European Stability Mechanism

The crisis in Greece: missteps and miscalculations

This paper analyses the origins of the Greek economic and financial crisis, covering 1981 to 2012. The work depicts how unsustainable imbalances built up over a prolonged period, often fueled by ample low-cost financing sources. It analyses the underlying forces such as institutional shortcomings, data misreporting, and deeply engrained social values and practices that nurtured a climate of widespread corruption and political favoritism. The paper addresses the achievements and shortcomings of the 2010 international support programme and its overall weak traction in Greece. While deficiencies in international surveillance and financial architecture played a role, the paper concludes that the key drivers of the crisis and of the mixed progress in the previous decades were home-grown.

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Foreword

JOAQUÍN ALMUNIA

High Level Independent Evaluator

11 June 2020

This special series of ESM Discussion Papers gathers analyses that inform the independent evaluation exercise. The objective of these Discussion Papers is to feed into the inference process, help generate debate on the evaluation themes, and provide a broader background to the evaluation mandate. The choice of themes for these studies was guided by the terms of reference of the evaluation.

The authors are external experts to the evaluation exercise. It is important to note that they have not served as members of the evaluation team, nor participated in the Institutions' country teams for Greece. As these Discussion Papers' analyses represent only the views of the authors, the input further strengthens the independence of the exercise. As such, these Discussion Papers represent the third formal element of independence in the evaluation, beyond my role as the High-Level Independent Evaluator, reporting to the Chairperson of the ESM Board of Governors, and of the Evaluation Reference Group.

I am grateful for the detailed work conducted, and would like to thank the authors for their valuable contributions.

Executive summary

Greece's economic and financial crisis stemmed from a combination of factors but was fundamentally a crisis of values, allowing the build-up of unsustainable macroeconomic and financial imbalances. Any sustainable crisis solution needed comprehensive, sustained values resolution, which was uneven and slow in coming in Greece. The roots of the values crisis developed from home-grown social and political issues, as well as structural problems in the malfunctioning of Greece's political economy. Perennial causes for concern were deep-seated corruption, weak institutions, sustained tax evasion, overgenerous pensions, high public salaries, and excessive state spending.

The crisis in Greece was fundamentally rooted in a crisis of social values that paved the way for unsustainable macroeconomic and financial imbalances. Corruption, weak institutions, tax evasion, and excessive spending persisted for decades.

Various social practices had become deeply engrained in Greek society, including 'diaploki' or entanglement, 'fakelaki' bribes in little envelopes and expensive 'rousfeti' political favours, for example in hiring decisions and property deals. For decades, Greek policymakers had been unwilling to cut public expenditures, with a large share flowing towards specific interest groups connected to parties in power; and they had closed their eyes to widespread tax evasion. Besides this, weak data and misreporting incidents weakened trust between Greece and its partners and creditors.

Intertwining interests, bribes, and political favours have been deeply engrained in the Greek society. Data misreporting incidents weakened trust.

These issues remained fundamentally unchanged for decades, together with politics focusing on the short-term. In an environment of easy access to cheap financing, this facilitated the accumulation of severe macroeconomic imbalances domestically and externally, including a prolonged declining trend in the national savings rate. Key factors underlying the crisis were a failure to address deep-seated structural problems, easy access to structural funds following EEC/EU membership and, later, minimal borrowing constraints after Greece entered the euro area. Euro area institutional shortcomings played a role, notably weak discipline and insufficient enforceability of economic policy rules. An approach that addressed imbalances by only using macroeconomic and financial policies was akin to giving painkillers to a patient needing surgery – like treating a competitiveness issue with just an exchange rate devaluation. Instead of disappearing, the underlying problem resurfaces with renewed strength.

Easy access to cheap financing and euro area institutional shortcomings also played a role.

Rather than use EEC/EU membership and later euro area participation to bring the country's own house in order, Greece instead relaxed policy discipline.

Greece was expected to reap much benefit from the EU's free internal market and expected euro area member discipline, but it used the integration with European partners to relax policy discipline rather than focus policies on maximising potential benefits. It never climbed to a higher, more stable, growth trajectory nor strengthened its resilience to shocks. By 2012, production in real terms still stood below that achieved in 2001, the year of euro area membership. And each year from 1980 – a year before Greece joined the EEC – its budget deficit sat above the 3%-of-gross domestic product (GDP) threshold demanded by the EU Treaty and the Stability and Growth Pact (SGP). Greece became dependent on borrowing to sustain an economy that was not viable. Rather than focusing on getting its own house in order through sustained stability-oriented policies and comprehensive economic reforms, Greece leveraged European funds and later its euro membership to provide cheap financing for excessive domestic demand. Through widespread acceptance of corruption, the Greek state neglected facilitating a competitive economy.

Weaknesses in international organisations' surveillance of Greece were exposed. Traction was weak with insufficient focus on the cultural and political economy forces at play. At the IMF, the framework for EU coordination provided little if any value-added peer pressure from Greece's European partners.

Surveillance of Greece by international organisations during the 1990s and the 2000s did little to prevent the mounting predicament. It suffered, in Greece and in many other countries as documented by ex post evaluations, from a number of weaknesses. The international organisations failed to address with perseverance, vigour, and traction the accumulating macroeconomic imbalances and structural weaknesses that morphed into a full-blown crisis when the financing sources dried up. Better traction is not only about addressing the right macroeconomic, structural, and financial sector issues, measuring and explaining what works, and closely following up. It is deeper. To gain traction, it is necessary to focus on the cultural and political economy forces at play, the incentives and values of decision makers, and of the public. While necessary, this is admittedly a tall order for surveillance alone. At the IMF, the internal processes for EU coordination through the group of EU board members (EURIMF) were not conducive to sufficiently strong surveillance. The representatives from neighbouring and other countries in the regions should be particularly well equipped to provide value-added peer pressure input to the surveillance discussions and help IMF staff provide sharp and focused surveillance. Instead, the agreed EURIMF framework meant EU board members tended to align themselves with EURIMF Chair statements based on European Commission and ECB inputs that in turn conformed to documents in the official EU surveillance framework. No one wanted to wash 'dirty laundry' in public.

Progress proved mixed during the first international financial support programme for Greece from 2010 to 2012. Successes included avoiding disorderly default, keeping Greece in the euro area as wished, achieving strong fiscal consolidation in numbers, containing spillovers into other countries, and triggering much-needed policy adjustments in other euro area countries, known as positive contagion. Arrangements bought time to build stronger regional and global firewalls, to advance towards a banking union, and to encourage better euro area risk sharing. But success was short-lived and costs became substantial. Output contracted and unemployment rose. In 2012, the country's real GDP per capita dropped below that of 2001, the year Greece became member of the European Economic and Monetary Union (EMU), while unemployment increased to over 24%. An emigration wave promoted a brain drain; in 2013 alone more than 100,000 left the country, mostly young, educated people with professional experience (Lazaretou, 2016). Poverty and income inequality increased substantially.

The first international support programme kept Greece in the euro area and avoided a disorderly default, but output fell, unemployment rose, and poverty and income inequality increased. It induced positive contagion for other countries and bought time for the international community to build stronger regional and global firewalls.

The programme assumed too much ownership by key political parties and the general population, and it overestimated the capacity and political will to implement vital structural reforms. The importance of working with partners towards social consensus was misjudged and a broad-based will to eliminate malpractices and enhance public and private sector efficiencies did not appear. Poul Thomsen, Director of the IMF's European Department and a key programme negotiator, said, "Contrary to other crisis-hit countries, there was no broad political support for the program from the outset. It was opposed from the start by the main opposition party, and soon also by the old-guard within the ruling party" (Thomsen, 2019). Vested interests resisted privatisation, public sector downsizing, and labour market reforms.

The programme suffered from weak ownership and lack of broad-based will to eliminate malpractices and enhance efficiencies.

Greece's population underwent more than 30 years of mixed progress and missed opportunities. But nothing is so bad that it is not good for something. The crisis exposed an unwieldy EU framework lacking contingency plans, where surveillance missed the importance of current account deficits, financial flows, and macro-financial linkages. The crisis helped identify problem areas to amend – and many have been addressed – while much has been learned about macro-financial feedback loops and intra-euro area contagion risks.

The crisis exposed gaps in the European macroeconomic and financial framework that were later addressed by drawing on lessons learned about macro-financial feedback loops and contagion risks.

Introduction

This paper describes and analyses the bumpy route leading up to and during the first years of the devastating Greek economic and financial crisis that erupted in 2009. It identifies the macroeconomic, structural, and financial market developments that explain the crisis. The paper also describes the underlying political, cultural, and social forces, prevalent for decades, which drove developments and hindered sustainable growth and convergence within the European Union (EU).

It surveys the way unsustainable internal and external imbalances accumulated in Greece and the part played by weak institutional foundations, repeated data misreporting, a frail business climate, and widespread corruption. These issues remained fundamentally unaddressed throughout the 1981–2012 period covered by this paper – despite closer integration within the EU and the euro area, and targeted conditions under international financial support programmes. The paper documents and discusses weak internal governance and strong links between corruption and poor fiscal outcomes.

The study also addresses issues that underlay weak traction and other shortcomings in the comprehensive surveillance by the EU, the Organisation for Economic Co-operation and Development (OECD), and the International Monetary Fund (IMF), including during periods of financial support, as well as design and governance imperfections in the 2010 international support programme.

