

European issues

n°244

19<sup>th</sup> June 2012

# European Greece or Greek Europe?

## Abstract

*The results of the Greek general election of 17th June apparently open up a political path to Greece remaining in the euro zone, with the implementation of the Memorandum (a programme to reform and reduce deficits, as signed by Greece in exchange for European aid). In any case the maintenance of the euro by Greece depends less on the EU, which has demonstrated its solidarity with a series of aid programmes since 2010 totalling 340 billion €, than on its ability to return to reality and to rise to the challenge of competitiveness. Even though the return to the drachma is now a waning prospect the Greeks probably ended by believing that this would have led to a financial and banking disaster and also to economic ruin. Moreover it would be vain to believe that the activation devaluation would not go hand in hand with austerity measures, that would be just as draconian as those "set" by Europe, with the solidarity of its neighbours being reduced to a much lower level, if not disappearing completely. The Greek situation reveals that we have to shed all illusions about the creation of fictitious wealth via the distribution of generalised annuities at the service of political clientelism. It is necessary to build real growth on a competitive base. This diagnosis is valid for the 17 euro zone members. The dangers comes less from Greece than from the ability of the "big" States to implement the necessary reforms to re-establish a competitive economy. The cold wave that has hit Franco-German relations just as Greece seems to be about to banish the spectre that threatened the euro zone is a much more serious threat long term. Europe finds itself deprived of one of the most effective means to solve its crises and to build the vital stages on the path to political integration, the basic condition to settle the crisis and to increase growth. We might hope that the end of the French electoral season will lead to convergence on the part of the two main States in the euro zone towards greater political and budgetary integration and also to a growth strategy. Otherwise the dangers of political impotence according to the model of the ancient Greek cities could undermine progress towards European political integration.*

It is immoral to lie to others but it is tragic if you lie to yourself. This is the dead end that the Greeks have found themselves trapped in and out of which they cannot really escape unless they return to reality by assuming their responsibilities. Europe has and will do all it can to help Greece out of the pit, but it cannot be made into a scapegoat nor pay out endlessly. The austerity cure that Greece is implementing is the result of the situation which the Greeks and the political class have knowingly allowed to occur. None of the institutions in Brussels or Frankfurt forced the 110% increase on Greek civil servants' pay between 2000 and 2010 whilst France, which is not really subject to wage austerity, only granted a 30% increase to its own civil service over the same period. On the contrary, the fact

that Greek interest rates remained at a reduced level until the end of 2009 should have enabled, as part of a responsible policy, the development of a productive economy and the completion of the necessary reforms. Greece – and it is not the only one – since France, Italy and Spain have each followed similar paths – preferred to take advantage of free collective possibilities which the single currency represents, by distributing generalised annuities to the benefit of a clientelist political class.

After the confused vote of 6th May last the Greek electorate, with the second general election organised on 17th June now seemed to have opened the way for a coalition government with New Democracy led by Antonis Samaras, that will establish Greece in the euro zone, at

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the price of sacrifices set by the European Memorandum, the reform programme adopted in exchange for Europe's financial aid. The election on 17th June – a kind of referendum on the maintenance of the euro and the political coherence that goes with it, is above all about political acceptance on the part of the Greeks to continue with their domestic reforms together with the continued support of Europe.

### ***European Solidarity, Greek National Responsibility***

According to the Gospel of John, if lying imprisons then the truth sets you free. This is the path that Greece has now embarked upon to rebuild its society and its economy. Firstly because it will find itself on course for a winning growth strategy, and then because it will strengthen its establishment in the European Union. The confusion that followed the general elections on 6th May – which led to the need for a further election on 17th June, must finally be banished: it is impossible to want to keep the euro, as do 80% of the Greeks, including Alexis Tsipras' radical left, benefit from such massive amounts of aid as that provided by Europe – which totals around 340 billion €, ie equal to all of the amount of the debt before the crisis or 30,000 € per person – and also postpone reforms to later or only accept superficial measures. No one can pretend that these reforms will be painful, and that they will bring to the fore a feeling of disillusionment about a fictitious reality which the entire country and the political class has entertained for so long. But the Greek government and the population cannot want to count on the indefinite solidarity of the citizens of Hamburg, Milan and Toulouse and yet refuse to agree to the sacrifices, which are as real as the funds are necessary to prevent the default of both the banks and the State. The euro zone cannot accept that Greece, as its swerves to extremes, should take the entire euro zone hostage: *"you have to save us whatever happens to prevent the contagion of Spain Italy, from neighbour to neighbour and of all of the Member States."* The major countries in the euro zone already know that they will be asked to provide a great deal of financial input for Greece to stay in the euro zone or to end by leaving it, which is now highly unlikely: "blackmail" will lead to a dead end, even if the Memorandum is

challenged in several years time. This is because the 17 euro area States will always be able to opt to aid the Greek banks that are in danger directly rather than aid Greece indefinitely as it refuses or has refused to cooperate by undertaking domestic reform in exchange for European solidarity.

