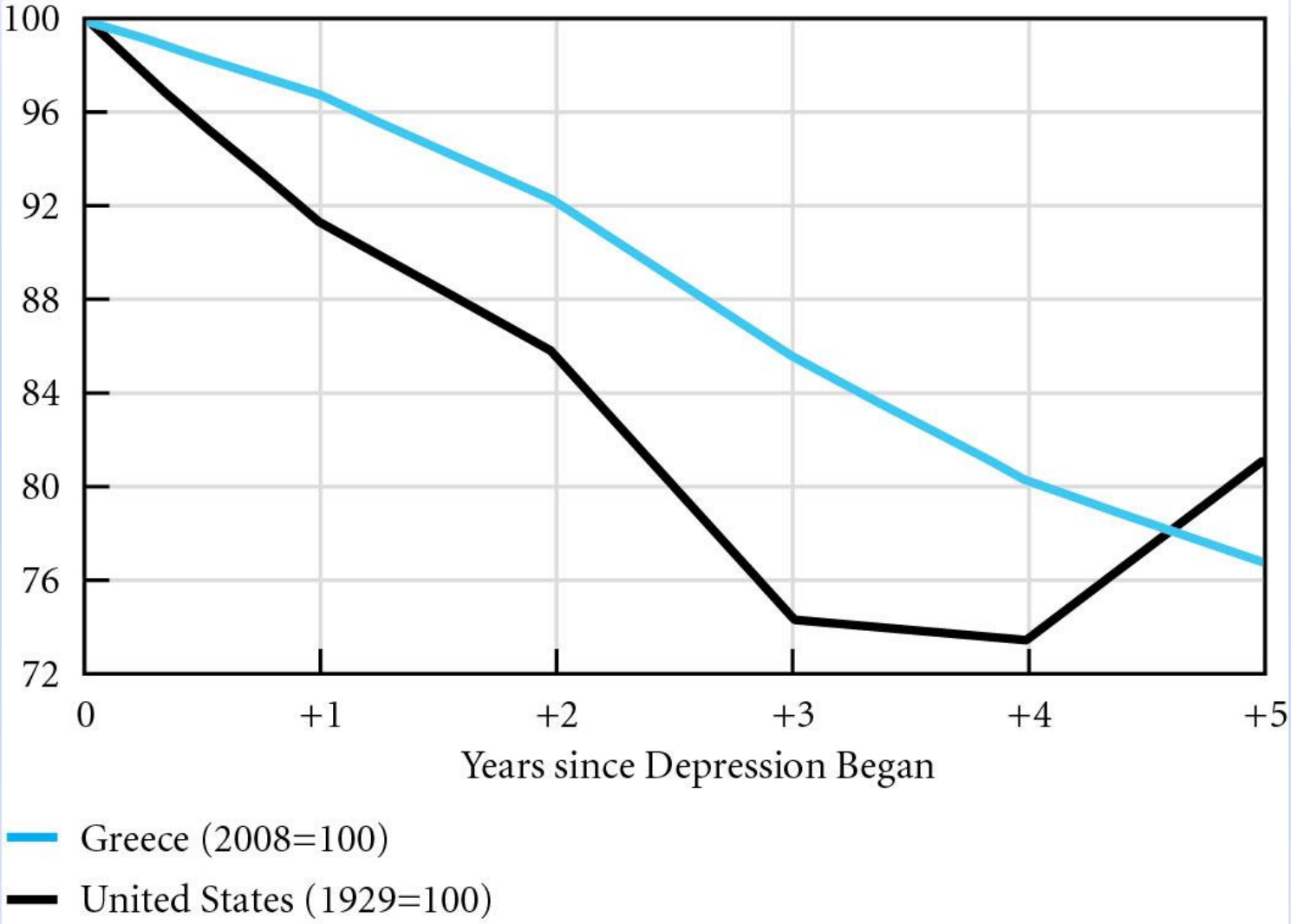
Inability of Greece to roll over maturing debt in 2009 because of much higher government deficits (15.8%) and accumulated debt of over 125% to GDP than originally estimated.

Fear of contagion involving other Eurozone countries, i.e., Portugal, Spain and even Italy.

Greece turned to EU and IMF. The result was two rescue programs totaling about 250 billion euros with harsh austerity measures that are still continuing and causing devastating effects.

Greece is, for the sixth year, in continuing deep recession, and the cumulative economic effects are much worse than those experienced by the U.S. during the Great Depression.

Figure 1 Greece and the United States: Two Great Depressions—Real GDP Indices



Sources: BEA; ElStat

Figure 2

Greece. Contributions to real GDP growth

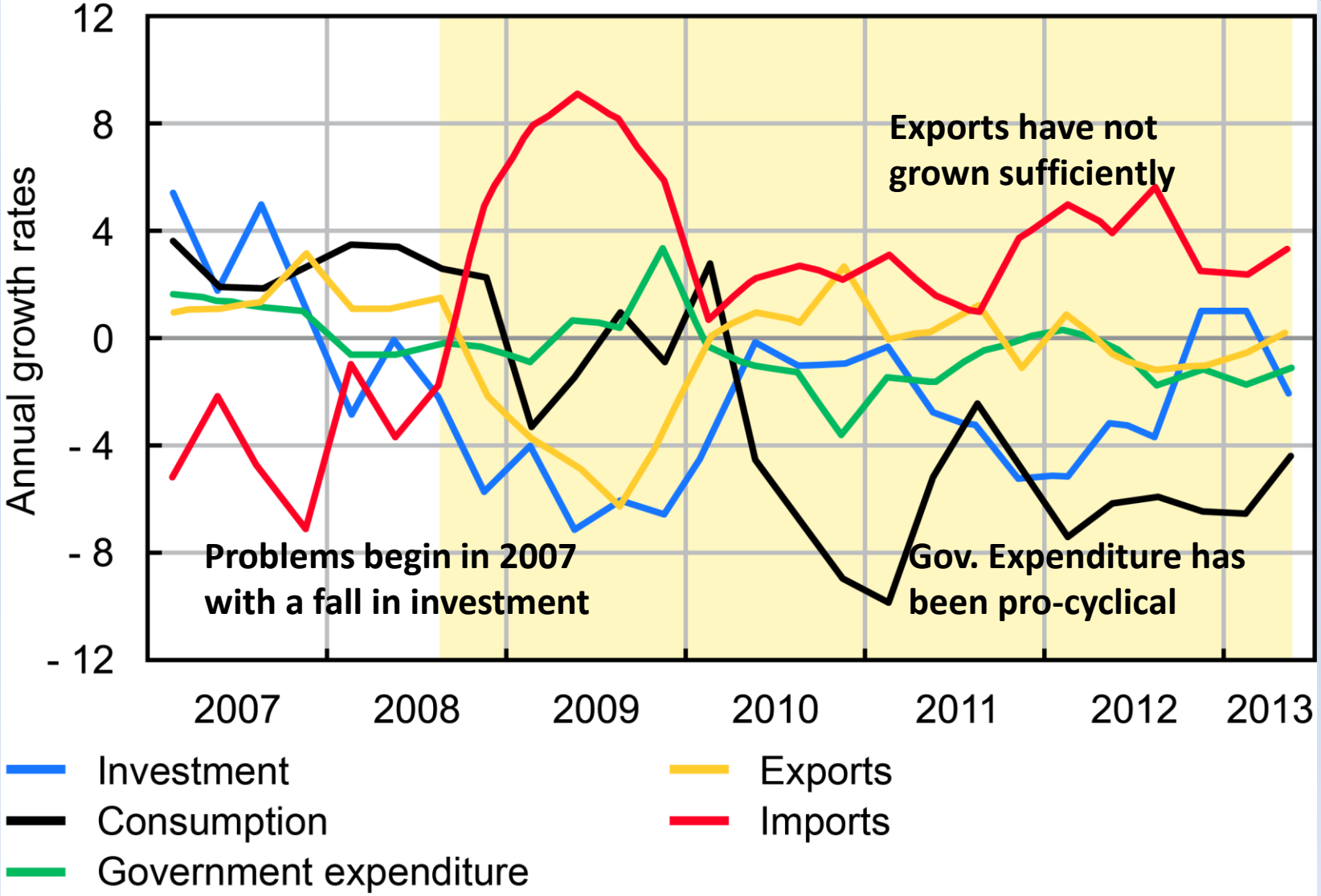
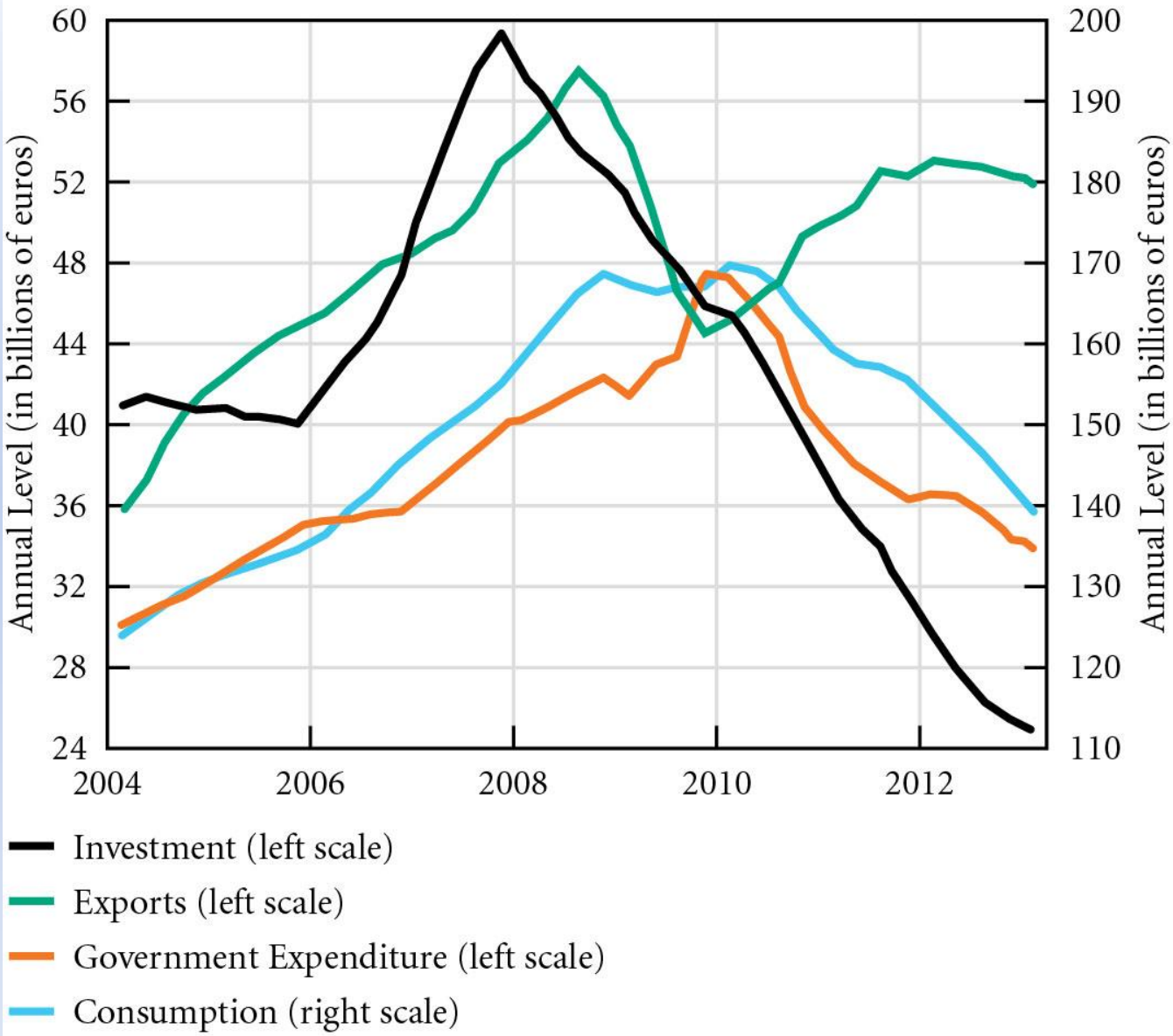