The analysis is divided into key sub-periods to discuss what went wrong in Greece: after accession to the European Economic Community (EEC)/EU in 1981; then the period between the Maastricht Treaty ratification and joining the euro area; followed by the "happy years" after euro entry; and then during the 2010 international support programme before the first European Financial Stability Facility (EFSF) programme with Greece was approved in March 2012.

The study is primarily based on published written material and the author's experiences from three decades of professional involvement in international monetary and financial affairs across Europe and at the IMF. It draws on key surveillance, programme, and evaluation documents from the European Central Bank (ECB), the European Commission, the IMF, and the OECD, together with numerous political economy sources.

Chapter 1 describes the general economic developments since EEC membership was achieved in 1981, dividing the period into the following sub-periods: 1981–1993; 1994–2000; 2001–2009; and 2010–2012. This perspective underscores the overall stop-go approach in economic policy, with the goal of integrating Greece with her European partners serving as an incentive and driver of progress, only for Greece to experience significant policy shortcomings and economic weaknesses soon after the goals were achieved. Chapter 2 discusses underlying reasons for the inadequate surveillance by Greece's international partners (EU, IMF, OECD) and the limited traction. Chapter 3 looks at the first international financial support programme from 2010 and the reasons for limited, short-lived successes. Chapter 4 details the data misreporting that changed Greece's destiny and also carried severe repercussions for other euro area members, with Greece de facto never fulfilling the entry criteria for euro area membership or complying with the budget deficit threshold under the EU Stability and Growth Pact (SGP). Chapter 5 discusses political economy issues of the crisis, including widespread and largely unaddressed corruption, weak institutions, and other cultural and social shortcomings hindering sustainable progress. These aspects generally received little attention in macroeconomic literature covering the Greek crisis. As this paper concludes, these political economic aspects could be considered as much the root causes of the crisis as the large accumulating economic imbalances.

1. General economic and financial developments (1981–2012)

The underlying economic and financial imbalances and vulnerabilities that led to the crisis accumulated over several decades, during which Greece did not use EEC, and later euro area, membership to discipline policies nor fully exploited the potential from the internal market and substantial EU structural and cohesion funds – apart from brief periods, including in the second half of the 1990s.

Private and public sector structural impediments blocked or delayed progress in various areas. Many persistent obstacles were rooted in social values that accepted widespread corruption and tax evasion, a heavy bureaucracy, and government susceptibility to granting favours to privileged groups. An effective, sustained change of social values, and an end to stop-go policies closely related to the political economy aspects of the post-military junta period, were vital to avoid a crisis. When that proved impossible, it led to history's largest sovereign debt restructuring in March 2012.

Greece has a history of heavy state involvement in the economy and problems in servicing public debt. Before this crisis it had defaulted on or rescheduled debt five times and lived in a state of default for more than a hundred years combined since 1800 (Reinhart and Rogoff, 2009). A closer look at developments in some important time periods will cast more light on the long, rough road to the latest crisis and debt restructuring.

Table 1
Comparative economic performance of Greece (selected periods 1981–2012)
(Annual averages)

	1981–1993	1994–2000	2001–2009	2010–2012
GDP growth				
Greece	0.7	3.2	2.6	-7.3
Ireland	2.8	9.1	3.1	0.8
Portugal	3.4	3.5	0.6	-1.3
EU/euro area	1.9	2.9	1.1	1.0
Consumer price inflation				
Greece	18.5	6.1	3.3	3.0
Ireland	6.6	2.6	2.7	0.5
Portugal	15.4	3.0	2.6	2.6
EU/euro area	11.3	5.3	2.1	2.3
Unemployment rate				
Greece	6.8	10.7	9.6	18.3
Ireland	14.9	9.8	5.8	15.2
Portugal	6.4	5.8	6.9	13.0
EU/euro area	9.1	10.0	8.6	10.6

Fiscal balance (in % of GDP)				
Greece	-10.9	-6.9	-8.0	-9.3
Ireland	-7.1	0.9	-1.6	-17.6
Portugal	-5.8	-4.5	-5.1	-8.1
EU/euro area	-4.3	-3.3	-2.7	-4.7
Government debt (in % of GDP)				
Greece	64.1	99.9	107.4	162.1
Ireland	98.7	61.9	33.3	105.7
Portugal	59.2	54.7	65.6	109.5
EU/euro area	53.7	65.0	69.0	87.3
Current account balance (in % of GDP)				
Greece	-3.1	-3.1	-9.2	-7.5
Ireland	-2.7	1.6	-2.9	-2.1
Portugal	-2.3	-5.7	-9.7	-6.0
EU/Euro area	-0.3	0.2	0.0	0.4

Note: EU until 2001 (in general EU15), and euro area 2001–2012. Data comparisons until 1993/94 hampered by differences in sources and methodologies.
Sources: IMF World Economic Outlook Databases, European Commission's recommendation concerning the third stage of EMU, Convergence Report 1998, and European Commission economic forecast publications

1981–1993

Accession to the EEC became Greece's key foreign policy goal during the democratic transition from the 1967–1974 military junta, and membership arrived in 1981, helping to consolidate the still-fragile democracy. Negotiations were brief because EEC members welcomed an early accession, expecting Greece to implement the EU acquis to function efficiently within the EEC after membership – not before, as later demanded for newcomers. Professor Yannis Valinakis noted, "Even though a full member since 1981, as of today [2012], Greece has not yet fully organised and coherently coordinated its policy-making towards the European Union" (Valinikis, 2012). In 2010, it was the country with the longest overdue EU directives. Its overall 'Internal Market Scorecard' showed the highest number of internal market directives two years or more overdue: at 57, the most directives not timely or correctly transposed; and, at 94, the second most pending infringement cases (European Commission, 2010).

Soon after accession, the government changed when Pasok won elections on a largely anti-EEC platform. It wanted a 'special relationship' – where economic cohesion preceded political cooperation. It froze or dismantled reforms and administrative preparations, although it did soften its stance later in the decade when the EU extended cohesion policies and funds for agriculture, a dominant sector in Greece. The government also 'reformed' the public sector, replacing merit-based hiring criteria with social criteria, which entrenched patterns such as political patronage into civil service recruitment. A heavy state presence developed within the economy, giving prevailing political interests access to state resources and fostering a large ill-coordinated bureaucracy (Valinakis, 2012). Government spending on civil servants started to increase quickly as the public administration grew in size.

From 1981 to the mid 1990s, the Greek economy experienced a prolonged period of sluggish productivity and slow growth. Real GDP increased on average 0.7% per year, only about one-third of the average growth experienced in the EU (see Table 1). While the initial five years of slow growth could be explained by a general recession in EU Member States from 1981 to 1986, domestic factors were largely responsible for low growth in Greece in the remaining period. The substantially lower growth compared to its EU peers – and even to the EU average – took place despite noticeably more accommodative macroeconomic policies in Greece. In addition to budget deficits reaching double-digit figures, monetary policy conditions were accommodative with real interest rates in negative territory for prolonged periods. Conversely, long-term nominal interest rates climbed to historic highs, being above 20% in 1994.

Public debt increased to above 100% of GDP in 1993 from 23% in 1980, boosted in the later years by the central government taking over liabilities of various public legal entities to the banking system. General government revenues as a percentage of GDP increased to 27% from 22%, whereas the expenditure ratio rose almost 60% to 38% of GDP. The budget deficit rose to 11.3% of GDP in 1993 from 2.5% in 1980, the year before EEC accession and the last year until 2015 when Greece's budget deficit stood below the 3% threshold.

Increasing domestic imbalances and successive oil price shocks pushed Greece to ask its EU partners for a two-year stabilisation programme in October 1985. The programme sought to restore a sustainable balance of payments position and to reduce substantially the inflation differential between Greece and its main trading partners, including through a tightening of fiscal and monetary policies and a firmer income policy with a moderation of the wage indexation scheme to reflect projected rather than past inflation. An overall strict implementation of the 1985 programme produced impressive results, but following the completion of the programme, the government announced that its policy direction would change from adjustment towards development, and the macroeconomic policies were relaxed. Public sector wages grew faster than those in the private sector and the budget deficits needed to sustain high government spending contributed to rising inflation; from 1981 to 1993, the average inflation rate topped 18%, much higher than in Portugal or Ireland over the same period (Table 1).

A lack of transparency, rigidity in the labour and product markets, and cumbersome bureaucracy hampered foreign and domestic private investment. By the mid-1990s about half of public investments in Greece flowed from EU funds, helping to finance public enterprise investments, where economic health was questionable (Tsafos, 2013). Lacking foreign investment and expertise, Greek firms struggled to access the capital and the management skills needed to expand their small manufacturing base to improve export market competitiveness; during the 1980s, the export quota share of GDP dropped to 18% from 24%. In 1982, when most OECD countries were pursuing wage moderation, Greece introduced automatic wage indexation, which contributed to strong wage increases and lower profits, further hampering competitiveness.

The erratic economic performance stretched into the early 1990s. In late 1990 after another government change, Greece announced a medium-term adjustment programme, supported by a three-year EU balance of payments package that focused on fiscal consolidation and structural reform, targeting an ambitious reduction of inflation to 8% and of the fiscal deficit to 3% of GDP to prepare for eventual single currency participation. However, about a year after approval, that programme veered off track.

1994-2000

Greece's economic performance improved noticeably in the second half of the 1990s. Under the newly elected Pasok leader Costas Simitis (1996–2004), fulfilling the Maastricht criteria and joining EMU became a key priority – in line with Greece's Treaty obligations to its EU partners.