Hence Greece has to be aware that above all, its long term future in the euro area depends on it alone. Pretending in one way or another that the Memorandum can be rejected or that matters can be limited just to superficial reforms and yet also count on European aid, as Syriza (the far left party that came second in the election on 17th June) maintained during its electoral campaign or hope to renegotiate it more than from a technical point of view, as was pleaded for sometimes by Mr Samaras' New Democracy, means taking the risk, beyond electoral rhetoric, of perpetuating illusions and the danger of further painful surprises. According to an article printed in *The Economist* in April, the latest electoral results have shown, both in France and Greece, what denying reality can cost. One of the clearest messages of the crisis since 2008-2009 has been the decisive role played by national democratic life in the preparation of opinion with regard to reality. In fact the choice of reality, i.e. of reform, is probably the safest means to convince the major euro zone countries to re-organise the calendar and the modalities of the reform programme, as intimated by Guido Westerwelle, the German Foreign Minister, after the release of the Greek electoral results. Acceptance and above all the honest implementation of the resorption of public deficits might also be undertaken together with European action levers to foster the competitiveness of the economy: direct public or private investments, programmes supported by the structural funds or the European Investment Bank (EIB), etc. A strategy like this would incidentally be completely in line with the economic logic to transfer savings over to a budgetary federation that is now being created. The Greeks, starting with the political classes, must finally understand that the present sacrifices are a result of the situation they placed themselves in and not Europe. They are taking part in a consolidation that is linked to a growth strategy and not to punishment inflicted by the Gods of Valhalla on those of the Olympus Mount.

***And if in spite of this Greece ....?***

In these conditions the declarations made by the European leaders in support of Greece's maintenance in the euro zone, and even calls on the eve of the election on 17th June, like that made by the French President to the Greek electorate, are just as much a demonstration of faith as they are a reversal of the burden of proof. The euro zone States could not have prevented Greece quitting the euro zone if its leaders had decided in one way or another to circumvent the obligations of the European Memorandum after the election on 17th June.

In this regard, as in many others, it is never certain that the worst will happen, especially if matters are technically controllable. It has often been said that Greece, comprising barely 2% of the euro zone's GDP, was a problem that the Member States could cope with; we might say, even though this scenario seems to be waning, that Greece's exit, after an explicit or implicit rejection of the European Memorandum, without ignoring the disruption this would cause – would still be manageable by the euro zone. The main dangers threaten the banking systems which hold most of the Greek public debt. European banks carry 80 billion € in terms of the threat against Greece, 40 billion of which are in France, which is still bearable.

Moreover if Greece quit the euro this would not automatically imply Greece leaving the European Union. It is hard to see why. Even though the texts might lend themselves to this interpretation, we would be able to count on an orderly political response Europe wide: from a monetary point of view the possible return to the drachma might go together with an immediate or ulterior orderly fluctuation – according to the European monetary system – in relation to the euro. From a banking and financial point of view, the re-introduction of a national currency, which logically would be greatly devalued against the euro – a rate of 50% would be quite possible – would increase the existing debt by a equivalent rate and assets would depreciate correspondingly, which would then lead to a significant depression on the real economy and would lead, all things being equal elsewhere, to default.

In spite of this the end of the euro in Greece would in no way necessarily mean the end of solidarity in Europe: it is likely that short term support measures to the Greek banking system would be implemented to

prevent collapse and the start of a "South American" spiral. We might also imagine that even if it is technically against European rules, the Greek authorities might decide to take temporary measures to control exchange rates. Finally,, contrary to what is maintained by all of those who rather flippantly laud expansionist policies and devaluation which is supposed to free them from austerity and re-introduce growth by magic, a return to the drachma together with its significant depreciation in comparison with the euro would not bring about the benefits it is said it would bring, except if there were to be an extremely strict austerity programme. With the drachma or the euro the Greeks are condemned to adopting draconian austerity measures before benefiting from the effects of the devaluation of their national currency. Austerity measures do not just concern public spending, they also cover prices and salaries. Likewise it would be an illusion to hope to benefit from the advantages of devaluation and also retain an inflexible labour market. Maybe it was the sudden awareness that a "national" solution, might prove to be worse for the Greek economy than the bitter potions administered by the IMF-ECB-Commission "Troika" that opened the path to reason on the part of the Greek electorate.