Figure 3 Greece: GDP Components



Source: ElStat

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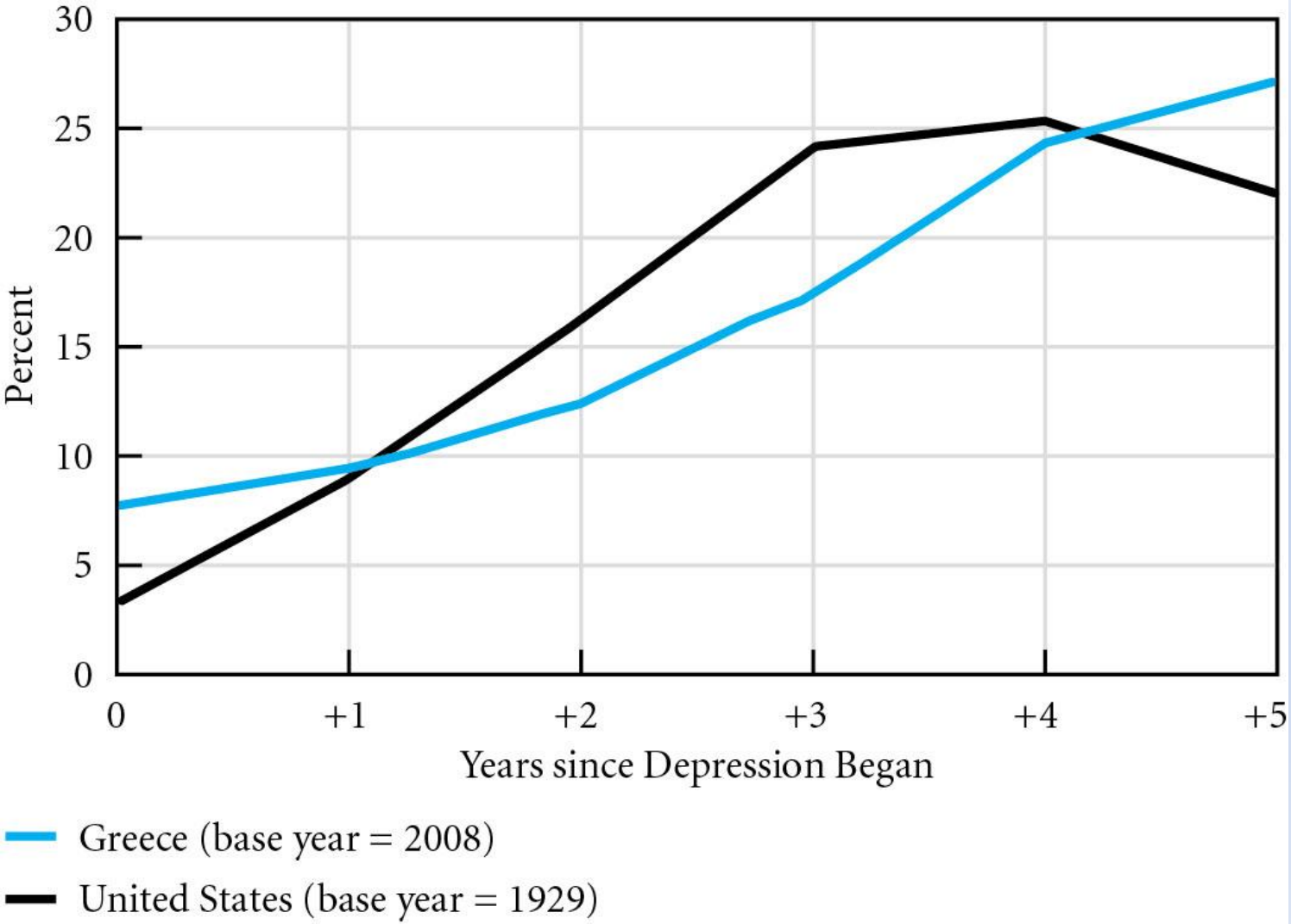
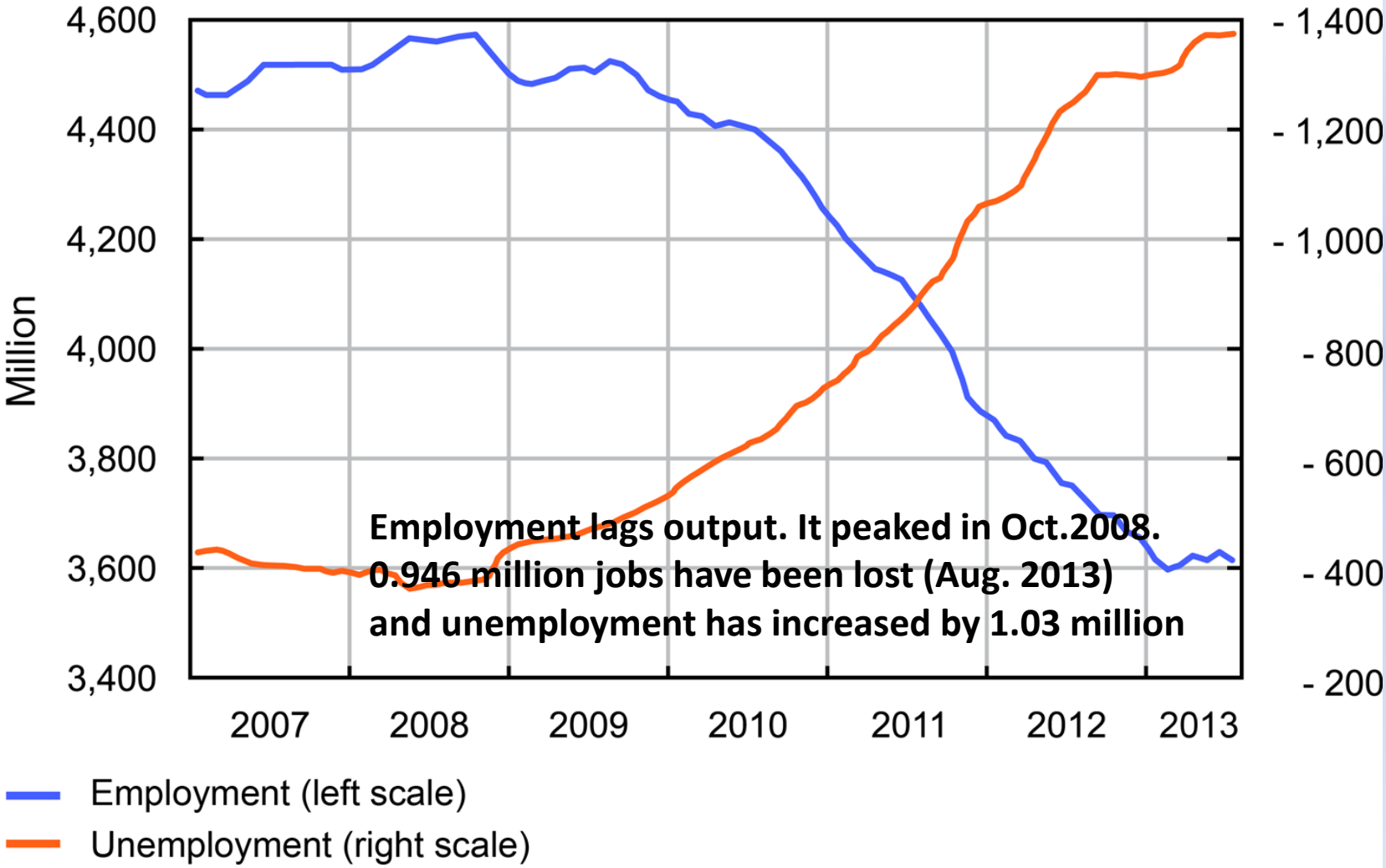
Figure 4 Greece and the United States: Two Great Depressions—Unemployment Rates