And this guiding star of EMU membership helped discipline policymaking, with monetary policy focused on attaining price stability. From the start of 1995, Greece pursued a hard drachma policy, with the central bank limiting the drachma depreciation to a rate that did not fully compensate for the inflation differential between Greece and its main trading partners in Europe. High official interest rates supported this price stability objective, as did comprehensive financial system deregulation. Bank of Greece efforts appeared to be supported by a tightening of fiscal policy, although later data disclosures and revisions painted these achievements as less impressive. After a 12.3% devaluation against the European Currency Unit, supported by additional budget measures, a tighter income policy, and an acceleration of both labour market and structural reforms, the Greek drachma entered the European Exchange Rate Mechanism (ERM) in March 1998 (Bryant, Garganas, Tavlas, 2001). The revised convergence programme aimed to fulfil the convergence criteria in 2000 and prompted improved macroeconomic policy discipline, including the granting of Bank of Greece independence.

Long-term interest rates fell sharply to around 6% in 1999 from over 20% in 1994. With public debt close to 100% of GDP, interest costs plummeted and helped reduce fiscal deficits, so hardly any structural fiscal reforms were needed to push fiscal deficits down towards the convergence criteria requirement. The reforms and better policy discipline – still falling short of EMU requirements – paid off. Greece's average growth more than quadrupled compared to the previous 13 years. In every year from 1996 to 2001, growth exceeded the averages in both the euro area and in the EU as a whole. Productivity growth went from around zero to an average close to 3%, also above the EU average, and fixed investments soared alongside a marked increase in non-residential business investment.

These impressive improvements across the economy meant Greece hit most successive convergence programme targets during the second EMU stage. But shortcomings and less-than-satisfactory developments also emerged. Bilkent Universty Associate Professor Dimitris Tsarouhas notes, ""Modernization" became synonymous with the need to Europeanize (i.e. reorganize, rationalize, and improve according to west European standards) various facets of public life … 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" (Tsarouhas, 2012). Part of the widening current account deficit "might have reflected underlying structural weaknesses and, to some extent, weaknesses in external competitiveness" (Bryant, Garganas, and Tavlas, 2001).

Despite stronger growth, unemployment kept rising. It reached 11.4% in 2000 from 9.6% in 1994, which contrasted with a small unemployment rate decline in the future euro area as a whole during the second half of the 1990s. With weak competitiveness and underlying structural weaknesses the current account deficit widened to a 6%-of-GDP deficit in 2000 from an almost-balanced position in 1994. Despite strong inflows from remittances and EU Structural and Cohesion Funds, such a deficit underscored the importance of promoting sound macroeconomic policies and effective structural reforms – becoming even more important given the pending removal of any option to adjust exchange rates.

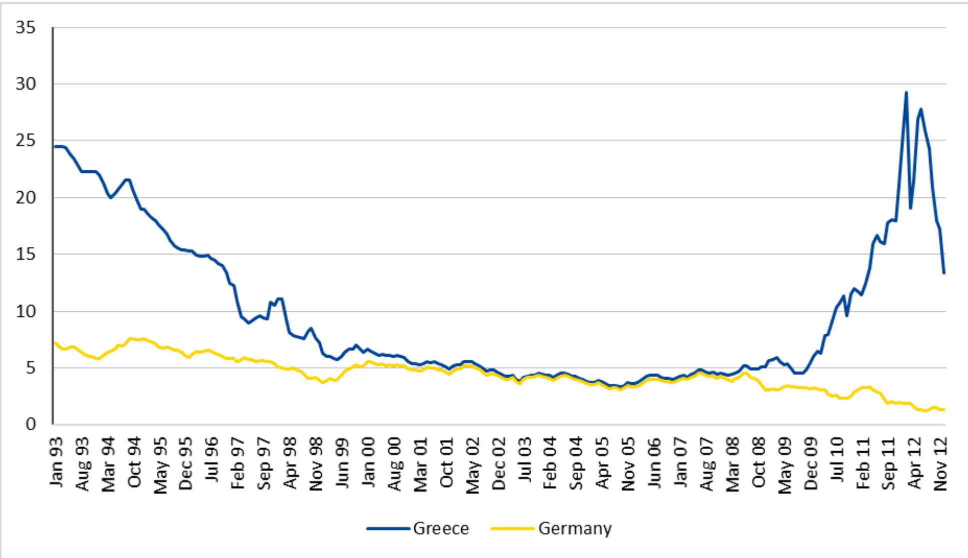
Greece progressed towards meeting the Maastricht criteria after its ERM entry and was admitted as the 12th euro area member in 2001. Membership criteria were assessed as fulfilled but caveats surfaced, notably at the ECB (ECB, 2000). Greece's inflation rate at 2% over the reference period was lower than the reference value, but the ECB noted, "due attention needs to be paid to the fact that the recent reduction in inflation rates is partly attributable to temporary factors". An indirect tax reduction and informal arrangements between the Greek government and enterprises to reduce selected retail prices partly explained the inflation decline (Herz and Kotios, 2000). The 6.4% long-term interest rate over the reference period stood below the reference value, as did the budget deficit at 1.6% of GDP. But public debt, at 104.4% of GDP, was far above the 60% reference criteria; although several other EU countries also exceeded the criteria. Nevertheless, the debt ratio was seen to be, "sufficiently diminished and must be approaching the reference value at a satisfactory pace." But this was also thanks to some legal, and expensive, transactions that aimed to reduce the recorded public debt. The ECB expressed concerns, noting that deficit-debt adjustments were still adversely affecting debt developments, such that public debt was only falling slowly despite high primary surpluses and privatisation receipts. The ECB worried, "whether sustainability of the fiscal position has been achieved" (ECB, 2000). It did not help that a definition of sustainability had never been established and that the market assessment – reflected in long-term bond yields – turned out to be insufficient.

Sustainability soon became a major issue and several years later it was found that the public finances were never even close to compliance with the Maastricht criteria.

2001–2009

The euro's introduction prompted further falls in long-term sovereign bond yields and a convergence close to those of Germany (see Figure 1).

Figure 1
10-year government bond yield: Greece and Germany
(in %, monthly average)



Note: Harmonised long-term interest rates for convergence assessment purposes (percentages per annum; period averages; secondary market yields of government bonds with maturities of close to 10 years).
Source: ECB

Markets basically were treating euro area members' sovereign debt as encompassing the same risks, supported by what turned out to be costly regulatory and collateral rules. Euro participation was considered irrevocable and, despite the Treaty's no-bailout clause, the markets expected that if any member encountered trouble other members would assist. Greek government interest expenditures fell to 5% of GDP by the mid-2000s from over 11% in the mid-1990s. In response, fiscal policy turned highly pro-cyclical as discipline waned with euro membership achieved. The budget and current account deficits widened once again. Escalating expenditures swallowed the euro-adoption windfall, as higher spending spread across pensions, wages, and other transfers, while the public labour force expanded. The conservative government from 2004 embarked on a spending spree similar to that of the 1980s. Pensions, wages, and social transfers increased by a clearly unsustainable 10% of GDP between euro adoption and the crisis eruption, a key economic development underlying the crisis.

Euro entry was treated similarly to a credit card with no limits and a very low interest rate. The access to cheap loans reduced pressures to cut public spending and expand revenues. Problems were deepening within the pension system with the government unable to implement reforms proposed in 2002. A more successful attempt helped in 2008 but still the pension system was becoming progressively underfunded, while the already-high number of public employees in Greece expanded even further after the country joined the euro. Defence expenditures touched 3% of GDP, a large outlay compared to other European countries, and substantial contingent liabilities accumulated as public enterprises used state guarantees to expand their borrowing.

Public expenditure's share of GDP rose more than seven percentage points from 2000 to 2009. Heavy spending supporting growth took place when Athens prepared for the 2004 Olympics, and as EU Structural Funds and the Cohesion Fund financed various projects. The revenue share fell to 39% of GDP from 42%, suffering from widespread tax evasion and an inability to collect overdue tax payments from large corporates. Researchers were estimating Greece's shadow economy at somewhere from 20% to 30% of GDP. Budget deficits increased to 15% of GDP in 2009 from 4% in 2000.

GDP growth rose to an annual average 4% from 2000 to 2007, the highest across the euro area countries, other than Ireland and Luxembourg, fueled by a housing boom that started in 1996. Historically low mortgage rates, mortgage securitisation, financial liberalisation, and easy credit helped triple real estate investment from 1999 to 2007. Supported by capital inflows from other European countries, the housing market share of GDP expanded to 12.5% from 6% and the availability of cheap credit prompted households to boost consumption, using credit cards, and consumer loans (Neubäumer, 2015).

During its membership of the EEC and EU, Greece has received support from the European Regional Development Fund, European Social Fund, the Cohesion Fund and structural support for agriculture, with average yearly EU transfers ranging from 2.4% to 3.3% of Greece's GDP. The European Commission estimated cohesion policies helped raise GDP 2.8% from 2000 to 2006, but impact evaluations demonstrated mixed results. Most studies found a positive correlation between EU funds and economic performance, but some have been more critical with a few analysts concluding the support did not improve growth in the recipient regions and countries. Some studies identify improvements in infrastructure and human capital, but other studies not. A weak institutional framework and capabilities, low planning capacity, cumbersome bureaucratic procedures, and a lack of experienced staff were often cited as factors delaying decisions and preventing progress. A 2018 study by Becker, Egger, and Von Ehrlich concluded that transfers tend to display immediate positive effects, but those benefits seem to vanish when transfers are discontinued. During the crisis, those effects were weaker than before, especially in countries where the crisis hit harder. The same authors showed in a 2008 study that only per capita GDP and not employment grew during the period in which transfers were allocated (Becker, Egger, and Von Ehrlich, 2008). Corruption made matters worse. "For instance, the EU Court of Auditors reached the conclusion that in several cases a significant percentage of total payments should not have been made in the first place" (Liargovas, Petropoulos, Tzifakis, Huliaras, 2016). Studies that highlight the importance of institutional capacity are consistent with empirical findings on the effectiveness of foreign aid to less developed countries (World Bank, 1998).