What the Greek problem and other similar situations tell us is that there can be no strong long term growth that will lead to the creation of jobs without financial consolidation together with a policy to re-establish conditions for a competitive economy. The only exception that confirms the rule is, incidentally the USA, which can continue with this almost indefinitely due to its capacity to issue an international currency and offer the best conditions for world saving thanks to the depth of its financial market. Moreover the USA has a much more flexible labour market than in Europe. American leaders have also pointed to the limits of the growth model focused on consumption and the support of this via speculative bubbles. In the case of the European countries it is vain to want to copy the American model especially since the conditions for an optimal monetary zone – price, salary and labour market flexibility, have not been met. As we see everywhere on the old continent, domestic efforts in support of competitiveness are necessary both for the euro zone members and the other members of the EU who have not adopted the single currency.

***The salvation of the euro zone depends on the ability of the big countries to adopt competitive growth strategies.***

The euro zone crisis, as it has developed since the start of the Greek crisis, has shown us that its member countries cannot continue with their national policies unless they have a common budgetary strategy. This is the first phase of budgetary federalism. Beyond the quest for high compatibility between national policies, it also shows us that the continuation of economic policies other than those based on the competitiveness of businesses is extremely dangerous, which finally end in stalemate, exhaustion and the impotence of what is presented as state voluntarism. In different ways Spain, Italy and France have, over the last ten years, chosen models based on consumption stimulated either by private speculative bubbles – Spain – or by State stimulated bubbles – France. At the end of the day the result of basing growth on the illusion that we can do without the basis of economic development, i.e. productive work, innovation, investment and exports leads to economic paralysis and political crisis.

The “tragedy” that has hit the Greeks and which is leading them to understand the false nature of a major part of their living standard is mainly a result of the distribution of rights via political clientelism over fictitious output levels. Within and outside of the euro zone this strategy would lead to the same results. The root of the problem in Greece, as in the rest of the euro zone States is inextricably linked both to inadequate national competitiveness and a lack of Europe wide budgetary federalism, as practiced in the USA, where the federal level represents 20% of the GDP combined with the implementation of obligatory budgetary balance in 49 of the federal States. Both are linked: if the Europeans want to put an end to slow growth they have to all push twice as hard in the same direction.

Although it is important to encourage Greece to work towards reforms and remain in the euro zone, the future of the single currency mainly lies in the hands of the big countries. In terms of the problems to settle and the strategies to define, it mainly depends on the ability of countries like Germany, France, Italy and Spain to agree on a strategy that is joint and competitive as far as finding a long term solution both to

the financial crisis in the euro zone and the growth crisis. are concerned. In the main Italy and Spain, which has just received 100 billion euros to support the stability of its banking system, have opted for deficit resorption policies and structural reforms.

At present it is the almost total break-down of the Franco-German motor, which more than the threat set by the Greeks, is the biggest cause for concern in the euro zone. The new French government, which is basing its economic policies on neo-Keynesian concepts of inadequacies in global demand, has shown that it wants to break away from the European approach of its predecessor and has decided to isolate Germany in order to push the euro zone members to extend this type of strategy Europe wide. From a political point of view the almost total breakdown of the Franco-German motor is depriving the euro zone of one of the most powerful means it has to settle its problems and to build political solutions that lean towards budgetary federalism and political integration. Germany's call on 7th June to progress towards this has not been answered to date by the French government. From an economic point of view François Hollande's “growth pact” to a total of 120 billion € is, in Keynesian terms, very weak on the scale of the euro zone's GDP – around 1% - and it ignores the problems associated with competitiveness – the cost and inflexibility of labour in Europe – which weighs heavy on its Member States' growth. Even if their governments were sensitive to enhancing the value of either Italy or Spain, we might doubt that Mariano Rajoy and Mario Monti would agree with François Hollande's idea of “growth”. Since the general elections have given the new French executive a majority in Parliament will Msrs Hollande and Ayrault know what to do to settle the problems affecting French growth? Far from being a result of inadequate consumption since it is artificially stimulated by public debt, weak French growth is the result of competitiveness that was destroyed with the collapse of the profit margins of failing companies, (gross operating surplus/value added) – 28% in 2011 against 42% in Germany – and labour costs that are 10% higher than our neighbours. But the French have not been prepared, as witnessed by some international observers, either for the diagnosis nor the remedy.

***Avoiding the confusion of the Ancient Greek Cities.***

If Greece's membership of the euro zone has been able to raise the most passionate and most varied type of comment, then the reason for being of its policy to play a full role and the European project depends from many points of view on its heritage and its civilisation. By constantly wanting to place Europe on the edge of the abyss, by creating a single currency and yet refusing the budgetary constraints of an enterprise like this and the need to draw up a competitive growth strategy,

the Europeans are putting themselves in situation similar to that which divided the cities of Ancient Greece. Having probably found the economic means to settle the crisis at a time when Greece, in spite of the temptation to do otherwise, is starting to listen to reason, it would be sad for Europe to ignore the lessons provided by Ancient Greece.

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