Sources: BEA; ElStat

Figure 5

Greece. Employment and unemployment



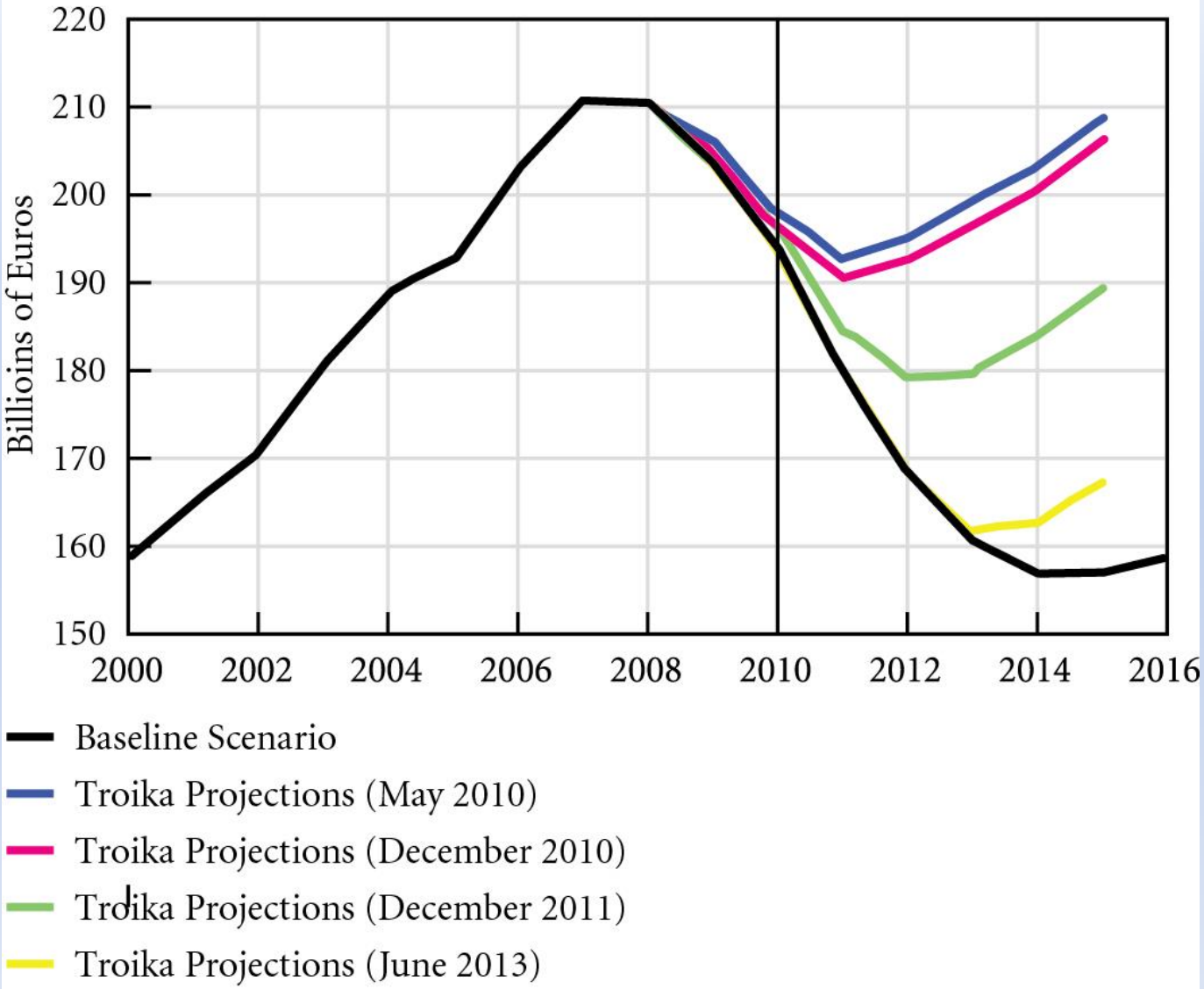
Source: ElStat

THE TROIKA PLAN

The Troika (IMF; EU; ECB) plan aimed at solving the problems trough

- **Fiscal austerity: reducing public employment; increasing taxes; privatizing public enterprises**
- **Internal devaluation: target 15% decrease in nominal wages; actual devaluation is 30%, double the target**
- **Public debt has been restructured (haircut) and gradually transformed. Now most of Greek public debt is a credit of EFSF and other Eurozone institutions**

Figure 6 Greece: Real GDP (2005=100)



Sources: IMF; EC; authors' calculations

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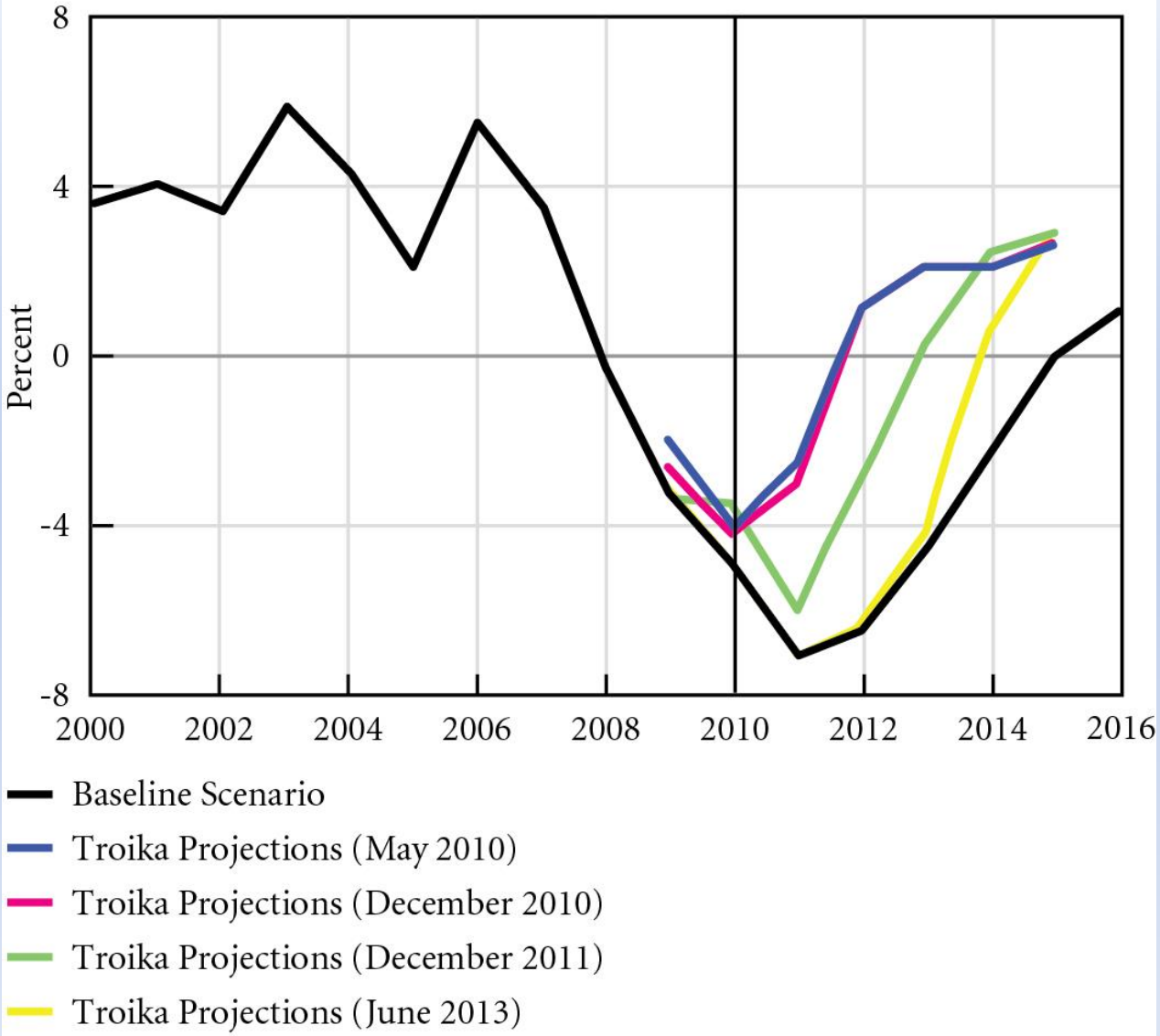
Figure 7 Greece: Real GDP Growth Rate