Late in October 2009, George Papandreou's newly elected Pasok government announced the 2009 fiscal deficit would likely be 12.8% of GDP rather than a previously estimated 3.6%. Such a large revision was unheard of but did not arrive without warning. Former Finance Minister George Papaconstantinou notes that Central Bank Governor George Provopoulos had privately alerted outgoing Prime Minister Kostas Karamanlis to a deficit that might hit double digits, and an EU Commission note discussed at the July 2009 Eurogroup meeting, based on first quarter data, said, "Should these trends continue over the year the central government deficit would exceed 10% of GDP, which contrasts with the official target for the central government of 5% of GDP" (Papaconstantinou, 2016). Eventually, the 2009 deficit exceeded 15% of GDP, (see Table 2). Earlier revelations about the warnings might have been helpful – and the absence of statistical reporting quality checks was worrying.

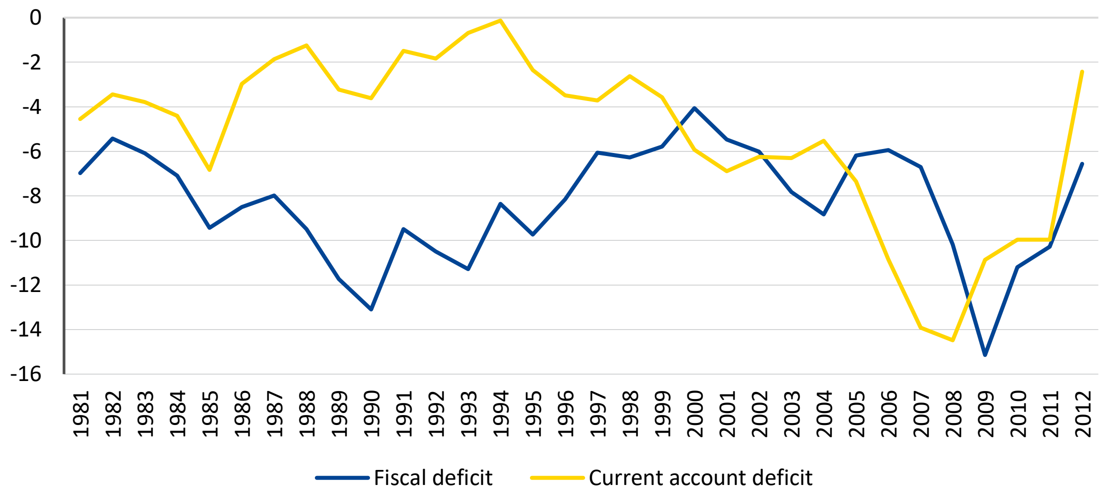
Table 2
Greece: Government budget data

	2001–2005	2006	2007	2008	2009
General government fiscal balance (in % of GDP)	-6.9	-5.9	-6.7	-10.2	-15.1
Structural fiscal balance (in % of potential GDP)	-7.7	-7.7	-9.1	-12.1	-15.0
Gross government debt (in % of GDP)	104.7	103.6	103.1	109.4	126.7

Source: IMF World Economic Outlook database

This large, and at first under-reported, fiscal deficit was an important underlying economic cause of the Greek crisis, together with an increasingly large current account deficit (see Figure 2) and the resulting foreign debt increases in the years after EMU entry. IMF calculations identified a sizeable 20% to 30% real overvaluation of Greece's exchange rate by 2009, with the balance of payments deteriorating sharply as the current account deficit widened to 14.5% of GDP in 2008 from 5.5% in 2004. And throughout the decade, inflation in Greece consistently ran some one to two percentage points higher than in its euro area trading partners, with productivity increases low and wage increases outpacing those of euro partners'.

Figure 2
Twin deficits in Greece
(in % of GDP, 1981–2012)



Source: IMF World Economic Outlook database

Vulnerability to the considerable external imbalance was consistent with a 'sudden-stop' theory, whereby capital flows grind to a halt when a financial crisis sharply reduces the risk appetite of investors. As discussed by Baldwin and Giavazzi, the absence of a central bank to provide lender-of-last-resort support to Greece amplified the sudden-stop fallout. Contributing factors were the predominance of bank financing, a vicious feedback loop between banks and sovereigns, and inflexibility in labour and product markets (Baldwin and Giavazzi, 2015).

Initial market reactions to the budget data disclosures were modest, but soon bond yields rose as a succession of rating agencies downgraded Greek debt. Investors characterised the EU Treaty as a block to any monetary financing of the deficit or intergovernmental bailouts. Strong resistance existed at the outset to the idea that Greece seek IMF financial support both in Greece itself and in other euro area states, but this view lost favour as interest rate spreads continued to widen and large debt amortisations approached. In April 2010, Greece formally requested IMF-EU assistance.

In the background, another deficit was accumulating, one less discussed – a deficit of values and institutions. In the words of Finance Minister Papaconstantinou, "Greece had reached a critical point as a country where mistakes, omissions, and the lack of political will to face up to decade-old problems had caught up with us. The catalyst was the fiscal derailment of 2009 and the blatant attempt to hide it. The Greek state had for a long time been spending more that it collected in taxes, borrowing the difference. With the borrowed money, consumers mostly bought imports. It was a wild party but it had come to an abrupt end" (Papaconstantinou, 2016).

2010–2012

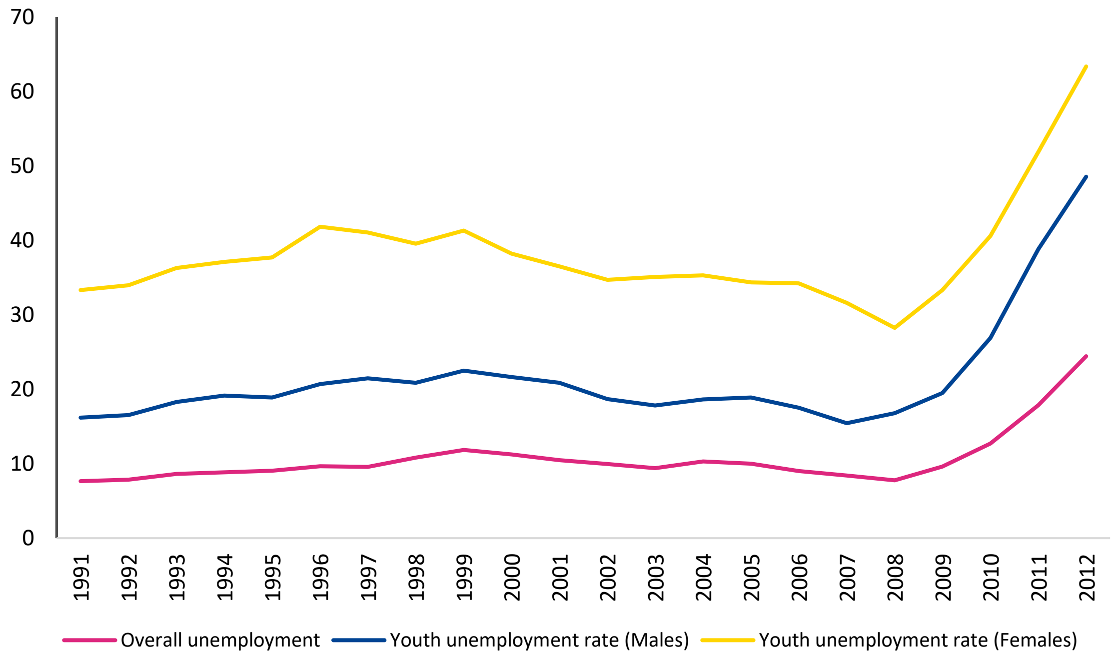
The IMF and euro area member states approved the first aid package of about €110 billion in May 2010, which envisaged an exceptionally strong frontloaded fiscal effort to bolster confidence and support a sharp internal devaluation, given that exchange rate and monetary policies could not be used. Public sector wages were reduced to spur wage moderation also in the private sector to help Greece regain market access and set the debt-to-GDP ratio onto a declining path from 2013.

The adjustment was brutal. Wage and pension cuts were the centrepiece of the programme, including eliminating '13th and 14th month' traditional bonus payments and undertaking far-reaching pension changes. This did achieve a large fiscal deficit reduction, but progress fell short of an ambitious adjustment package of 11% of GDP through 2013. The programme used indirect tax increases and expenditure measures to reduce public wages and social benefits, to eventually shunt the deficit below 3% of GDP. After an impressive start, achievements quickly fell short of targets, with more adjustments needed to maintain programme momentum. Important tax administration reforms encountered setbacks and only few signs emerged to suggest tax collection efficiency was improving. Privatisations disappointed, labour market reform slowed, and product market changes stalled. It all demonstrated how hard it would be to pursue ambitious structural reform when the economy was shrinking. Inadequate statistics remained an issue and Greece's administrative capacity proved to be more deficient than many thought; for example, Rolf Strauch, the euro area rescue fund's chief economist, pointed to Greece lacking a common state employee registry, so it was impossible to measure exactly how many civil servants there were (Wieser, 2019).