Sources: IMF; EC; authors' calculations

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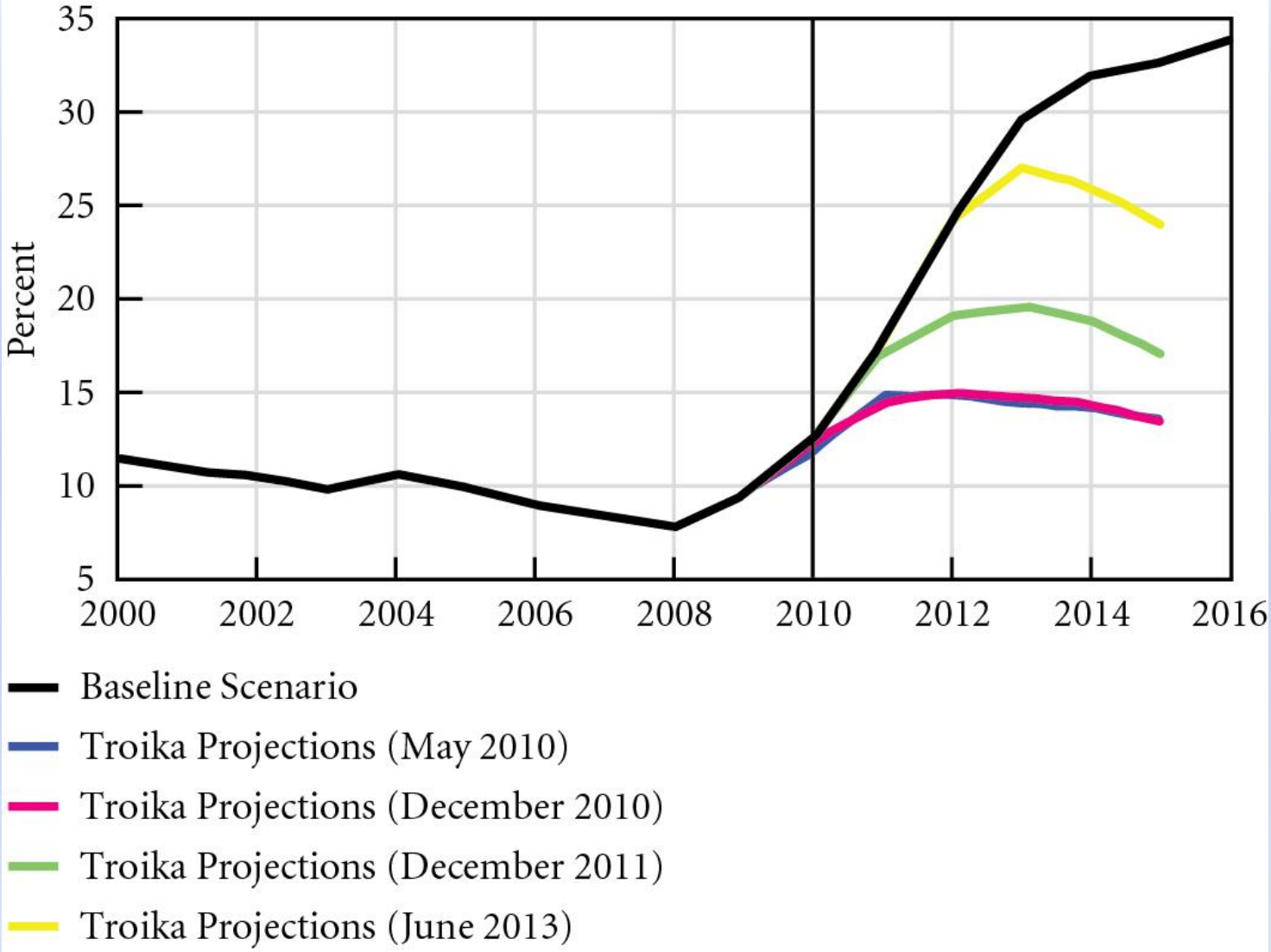
Figure 8 Greece: Unemployment Rate



Sources: IMF; EC; authors' calculations

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Figure 9

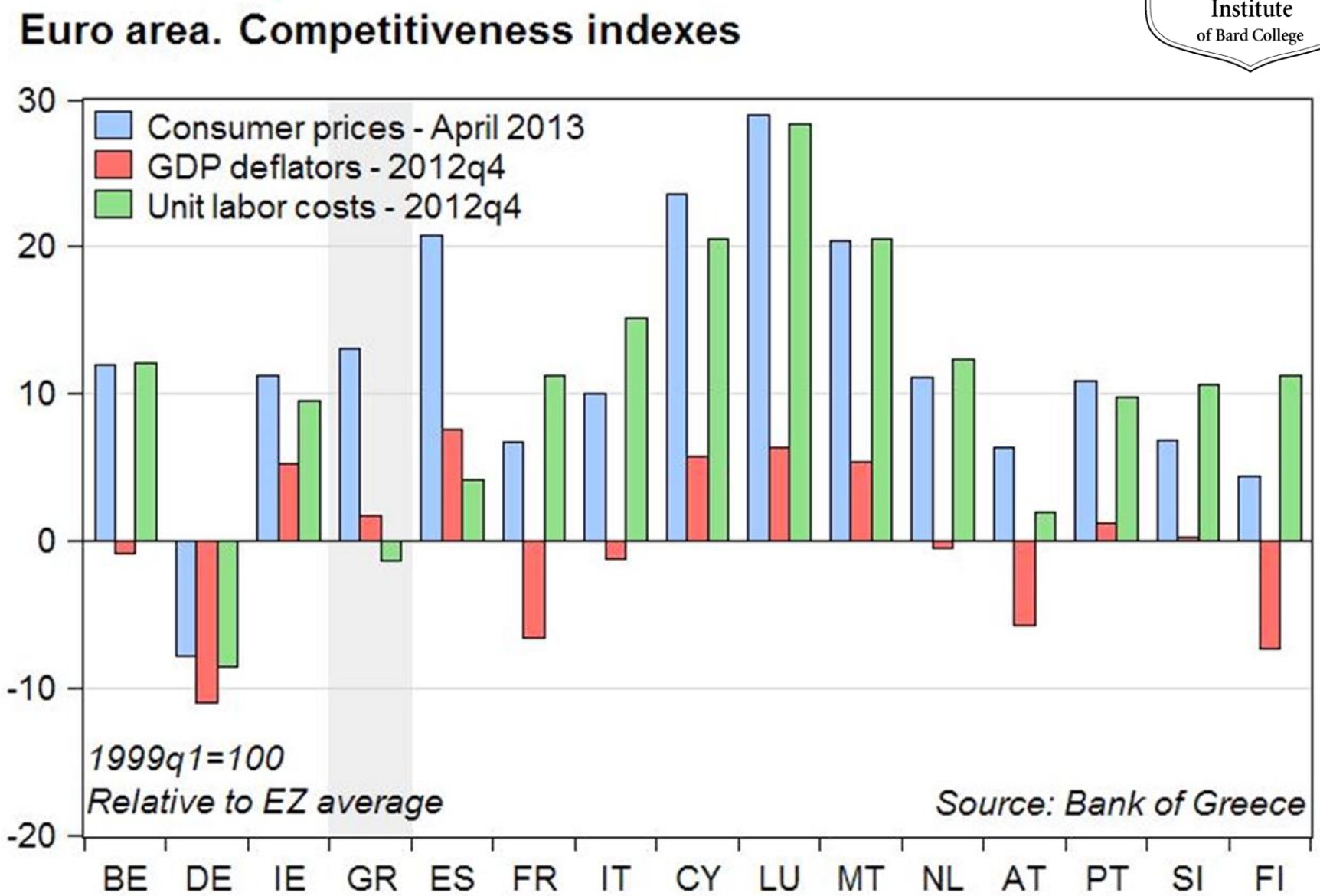
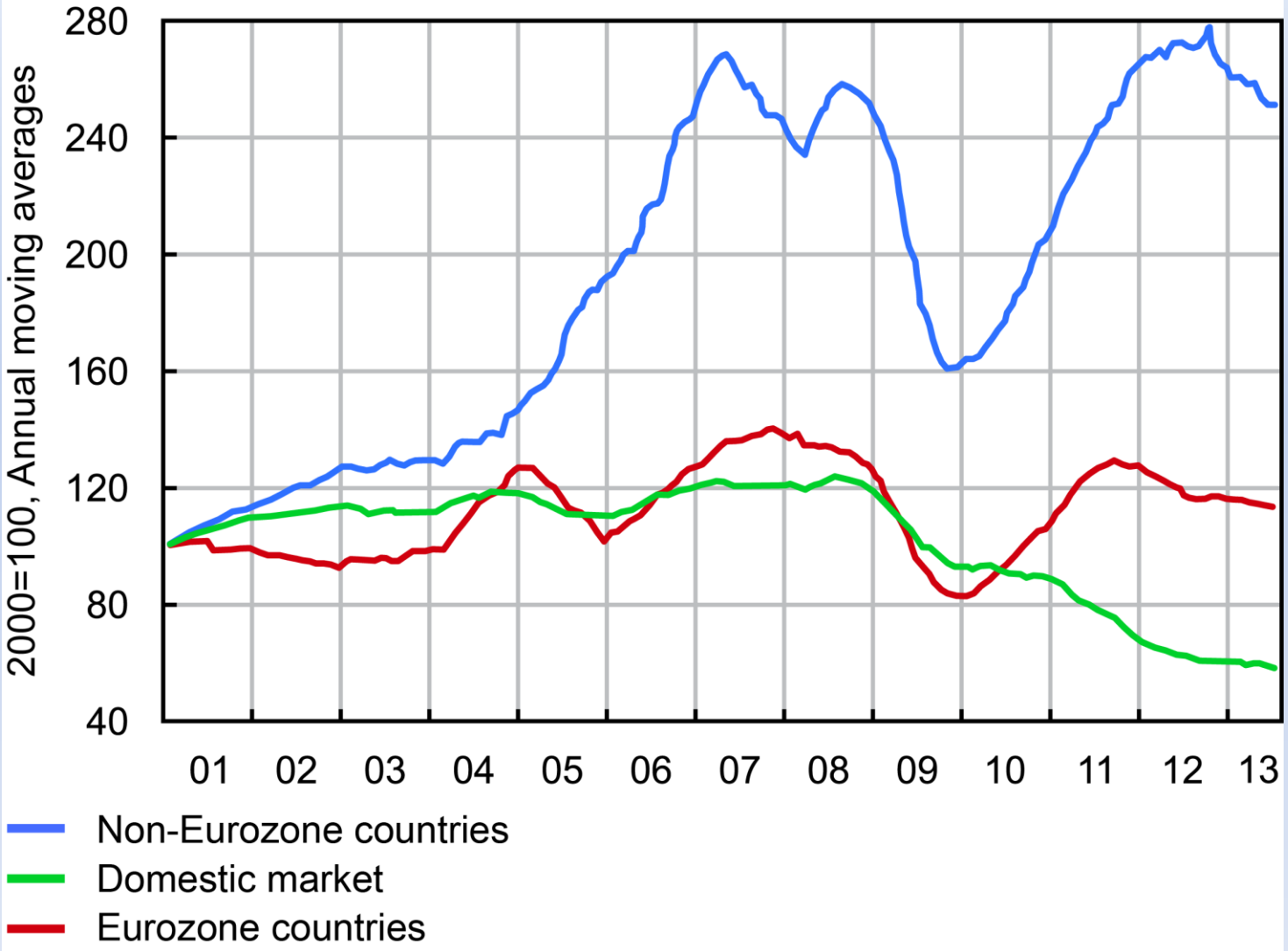