The programme projected growth would decline by 5.5% from 2009 to 2012, but it dropped an estimated 17%, although data revisions complicate comparisons. The IMF later said it felt the short- and medium-term growth payoffs from reforms were "in a highly optimistic range" (IMF, 2017). Also, the plan might have underestimated the fiscal multipliers and the exogenous negative impact of the crisis on aggregate demand.

The unemployment rate climbed to 25% rather than a projected 15%, with youth unemployment topping 50% for men and 60% for women (see Figure 1.3). And Greece experienced a brain-drain emigration wave with more than 100,000 people – mostly young, educated, and with professional experience – leaving in 2013 alone (Bank of Greece, 2016). Real GDP per capita in 2012 fell below that of 2000, the year before euro entry, with poverty and income inequality bourgeoning from 2010 to 2012.

Figure 3
Unemployment rates in Greece
(1991–2012)



Sources: World Bank Group, World Development Indicators

Financial sector vulnerability began to worsen, even though it had been assessed as relatively strong at the programme's beginning. Confidence drained away as the sovereign debt problem intensified, and the recession proved sharper than expected. Liquidity tightened when sizeable deposit outflows appeared, leading to substantial and extraordinary ECB support.

In October 2010, the Deauville EU Summit supported a permanent European crisis resolution mechanism to replace the European Financial Stability Facility (EFSF), including private sector participation, a move markets interpreted as preparing for a possible sovereign debt restructuring for euro area members.

In response, Greek bond yields increased sharply, rendering the prospect of Greece returning to international capital markets in early 2012 increasingly remote. Uncertainties and exit fears mounted as programme implementation in Greece weakened and doubts about continuing European partner support intensified. Greek domestic demand weakness accelerated sharply in 2011. Fixed investments fell about 20% and contingent liabilities associated with banking recapitalisation increased as the recession deepened. Greece's public debt could no longer be considered sustainable except with more considerable private sector involvement, which set the stage for negotiations with private creditors. Financial markets increasingly doubted Greece could maintain its euro area membership.

By early 2012, it was clear Greece would not regain market access anytime soon. The programme was cancelled in March 2012 and converted into an Extended Financing Facility

(EFF), with more emphasis on structural reforms and with a private sector involvement that had reduced Greece's total public debt by almost a quarter.

2. Surveillance with teeth – but too little bite

This chapter evaluates the effectiveness of surveillance in Greece, focusing on the years leading to euro area membership in 2001 and until the 2010 stand-by arrangement approval, mainly using IMF documents, but also European Commission, ECB, and OECD surveillance reports, together with the work of outside analysts.

International organisations' surveillance of Greece through the 1990s and 2000s suffered from a number of weaknesses, failing to address with perseverance, vigour, and traction accumulating macroeconomic imbalances and structural weaknesses that morphed into a full-blown capital account crisis when financing sources evaporated.

Insufficient enforcement of EU economic policy rules and thereby a weakened implied discipline also played an important role in the run-up to the crisis. Many market players believed EU membership safeguarded individual countries. A 'Europe-is-different' mindset developed, with an advanced country bias encouraging the idea that such countries were immune to a crisis. Europe would be expected to be able to handle its own problems, including regional weaknesses and over-exposed banking systems (Boorman, 2016).

To be fair, Greece was not the only case where the international organisations failed to warn about crisis causes and triggers. During the 2000s, policymakers worldwide were lulled into complacency, neglecting an accumulation of underlying flaws that rendered the global financial system vulnerable. An IMF Independent Evaluation Office report from 2011 looking at the IMF's performance during the crisis run-up, tried to establish why the IMF failed to presage the escalating risks, concluding that detection abilities were hindered in part by a uniform mindset that regarded a financial crisis in advanced economies as implausible. Group thinking and an organisational silo mentality offered little incentive to contrarian views (IMF, 2011A). Another evaluation noted a common IMF surveillance feature over the years was a tendency to side with positions or views held by country authorities. "The Fund's effectiveness as a guardian of global stability is being diminished if it moderates the candor of its analysis for political considerations" (Dhar and Takagi, 2016). This second paper offered examples of frank, candid-language assessments in internal papers that did not reach the attention of decision-makers. IMF staff could have considered delivering these messages in private, but experience shows such warnings only work when made public (Wolf, 2011).

IMF surveillance of Greece and other EU smaller countries often reflected the view – also prevalent in capitals – that the IMF could add little value to already-available, comprehensive EU and OECD surveillance. Complex arrangements and processes governing IMF euro area surveillance probably resulted in work deficient in depth, focus, and consistency, especially for smaller euro area members like Greece. This could be because IMF surveillance divided euro area members into two parts; one addressed common policies with missions to the European Commission and the ECB, the other addressed national policies. Within this process, possible spillovers and overall consistency dropped out of sight (Pisani-Ferry, Sapir, and Wolff, 2011).

The IMF official line before the January 1999 euro launch emphasised common currency advantages and only vaguely addressed concerns expressed in prominent academic literature, such as the incomplete institutional arrangement, including the lack of a common fiscal policy authority, and unfulfilled conditions for an optimal currency area. The IMF 1997 World Economic Outlook noted, "...the emerging policy framework appears to strike a good balance between rules and the necessary scope for the exercise of judgment in the implementation of policies".

In 1999, several IMF Executive Board Members discussing an external evaluation of IMF surveillance, "considered that there might be scope to reduce the size and duration of missions to these countries as European integration proceeds." They felt the European Commission, ECB, and the OECD closely monitored the countries already, although "other Directors were not in favor of diminished attention to the euro area" (IMF, 1999). Eventually, such 'downsizing' materialised in the 2000s when missions shrank, changed composition frequently, and reduced participation from the specialised policies and market departments (Dhar and Takagi, 2016). The skills of mission members often determined the detailed analyses undertaken rather than the needs of the countries under review, including Greece.

Internal EU coordination processes through the EURIMF also tended to dilute strong surveillance. While representatives from nearby countries in the region should have been well-equipped to provide solid peer pressure input to surveillance discussions, so helping sharpen IMF staff focus, the agreed EURIMF framework meant EU Board members were expected to align themselves to EURIMF Chair statements, in turn based on European Commission and ECB input. That conformed to official EU framework surveillance documents – no one wanted to wash 'dirty laundry' for the rest of the world to see.

Examples of surveillance with insufficient depth were the convergence reports ahead of Greece's euro area entry. The 2000 European Commission and ECB Convergence Reports focus in strikingly weak fashion on the sustainability criteria, probably explained by a belief that this would be captured by the long-term interest rate criteria. However, looking back, the markets clearly did not undertake due diligence. Also, the fiscal criteria paid too little attention to the quality of fiscal adjustment and focused more on numerical targets, arguably detrimental to convergence process sustainability. And the IMF assessment carried a congratulatory tone; the Article IV report's staff appraisal issued in late 1999 refers to the impressive achievements of the stability-oriented policy over the years to date, better-than-budgeted fiscal developments, and appreciable structural area advances. Such a positive assessment was hardly justified when considering that data revisions meant Greece was quite far away from fulfilling the fiscal criteria and only satisfied the inflation criteria by reducing indirect taxes. The sustainability of the convergence was later cast into serious doubt.

Some weak fundamentals did receive IMF attention, but warnings in later years varied in quality, had little impact, and did not address several issues sufficiently, issues that later proved to be key problems. Matters chosen for deeper analyses were not really the issues of greatest concern, possibly reflecting in part the mission team compositions, with several IMF mission chiefs feeling the topics selected often tended to reflect the skillsets of individual economists.

After Greece entered the EMU, the IMF did warn about the large widening current account deficit and questioned the authorities' suggestions that it could be explained by fundamentals. It recommended more fiscal consolidation to meet SGP requirements and endorsed social security and pension reforms to foster sustainable medium-term public finances. It also repeatedly supported structural reforms to promote growth and convergence. The IMF frequently referred to weaknesses in the statistics supplied (Wyplosz and Sgherri, 2016). On the other hand, structural reforms were almost always cast in a positive light, even though Greece implemented very few substantive improvements. Too little attention focused on deeply entrenched obstacles. "IMF staff tended to praise the authorities for any reform announced or implemented without assessing its impact" (Dhar and Takagi, 2016).

External imbalance analysis tended to focus on the way competitiveness was diverging across the euro area. It often ignored the financing side and the way strong domestic demand growth was driving the imbalances rather than weak exports. Little, if any, attention was paid to the spillover risk to other euro area members from the concerns accumulating in Greece. Left broadly unaddressed were the risks of changes in investor sentiment, sudden stops, and a sovereign debt crisis in Greece and how it could affect the other countries.

Surveillance reports did not underline vulnerabilities arising from the brisk bank lending to Greece from other euro area countries, and financial sector reports such as the 2006 Financial Sector Assessment Programme (FSAP), tended towards the congratulatory, concluding that banks were well-capitalised, profitable, and appropriately supervised (Véron, 2016).

The IMF placed insufficient focus on risks stemming from increasingly high debt, an appreciating real exchange rate, and higher unit labour costs – all requiring consequent competitiveness adjustment – preferring to believe euro membership would render the challenges less severe and easier to manage (Pisani-Ferry, Sapir, and Wolff, 2011).