Euro area. Competitiveness indexes
Consumer prices - April 2013
GDP deflators - 2012q4
Unit labor costs - 2012q4
30
20
10
0
-10
-20
1999q1=100
Relative to EZ average
Source: Bank of Greece
BE
DE
IE
GR
ES
FR
IT
CY
LU
MT
NL
AT
PT
SI
FI

Figure 10
Greece. New orders indices in industry



Source: ElStat

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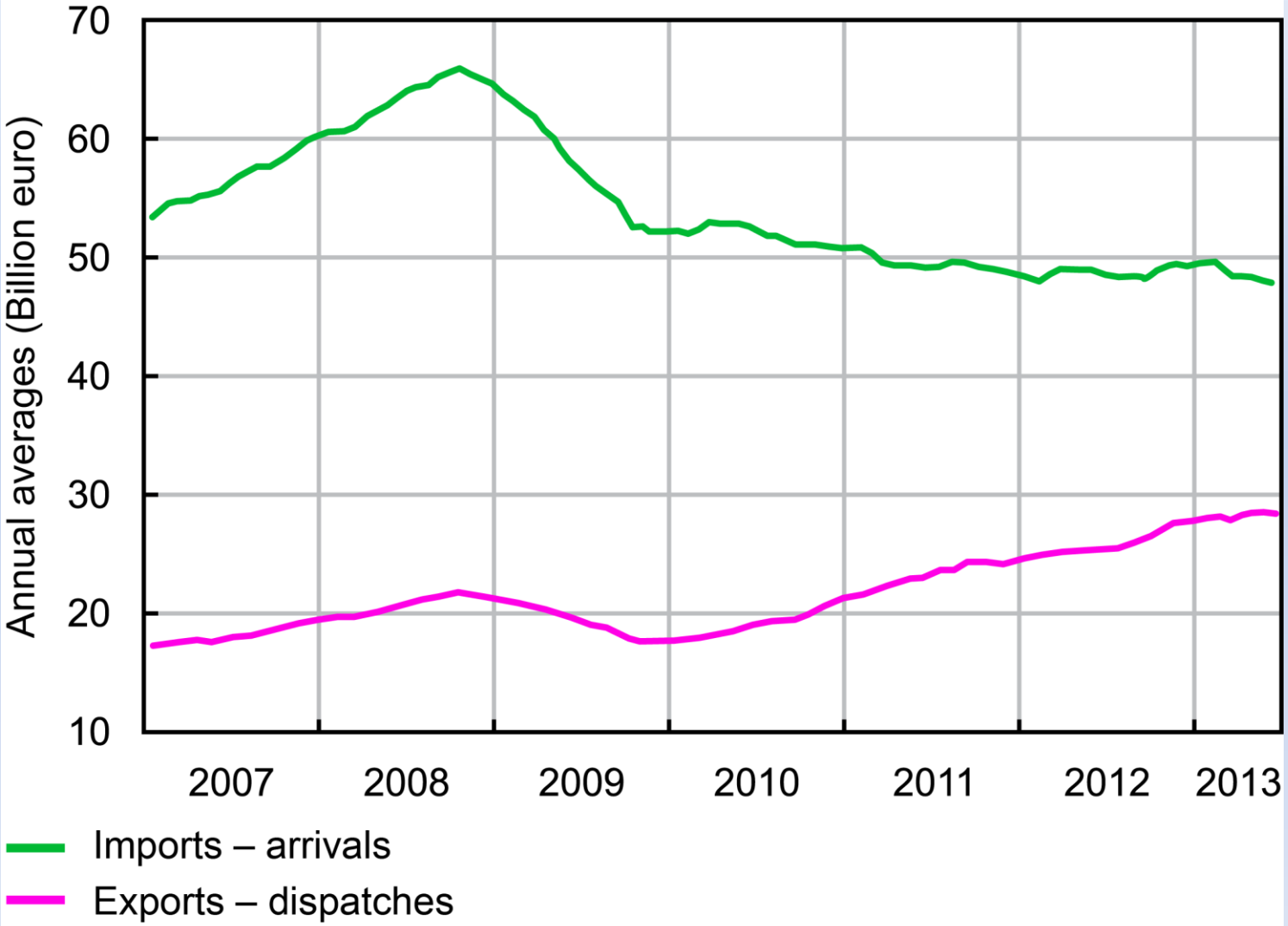
Table 1
Greece – Exports by destination (2011)

	Million euro	*Percent*	*Cumulated*
Italy	2,955	9.32	9.32
Turkey	2,485	7.84	18.64
Germany	2,454	7.74	26.47
Cyprus	1,903	6.00	34.21
Bulgaria	1,724	5.44	40.21
United States	1,712	5.40	45.65
United Kingdom	1,239	3.91	51.05
France	906	2.86	54.96
Romania	830	2.62	57.81
Singapore	818	2.58	60.43
Macedonia	794	2.50	63.01
Spain	640	2.02	65.51
Netherlands	637	2.01	67.53