Surveillance report language was often vague, general, and convoluted. It tended to be complimentary in tone and commend some improvements while talking of remaining challenges. The reports lacked sufficient specific policy response prompts, and recommendations often arrived without priorities and lacking impact assessments. Moreover, such recommendations carried a caveat to suggest euro area membership protected individual participating states from external financing difficulties, which clearly removed an important disciplining factor. That external financing disclaimer appeared in a 2008 Article IV report issued when Greece's current account was estimated to have reached 14% of GDP, which toned down the discussion on the risk of transmitting vulnerabilities to other euro area members. Instead, the report only carried subtle warnings about how accumulating large deficits might intensify vulnerability to possible market-sentiment reversals and higher funding costs.

A major concern of the surveillance for Greece was insufficient attention to perennial structural impediments such as corruption, an unfavourable business environment, and a crisis of values (addressed in Chapter 5.) During the 2000s, IMF reports flagged the importance of dealing with entrenched corruption and a deep-rooted tax evasion culture – to little effect. Technical assistance was on offer but would probably have had little impact given the lack of Greek political willingness to build capacity and implement the advice. The OECD, too, had raised similar concerns during the 1980s and Tsafos in 2013 notes tax evasion was increasingly mentioned in the reports as it became more political; "After a lull it got ~13 mentions per survey from 1986-1996…In 1985 and 1989, both election years, revenues as a share of GDP dropped by half a percentage point, halting an otherwise steady increase" (Tsafos, 2013). However, little suggested the OECD recommendations were being acted upon. Focus on the advice offered seemed somewhat arbitrary and recommendation follow-ups were not always ensured.

IMF staff frequently identified weaknesses in the data and questioned their reliability, notably in the 2003 and 2005 Reports on the Observance of Standards and Codes (ROSCs). These concerns found their way into the 2004 Article IV Report. The 2006 ROSC recorded as especially severe problems in fiscal reporting and in public financial management. But the subsequent Article IV reports did not reflect these concerns adequately so although repeated, the concerns tended to be downplayed in reality (Pisani-Ferry, Sapir, and Wolff, 2011). No action was taken about a 2004 misreporting of fiscal data.

The impression remains that very few sustained policy corrections emerged even after surveillance reports diagnosed vulnerabilities, so the surveillance impact in Greece – as in many countries – proved less than satisfactory. What was needed was traction – progress in convincing policymakers to work together to achieve sustainable stability and growth – but in Greece governments seemed in general preoccupied with blame games after taking office rather than in seeking broad consensus.

Communications to the wider public about the growing imbalances and the needed policy response did not garner much attention. Missing were an insistence on key messages, an assessment of the impact of recommendations, and follow-up with perseverance until the issues had been addressed.

The surveillance focused on macro-critical aspects of developments with a strengthened emphasis on macro-financial linkages and spillovers after the crisis erupted. This meant that the political economy aspect attracted less attention, except for corruption in rather general terms. When political economy matters were discussed and monitored the focus alighted mainly on quantitative developments such as law changes and institutional developments, with less discussion about the need to change qualitative aspects in underlying cultural and social values – anyway a rather tall order given the existing macroeconomic surveillance commitments of international institutions. When contrasting the 2018 Article IV IMF surveillance report and the June 2019 European Commission enhanced surveillance report, the IMF does seem to have raised awareness about corruption's negative impact, whereas the European Commission is rather vague and mostly addresses legal matters (European Commission, 2019). The IMF did indeed report cases of public officials facing criminal charges for official capacity actions, which it said could undermine data integrity and the independence of public institutions, or perceptions about such detachment.

Surveillance recommendations are grounded in the economic data and forecasting models. As noted in a 2012 analysis on European Commission forecast accuracy by Cabanillas and Terzi, real GDP forecast accuracy for Greece has been poorer than for most other countries, probably linked to the exceptionally high uncertainty surrounding the country's prospects since 2008. General government balance forecasts for Greece (and Ireland) stand out as particularly inaccurate. Inflation forecasts and forecasts for total investment were also relatively poor for Greece. The Commission's track record has been similar to that of the OECD, IMF, and Consensus Economics. The comparison of forecasting performance across institutions since the beginning of the crisis shows that the deterioration in forecast accuracy was a common phenomenon (Cabanillas and Terzi, 2012).

Fortunately, lessons learned from surveillance before the crisis helped implement a vital IMF overhaul that strengthened internal culture. The European authorities recognised EU surveillance shortfalls too, triggering a revamp of the surveillance architecture expanding it beyond the fiscal area to the financial sector and external imbalances. Euro area surveillance became more energetic after the crisis erupted, especially following the IMF's 2011 comprehensive triennial surveillance review and the application of an Integrated Surveillance Decision from 2012. The ECB says that, "Messages became more consistent and focused, and linkages and spillovers among member countries are better accounted for…there is better integration of surveillance at the bilateral and euro-area wide levels and with multilateral exercises…The IMF has also significantly improved its analysis of risks..the coverage of financial stability issues has been expanded" (ECB, 2015). Nevertheless, the focus on underlying public and private sector inefficiencies still looks too limited, at least during the period of this analysis.

3. The first programme for Greece 2010–2012 – a costly holding operation

The stand-by arrangement approved in May 2010 was the first IMF programme ever for a euro area member, with the largest amount compared to the quota for any IMF member in its history at 3,212%. It was the first undertaken within the Troika model that brought together the IMF, the European Commission, and the ECB, whereby financial assistance agreed by euro area countries became part of a joint package. Within the package, the IMF committed to a €30 billion stand-by arrangement and the Eurogroup agreed to provide bilateral loans totalling €80 billion pooled by the European Commission under the Greek Loan Facility (GLF).

The programme has been subject to various evaluations, notably the IMF ex post programme assessment (IMF, 2013), the IMF's Independent Evaluation Office review of crisis programmes in Greece, Ireland, and Portugal (IMF, 2016), and various analyses from academics. This chapter also benefits from the views of Greek officials who contributed to the ex post evaluation (IMF, 2013 Appendix 1), numerous background papers, and the perspectives of commentators.

General agreement suggests the programme was a success in some areas although the list of programme problems is long. Accomplishments include avoiding a disorderly default, with Greece remaining in the euro area as it wished. The country managed to achieve a strong fiscal consolidation in numbers and put its pension system on a more viable footing. The programme also helped contain negative spillovers or promoted necessary policy adjustments in other euro area countries, known as positive contagion. And the arrangement bought the time needed to build stronger regional and global firewalls, take steps towards a banking union, ensure better euro area risk-sharing arrangements, and strengthen fiscal rules and reduce vulnerabilities.

The time allowed for a broader strengthening of EU economic governance through monitoring, prevention, and correction, including the 'Six Pack,' a series of EU measures to strengthen the SGP and intensify macroeconomic surveillance, that entered into force in December 2011. Also, 25 of the then 27 EU Member States signed a more ambitious Fiscal Compact in January 2013.

However, the programme did not deliver the desired improvement and was off track by early 2011. Attempts to wrench it back on course that included extra fiscal measures from 2011 failed. IMF Director Poul Thomsen said, "With no more low-hanging fruits, quality of measures began to deteriorate. We [the IMF] became increasingly concerned that the adjustment – while extraordinary – was being achieved in a growth unfriendly and unsustainable way" (Thomsen, 2019). Little political will existed to reform the overgenerous pension system and to broaden the exceptionally low tax base. The programme was cancelled in March 2012.

This delay to structural reforms meant neither market confidence nor the investment climate improved enough to reach a sustainable position. Peculiarities in the Greek export structure hindered any external adjustment because only a small part of Greece's exports depended on competitiveness. A 2014 paper on the puzzle of missing exports said, "While Greece has already achieved major improvements in cost competitiveness since the start of the Greek adjustment programme, structural reforms must also address non-cost competitiveness factors such as the underlying institutional deficits to unlock Greece's export growth potential" (Böwer, Michou, and Ungerer, 2014).

In 2012, real GDP was languishing more than 10% below the programme baseline, with the unemployment rate about 10 percentage points higher at above 24%. Greece's competitiveness had improved a little but the structural reforms needed to enhance growth were scarce and productivity gains imperceptible. The lack of progress meant Greece's banks lost more than 30% of their deposits. Private sector involvement also proved elusive, despite pushes early on from the IMF, until banks and other investors eventually contributed by writing down some of the debt holdings in early 2012 within a private sector involvement programme.

Key lessons from the first programme, and explanations on what went wrong, include the following:

[1] Key assumptions were over-optimistic and downside risks materialised in an environment of political instability and shrinking bank deposits. The over-optimistic assumptions included a fiscal multipliers setting that was too low and underestimated price and income elasticities that reduced public revenues. The too-low estimates of the crisis impact on demand meant fiscal adjustment pushed the economy further under water. Multipliers were adjusted as reviews steered the programme. Historically, mixed evidence has charted the degree to which IMF forecasts are systematically biased. Aslund (2013) has identified a tendency to underestimate growth at the beginning of programmes, and then underestimate a pick-up when recovery materialises. The IMF’s 2011 Conditionality Review concluded that growth projections for programme countries in the conditionality review did not show bias overall, although previous studies had suggested an optimistic bias. The IMF’s Independent Evaluation Office 2014 forecast report concluded that short-term GDP growth and inflation forecasts within IMF-supported programmes were unbiased in most cases but tended to be optimistic in high-profile programme cases characterised by exceptional access, and over-predictions of GDP growth tended to arise during regional or global recessions (IMF, 2014). The IMF seems to have consistently underestimated the initial collapse of demand/output in major capital account financial crisis cases. In terms of growth, the IMF was slightly more pessimistic than the (May 2010) Consensus Forecast around the time of programme approval.