Figure 11

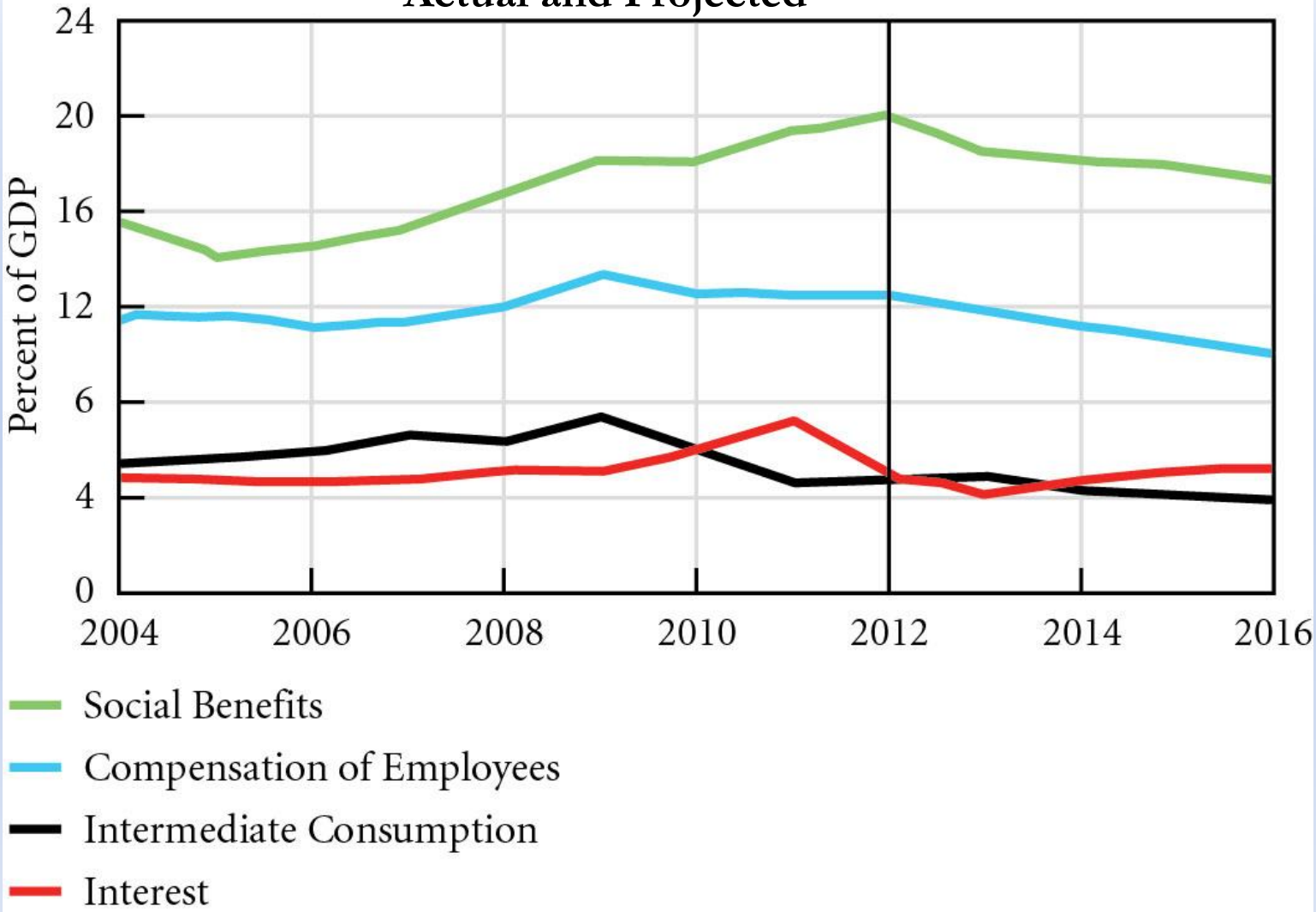
Greece. Trade in goods



Source: ElStat

Figure 12 Greece: Government Current Expenditure

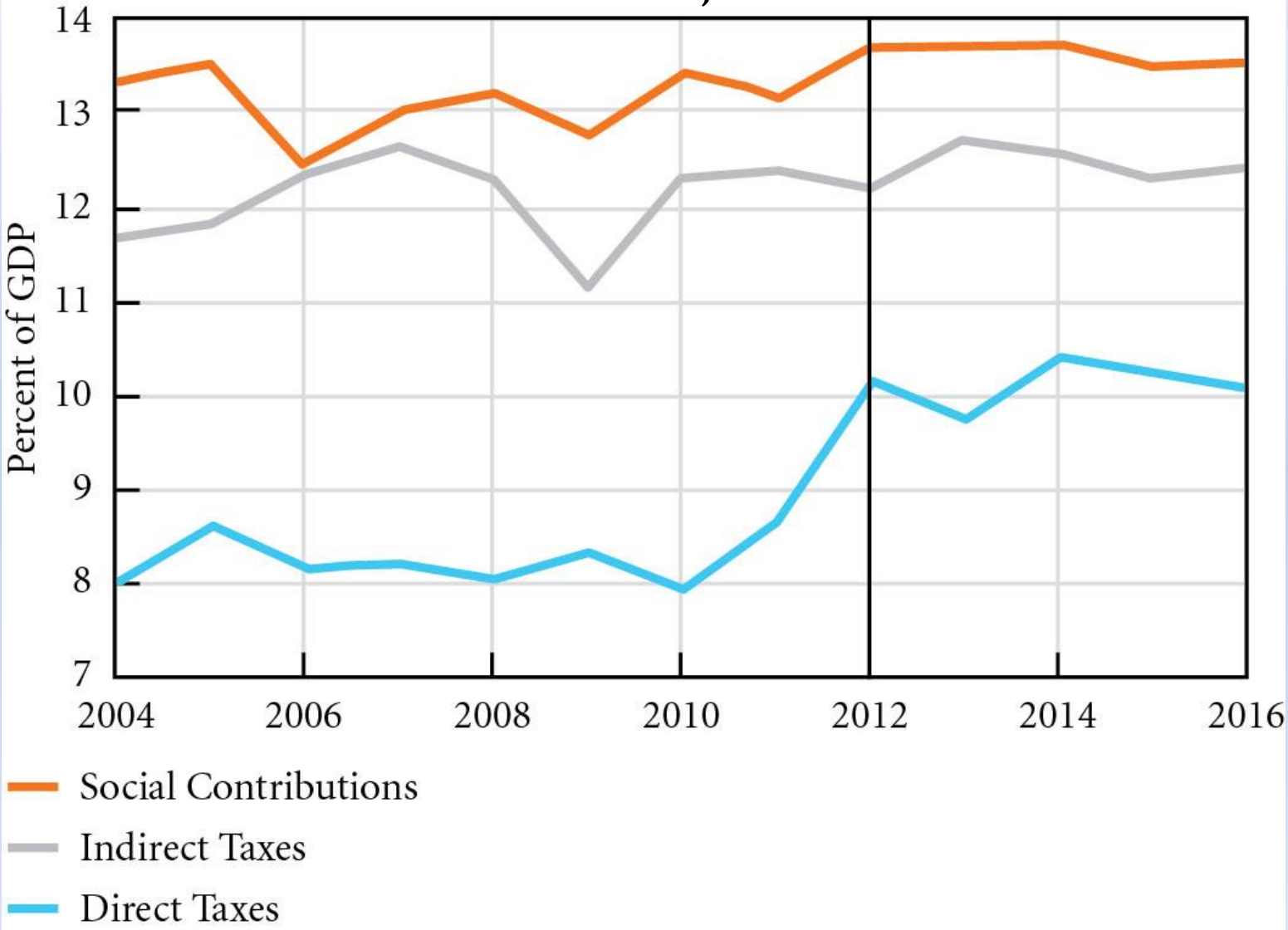
Actual and Projected



Sources: ElStat; EC; IMF

Figure 13 Greece: Government Current Revenue

Actual and Projected



Sources: ElStat; EC; IMF

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THE FAULTY STRUCTURE OF THE EURO PROJECT

- **If the European leaders had good knowledge of Eurozone countries' balance sheets, they would know that, for example, Germany's trade surpluses are matched with the north member countries' trade deficits.**
- **Member states with surpluses need to behave in a cooperative manner toward the trade deficit member states.**
- **An expansionary policy in Germany and other north European member states, together with increases in private sector wages, would help reduce Eurozone internal imbalances.**
- **Eurobonds, a Euro Treasury and/or a recycling of trade surpluses are the solutions to rehabilitate and complete the Euro project.**
- **But, since all of the above appear politically infeasible, other national options must be considered.**

AN ALTERNATE POLICY OPTION: A MARSHALL PLAN

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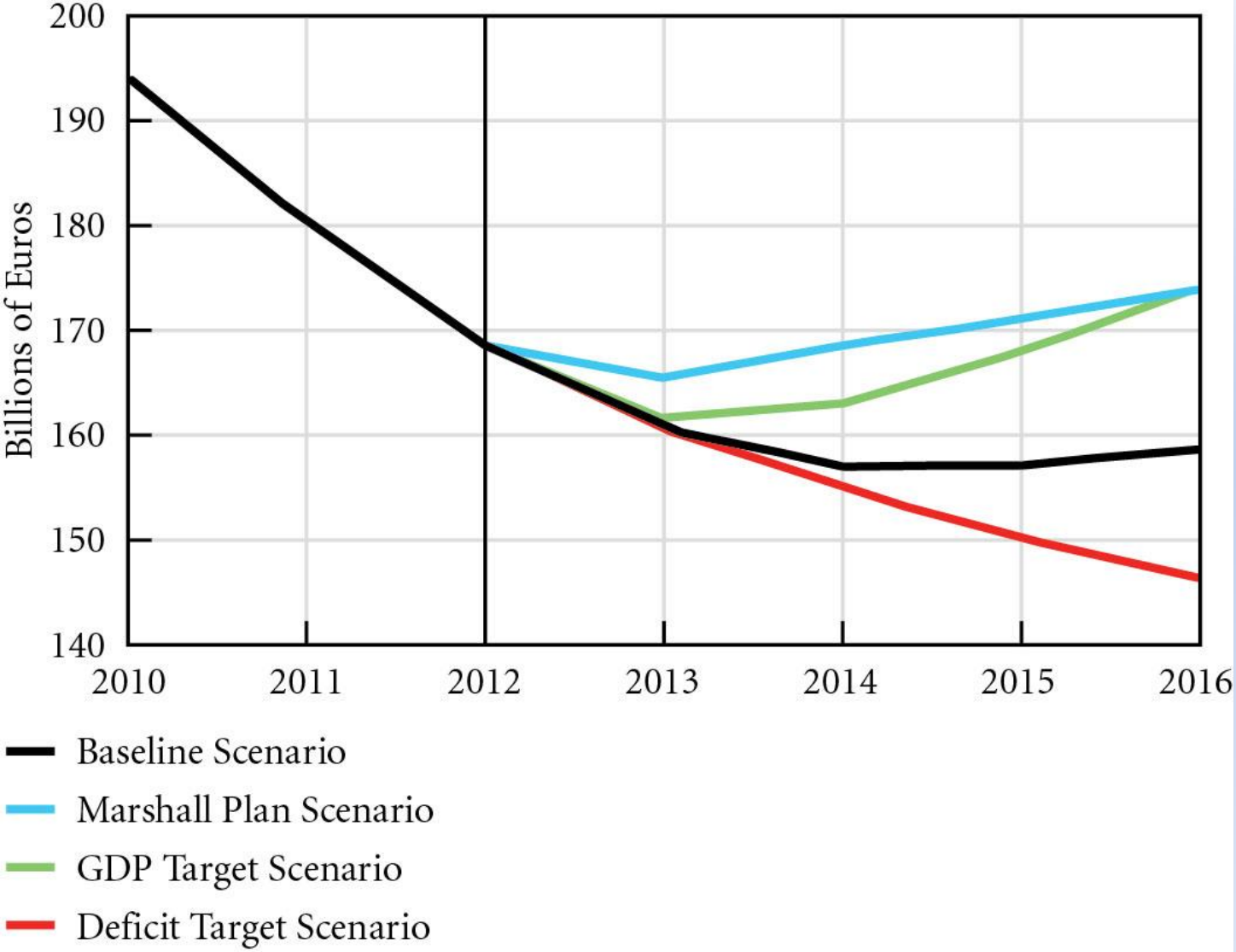
- **Externally funded and overseen by the European Investment Bank or other EU institution, for a total amount of 30 billion Euros at the rate of 2 billion each quarter beginning now.**

- **Funds would be spent for public consumption and targeted investment to foster growth in key production of goods and services.**

- **Funds could be used to finance a direct job creation program along the lines discussed.**

Figure 14 Greece: Alternative Scenarios for Real GDP



Source: Authors' calculations

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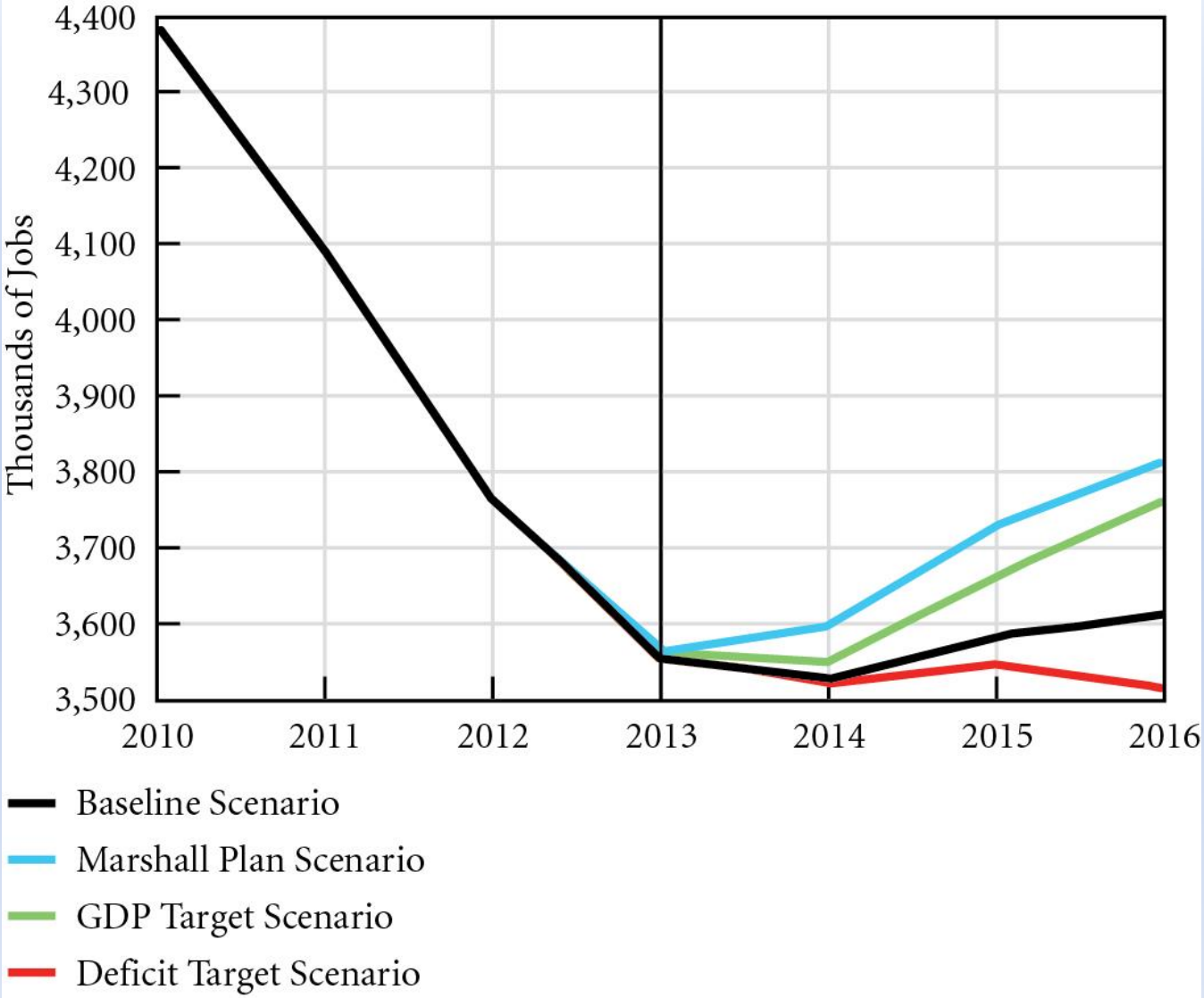
Figure 15 Greece: Alternative Scenarios for Employment