[2] The depth of programme ownership by the key political parties and the population and the capacity and political will to implement key structural reforms were overestimated. Within government, some politicians even distanced themselves from the programme measures. The fast-track negotiations offered precious little time for internal dialogue and consultations, including at the administrative level, and insufficient emphasis was placed on explaining the programme and its requirements to the public. Vested interests resisted progress in privatisation, public sector downsizing, and labour market reforms. Internal IMF documents recognised the problem, noting that such interests had already fiercely opposed structural reforms (Wyplosz and Sgherri, 2016). To some degree, successive governments blamed the outside world for hardships under the adjustment programmes, diverting focus away from the way the Greek authorities had not kept their own house in order, a key explanation for the hardship. The IMF tried to argue from the start that there was insufficient parsimony in the structural requirements and the number of structural conditions expanded considerably as the programme progressed, reflecting a growing recognition of entrenched administrative capacity weaknesses and insufficient political priorities to engender change. However, the idea that a narrower more-focused structural agenda would have produced much better outcomes is open to doubt.

[3] The adjustment burden fell unequally across different parts of society, contributing to inadequate programme buy-ins. For example, hardship-sharing by public and private sector employees was different, with the overstaffed public sector only committed to ensuring 20% of those retiring were replaced, whereas the private sector endured widespread job losses thanks to inflexible wage setting. A lack of progress in checking high-income earners’ tax evasion also dented any feeling that tax burden equity was improving. The IMF stated, “the lack of political will to make clear progress was nonetheless a considerable obstacle to the program’s success” (IMF, 2013).

[4] The overestimations of implementation capacity led to frequent programme implementation slippages. When laws changed, follow-up did not ensure full implementation, with results tracked and analysed. The delivery of IMF and EU Task Force technical assistance suffered from limited absorption capacity in Greece, while EU partners criticised the IMF for insufficient focus on providing hands-on training.

[5] The IMF and other creditors needed to be more sceptical about official data quality, given continued revisions, including another upward revision of the 2009 fiscal deficit by about two percentage points of GDP. By moving the starting point, these revisions did not render the adjustment easier.

[6] The programme focused excessively on raising revenues rather than on cutting expenditures. After all, the fiscal crisis had been mainly expenditure driven. The programme also placed insufficient commitment at the outset on privatisation. Despite a lack of progress, the fourth programme review envisaged privatisation receipts from €10 to €50 billion, which was unrealistic and became a virtual admission of an underfinanced programme.

[7] Some officials argued that it would have been preferable to have moved immediately into an IMF EFF arrangement in 2010, as with Ireland. However, insufficient firewalls at the outset and a lack of structural reform capacity favoured a shorter arrangement focused on macroeconomic adjustments.

[8] The IMF/European Commission/ECB Troika was initially beset by coordination problems and sometimes insufficient team continuity. Also, the European Commission suffered decision-making process fragmentation. All the Troika partners had some misgivings about elements of the arrangement, but eventually a broad consensus agreed the Troika mechanism promoted efficient coordination. Greek authorities seem to feel that if the European Commission and the ECB had had the necessary technical expertise for financial programmes, it would have been better to have dealt with them alone in the crisis, without an IMF lending involvement.

[9] Some have argued that the massive fiscal deficit reduction was too ambitious and reflected a too legalistic and unrealistic euro area focus to extract Greece from the excessive budget deficit procedure. A flatter adjustment path would, however, have required more financing than politically feasible. The size of deposit outflows was underestimated, complicating programme financing. A much sharper output contraction then demanded additional measures, which initiated a vicious cycle of need for additional measures and further output contractions.

[10] IMF and EU rules and principles were circumvented, raising the risk of moral hazard by yielding to political pressure. Concerns have been raised about insufficient IMF Executive Board involvement in decisions, leaving them only with a pro forma role in key decisions, including those on debt sustainability issues. The absence of a transparent decision-making process with open discussions of options brought about politically driven decisions and a lack of democratic legitimacy and accountability. At the IMF, officials amended the criteria that governed exceptional access at the very last minute to allow for exceptional lending to a country, even though the chance of regaining the required market access within the programme time horizon was remote. This policy change was not discussed by the Board or even disclosed until a staff report circulated. Also, EU rules were bent in two areas. Financial assistance from other Member States was provided despite the no-bailout clause in Article 125 of the Treaty on the Functioning of the European Union (TFEU). The Court of Justice of the European Union (CJEU) later ruled that this article "does not prohibit the granting of financial assistance by one or more Member States to a Member State which remains responsible for its commitments to its creditors provided that the conditions attached to such assistance are such as to prompt that Member State to implement a sound budgetary policy" (Pringle case, CJEU 27 November 2012). Furthermore, TFEU Article 123 prohibiting monetary financing by the ECB and national banks was compromised, with the ECB endorsing sizeable exposures to Greek sovereign bonds. European banks were heavily exposed to Greece and several other highly indebted euro area members, so contagion fear was high, which

prompted the willingness to amend the interpretation of rules and make exemptions to the already exceptional circumstances framework. The fear of moral hazard was being trumped.

It remains open to dispute whether an upfront debt restructuring should have been pursued. Some IMF staff and stakeholders preferred this route, as did many academics and private sector observers. Some even found it unavoidable. Professor Nouriel Roubini, respected as one of a few prominent economists that forecast the global financial crisis, wrote in a June 2010 Financial Times opinion piece, "It is time to recognise that Greece is not just suffering from a liquidity crisis; it is facing an insolvency too…The €110 bn bail-out agreed...only delays the inevitable default and risks making it disorderly when it comes" (Roubini, 2010). Roubini drew parallels with Argentina's crisis from 1998 to 2001, which culminated in a disorderly default, noting Argentina's fiscal and current account deficits at the crisis onset were less severe than Greece's. Roubini concluded that "If Argentina was insolvent, Greece is insolvent to the power of two or three" and suggested public resources would be better used to help ring-fence other crisis-prone euro area countries.

Private sector involvement, often through maintaining creditors' existing exposures, had been part of other programmes, including during the Asian crisis and more recently through the Vienna Initiative that encouraged foreign banks to maintain credit lines during some Eastern European IMF programmes. Without firewalls to guard against unwarranted contagion, ex ante debt restructuring was not politically feasible in Europe and faced resistance also from other IMF members. Greece and its euro area partners were opposed, given contagion concerns; in Greece, worries stemmed from domestic political costs, insufficient funds for bank recapitalisation, and implications for social security funds. Still, the decision not to seek debt restructuring at the outset left the debt sustainability concerns unaddressed during the programme, magnifying the required fiscal adjustment and causing a sharp output contraction. Already weak public support for the programme waned. And the ability to respond to negative shocks or set aside contingencies to allow private creditors to cut their exposures became constrained. This politicised the debt issues and reduced the amount of sovereign debt eligible for haircuts when implemented in 2012. So numerous arguments would seem to support an earlier debt restructuring, although the consequences of such a counterfactual are impossible to assess. As Thomsen said, an earlier private sector involvement while surely desirable "would not fundamentally have prevented the adverse debt dynamics that began to emerge as a result of the much-larger-than expected output contraction" (Thomsen, 2019).

With the benefit of hindsight, it is, as Wyplosz and Sgherri note in 2016, "debatable whether the program ever met the Fund's fourth criterion for exceptional access (i.e., a reasonable strong prospect of the program's success, taking into account institutional and political capacity to deliver adjustment)". It seems doubtful that at any point any broad-based will existed amongst politicians or the Greek public to embark on the necessary reform of malpractices to promote efficiencies in the public and private sectors. The accumulated costs were huge. The deep output contraction took real GDP per capita in 2012 to a point lower than at the time of Greece's EMU entry in 2001. The country had lost more than a decade of economic growth and opportunities and was still not out of the woods – as coming years would demonstrate.

4. The Greek data crises

A Eurostat disclosure of misreported fiscal data shortly after the Pasok government took office in 2009 helped trigger Greece's economic crisis. It showed the government debt and the deficit as severely underreported in the years from 2005 to 2008 and in the 2009-year forecast. Revisions completed in November 2010 were particularly extreme for 2009, raising a 3.7%-of-GDP deficit reported in the spring of 2009 in a series of steps to eventually reach a stunning 15.4% of GDP, with the debt revised upward to 126% of GDP from 100%.

The European Commission did not take these revisions lightly, with the Ecofin Council requesting clarity on "the renewed problems in the Greek fiscal statistics." A subsequent January 2010 report delivered a harsh verdict, noting, "Revisions of this magnitude…have been extremely rare…but have taken place for Greece on several occasions" (European Commission, 2010a). The report referred to weaknesses of method and political interference, with the quality of fiscal statistics subject to political pressures and electoral cycles. It described inappropriate governance, poor cooperation, diffuse personal and institutional responsibilities, ambiguous staff empowerment, and a lack of written instructions and documentation. Following consultations with the Greek authorities, the IMF concluded the data misreporting reflected serious institutional shortcomings. Remedial action to prevent any more misreporting included approving a law to grant the Statistical Office independence, something the IMF had been recommending for years. Eurostat accepted Greek government statistics without reservations from 2011 to 2015, but the IMF said later the independence of the Hellenic Statistical Authority (ELSTAT) "continued to be challenged by vested interest ... raising doubts about the underlying commitment of the country to truly independent statistics and pointing to risks of re-politicization in the future" (IMF, 2016a).