Source: Authors' calculations

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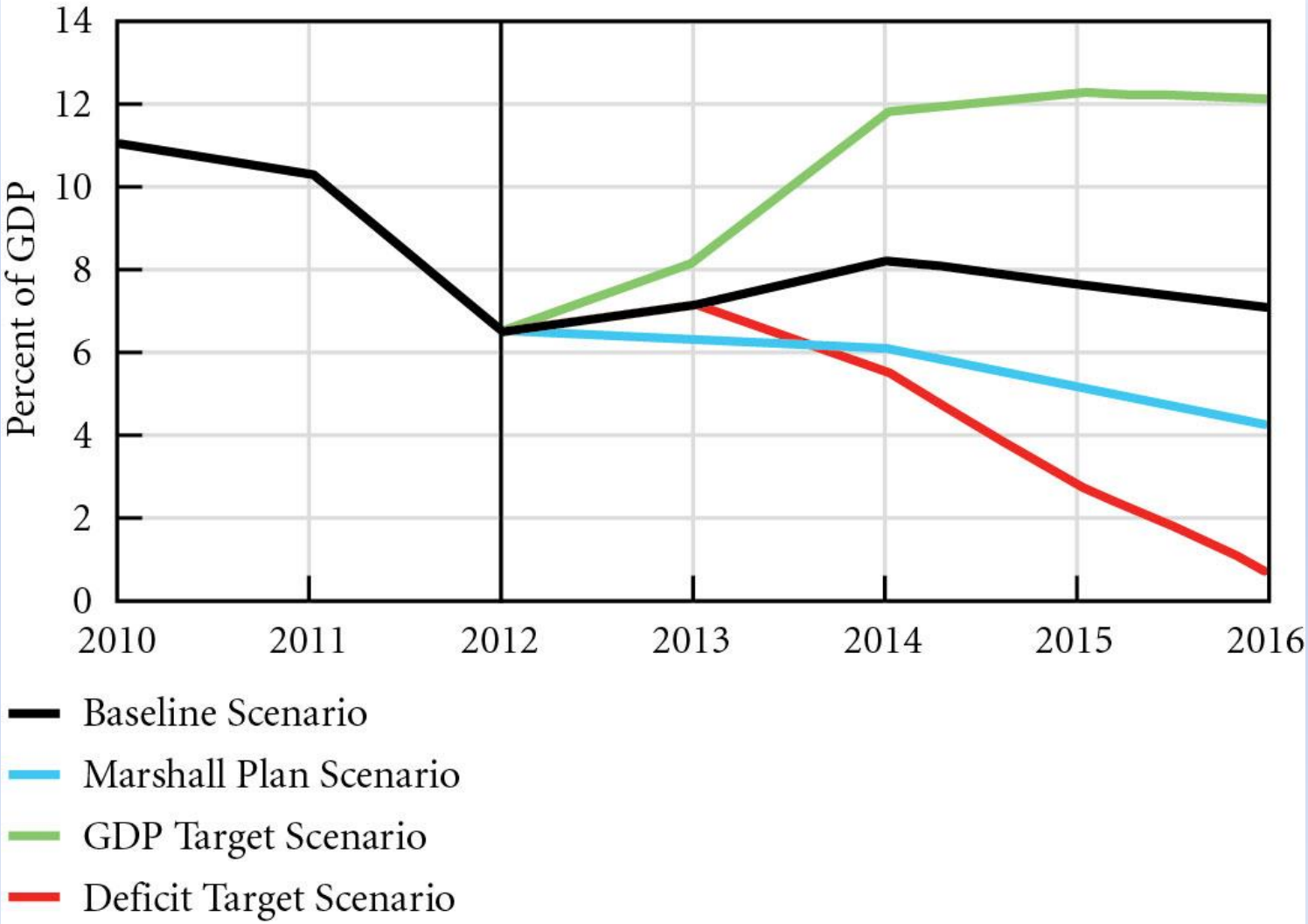
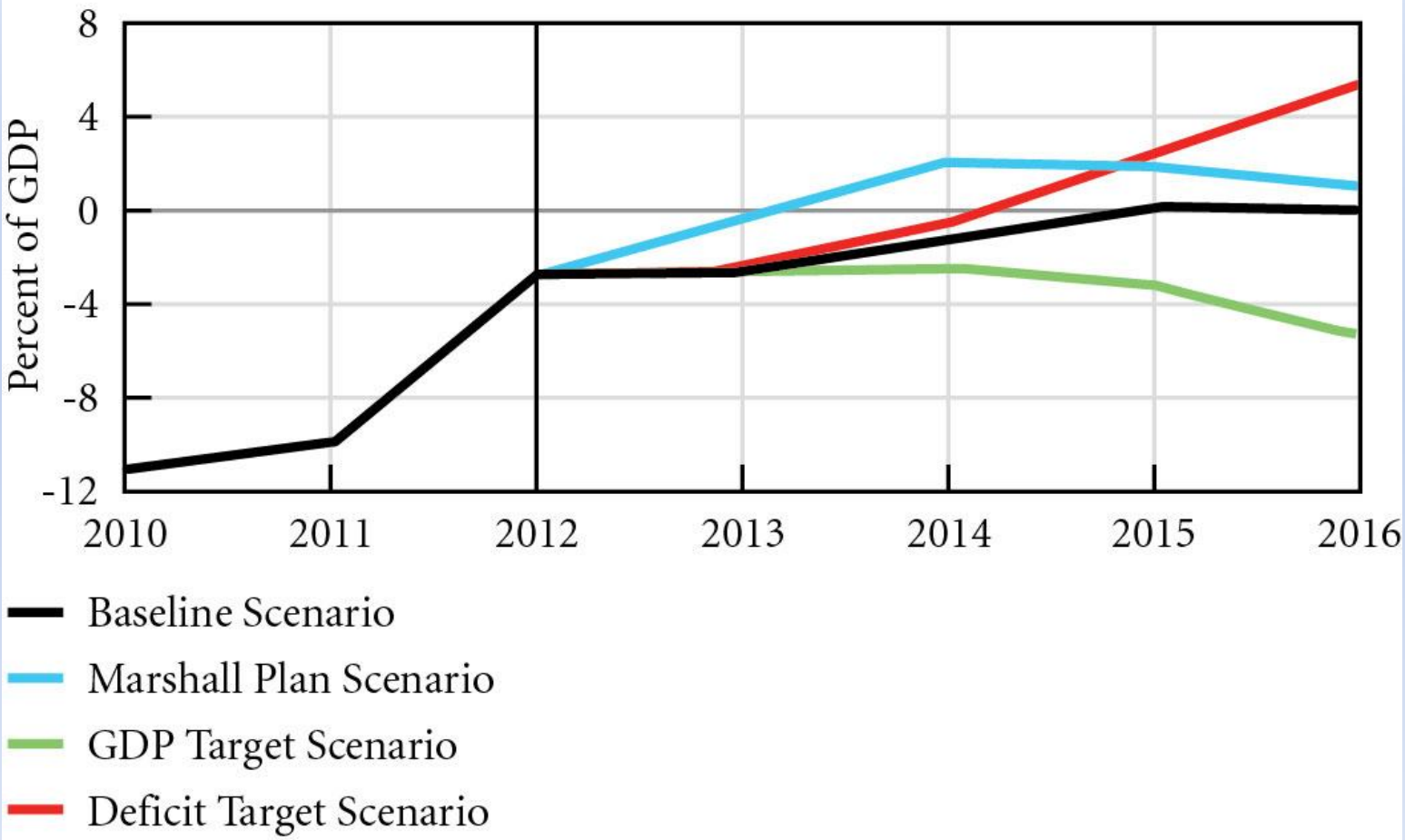
Figure 16 Greece: Alternative Scenarios for the Government Current Deficit



Source: Authors' calculations

Figure 17 Greece: Alternative Scenarios for the External Account



Source: Authors' calculations

A SECOND ALTERNATIVE POLICY OPTION: SUSPENDING ALL INTEREST PAYMENTS AND FREEZING PUBLIC DEBT

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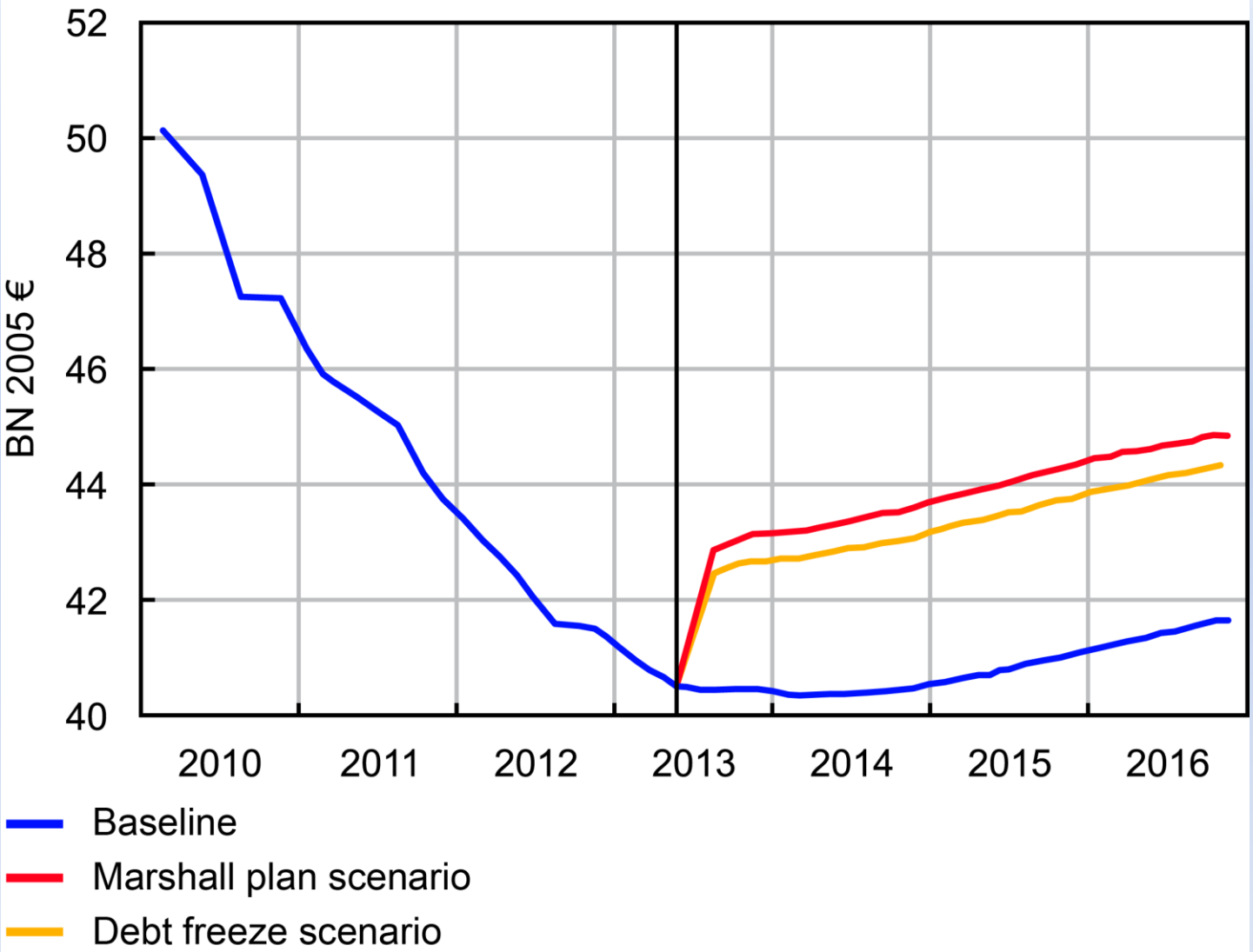
- **Public sector debt is frozen with no interest payments made until GDP levels are restored to 2010 levels.**
- **Creditors agree to roll over maturing debt for as many years, until 2010 GDP levels are restored.**
- **Interest payment is conservatively estimated at about 7.5 billion Euro per year.**
- **The amount of 7.5 billion Euro per year could be used, instead, for public consumption and targeted investments or to finance a direct job creation program.**

Figure 18

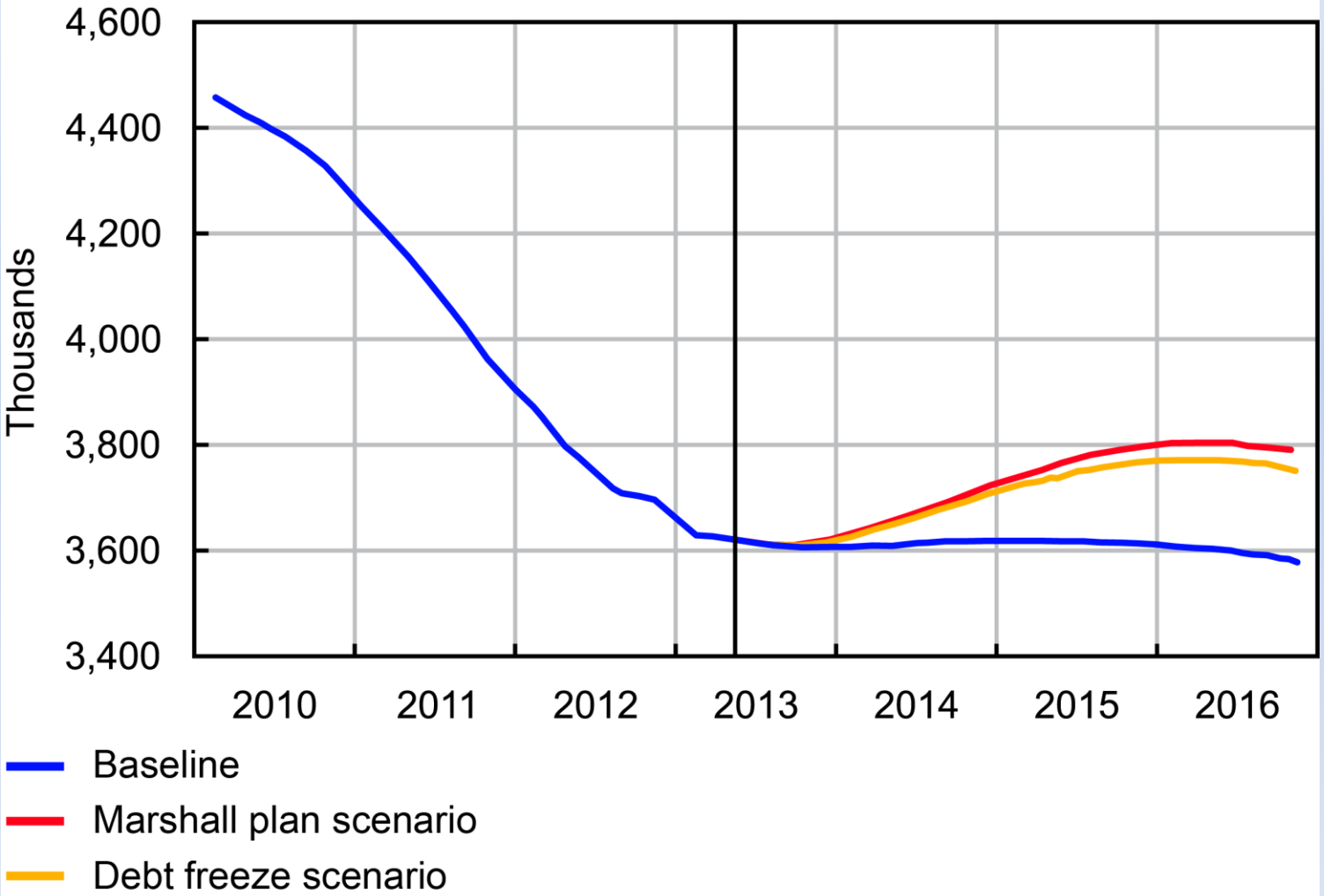
Greece. Alternative scenarios: Real GDP



Source: ElStat

Figure 19

Greece. Alternative scenarios: Employment level



Source: ElStat

TIME TO THINK THE UNTHINKABLE: A PARALLEL CURRENCY

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Important Issues to Consider:

- **Should it be convertible?**
- **Should it be backed by gold, reserves, future current account revenue, future tax revenue or nothing (fiat money)?**
- **How much parallel currency to inject?**
- **Which transactions should it be used for?**
- **Should existing financial assets be redenominated?**
- **Should foreign debt be redenominated?**
- **What would be the fiscal/monetary policy?**
- **Which institution would be the issuer of the parallel currency?**

A PARALLEL CURRENCY POLICY OPTION

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FEATURES:

- **Responsibility for the parallel currency will rest with the independent Bank of Greece to avoid government exceeding the agreed upon limits**
- **Government perpetual Geuro bonds, transferable, denominated at zero interest, acceptable at par in lieu of tax payments to government employees, domestic suppliers and transfer payments recipients, controlled by the Central Bank**
- **One way convertibility, from Euro → Geuro**

PARALLEL CURRENCY USAGE

- Conversion of government loans held by the financial sector in Geuro (about 15 billion Euro)
- 50 percent of social benefits paid in Geuro (about 19.3 billion Euro)
- 30 percent of public sector wages in Geuro (about 7.2 billion Euro)
- Conversion of government accounts payable (Tax refunds, etc.) in Geuro

PARALLEL CURRENCY TO FINANCE A DIRECT JOB CREATION PROGRAM

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- Research findings by the Levy Institute (presented in an earlier session) estimate the total cost for both direct job creation wages and indirect costs to be at approximately 7.1 billion Euros/year covering over 550,000 persons
- The multiplier of the program will create about 160,000 additional jobs and increase GDP by 11.6 billion Euros
- Tax revenues will also be increased by almost 4 billion
- The impact on imports should be smaller than in programs financed in Euro
- The program should be complemented with additional measures to increase productive capacity and provide some import substitution

ESTIMATED IMPACT OF A PARALLEL CURRENCY POLICY OPTION

- **If Euro "savings" are used to reduce the stock of debt, this policy option is somewhat contractionary**
- **If Greece continues paying interest on foreign debt at current rates, the growth path will be similar to our baseline scenario**
- **If the parallel currency option is in addition to the "debt freeze", the impact on the economy will be more substantial, and the consequences on the current account will be better**

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