The 2009 event marked the second severe fiscal data crisis in Greece within a few years, despite sustained efforts by the IMF and Eurostat to raise the fiscal data quality to the level of other Member States. Eurostat had discussed statistical budgetary issues for years with the Greek authorities, far more frequently than with any other Member State, and numerous footnotes appeared to state reservations about the quality of Greek budget data.

In 2004, Greece undertook exceptionally large revisions of its budgetary data, leading a Eurostat report that year to conclude that data for Greek fiscal deficits and debts had been misreported since 1997. Never over the years since 1995 had the deficit fallen below 4% of GDP, and from 1999, the government debt ratio had been on a rising trajectory. A May 2000 Convergence Report estimated a 1.6%-of-GDP deficit for 1999, but this eventually rose to 5.8% of GDP following Eurostat actions and a fiscal audit required by the incoming Spring 2004 Greek government. It meant Greece never fulfilled the Maastricht criteria in this area (Table 3). By January 2010, Eurostat had undertaken 10 Excessive Deficit Procedure visits to the country, expressing five reservations about the data. This included a number of methodological visits that are only undertaken, "in exceptional cases where significant risks or problems with respect to the quality of the data have been clearly identified" (Council Regulation (EC) No 479/2009, as amended).

Table 3
Greece: Budget data revision before EMU entry

	Government budget deficit (in % of GDP)		Government gross debt (in % of GDP)	
	2000 Convergence reports	Final	2000 Convergence reports	Final
1997	-4.6	-6.1	108.5	99.5
1998	-3.1	-6.3	105.4	97.4
1999	-1.6	-5.8	104.4	98.9
2000	-1.3	-4.1	103.7	104.9

Sources: 2000 Convergence reports by the European Commission and the ECB, and the IMF World Economic Outlook database

In contrast, the IMF on many occasions delivered rather subdued, sometimes even complimentary, assessments on the data quality. It offered only a few examples of more direct critical assessments such as in the concluding remarks after the 1998 Article IV discussion. With all sails set to meet the Maastricht criteria, at the IMF "Directors expressed concern about the serious shortcomings affecting Greece's economic data, and the extent to which this complicated the assessment of economic conditions. They entreated the authorities to strengthen their commitment to early and substantive improvements in this area" (IMF, 1998).

In later years, the IMF was generally overappreciative, typically welcoming improvements and suggesting data was adequate for surveillance, while also identifying areas for improvement. The 1999 Article IV Consultation noted Greece "commendably ranks among the few Fund member countries that have completed a self-assessment in relation to the IMF Code of Good Practices on Fiscal Transparency-Declaration on Principles" (IMF, 1999a). Later, the Greek authorities were congratulated for subscribing to the more demanding Special Data Dissemination Standard in 2002 and completing a Report on Observance of Standards and Codes (ROSC) in 2003.

The 2016 IMF Independent Evaluation Office report 'Behind the Scenes with Data at the IMF' reminded that the 2003 ROSC report praised all Greek agencies for demonstrating professionalism and adopting transparent practices and policies. The IMF did not identify major misreporting issues between 1997 and 2004 regarding military expenses and social security surpluses. However, the IMF did inquire about "large below-the-line operations and stock-flow discrepancies" (IMF, 2005). Even after the 2004 misreporting crisis, staff maintained an overall positive line (IMF, 2016a) and only sharpened their tone after the 2009 data corrections revelation.

Ensuring adequate data remains very much a work in progress, with the 2017 Article IV report stating, "Revisions of national accounts and fiscal data are frequent, significant, and consistently biased to the downside, and continuing discrepancies in fiscal reporting remain" (IMF, 2017). The more recent 2018 Article IV Report says, "Nonetheless, there remain important weaknesses, which include significant gaps in the fiscal source data" (IMF, 2018).

The mixed progress conforms to the general view that, "for a time after a crisis, data issues are front and centre…but this attention to data tends to wane after a while, as data becomes once again an afterthought" (IMF, 2016a).

5.Political economy aspects – persistent corruption and a crisis of values

The Greek crisis reflected many years of inefficient spending, maladministration, deep-rooted structural distortions and widespread corruption. These root causes of the crisis were not sufficiently addressed, even when Greece repeatedly found itself close to an economic abyss. Since Greece had suffered from particularly weak institutions and political cynicism for years, trust between the state and its citizens was very weak.

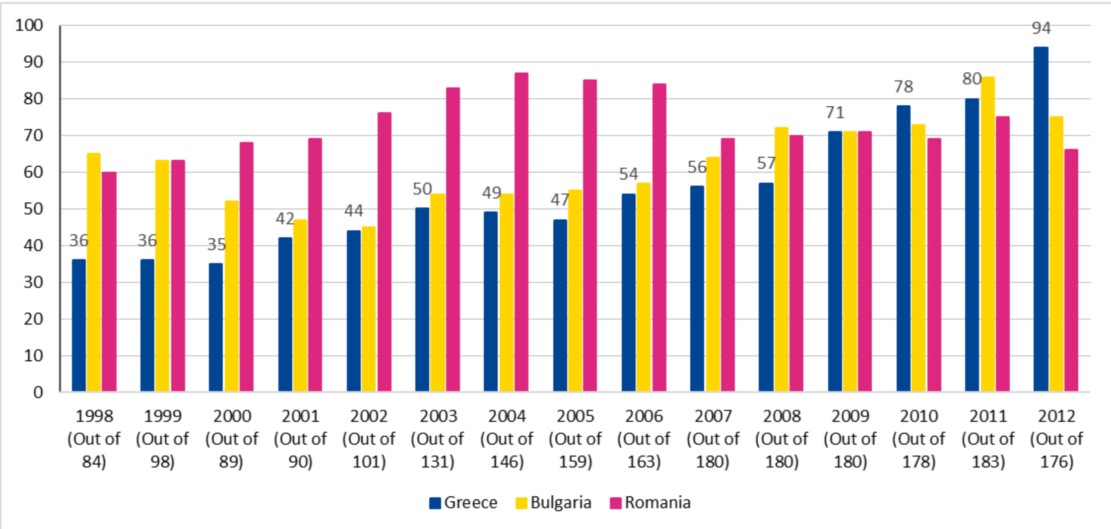
The costs and consequences proved severe. As Nobel Prize winner Paul Romer said, “Corruption and bureaucratic inefficiency act like the worst kind of tax – one that deters economy activity without raising any revenue” (Romer, 2010). Corruption ran rampant across the country, more so than in any other EU country (Transparency International, World Bank, European Commission).

A stunning 98% of Greeks asked told the 2012 EU corruption Eurobarometer survey they regarded corruption as a major problem, widely believing it permeated all the country’s institutions. Greeks were the most likely of all Europeans to consider corruption as more widespread in their country than anywhere else in the EU and felt it had intensified to the point where it had become a natural part of business culture. And only one in 10 Greeks regarded corruption prosecutions and punishments as adequate (European Commission, 2012).

Transparency International’s annual Corruption Perception Index persistently ranked Greece as the most, or one of the most, corrupt EU countries a quarter of a century after joining the EU, and a decade after becoming a euro area member. Even in the midst of the crisis, Greece slid several spots down the ranking in 2012 to 94 out of 176 countries listed, compared to its already relatively weak 2011 position (Figure 4). That was by far the worst performance of any EU country and nearly 20 positions below Bulgaria, although a change in methodology complicates the comparison.

Transparency International’s 2012 report on Greece stated, “Corruption is the source of numerous malfunctions in Greece… Greece suffers from abundant corruption mainly in the public sector…it is not only the relevant legal framework that needs to be amended, but above all the mentality that preserves corruption” (Transparency International Greece, 2012).

Figure 4
Corruption Perceptions Index rankings
(1998-2012)



Note: The number of countries included for each year is listed on the x-axis. Due to a 2012 update in the methodology, 2012 scores are not comparable with earlier scores.
Source: Transparency International database

When this report was published, it carried comments from Costas Bakouris, the President of Transparency International Greece, who said, “We all know about the debt crisis, but Greece is also suffering a crisis of values. It has the right laws in place but does little to enforce them. The law is being violated, the illegal is being legalized, and the international commitments to fight corruption are being ignored. The laws are there, and institutions already have teeth – they just need to bite.”

The study described a broadly adequate legal framework that embraced ratification of international treaties aimed at eradicating corruption and had established numerous anti-corruption agencies. But the number of such agencies looked disproportionally high given the volume of audited material – and they hinged on political agents. Consequently, corruption across Greece was detected neither thoroughly nor quickly.

The Transparency International Greece study said progress would depend on improving legal frameworks and strengthening institutions, but even that would be far from sufficient. It offered a strong reminder that counter-corruption progress demands that people embrace the spirit of change, not just establish changes on paper.

Former Greek Finance Minister Papaconstantinou has suggested that to improve institutions and implementation capacity, the World Bank rather than the IMF should have been involved because the IMF lacked the World Bank’s capacity to provide the required institutional reform support. “I know it is not politically correct to say so, but Greece was more of a World Bank case than an IMF case. It needed serious support for institutional reform. Not just the task force that came to help us, not just the very good technical assistance from the IMF, but much more long-term, deep institutional reform to be able to implement this” (Wallace, 2017).

Transparency International’s 2012 study covered about three years and was the first such study undertaken in Greece – something of surprise given that other countries had completed the exercise already. The report discovered that in Greece the poor corruption position arose partly because the state created conditions that tolerated non-compliance with the law. The study claimed that the state in certain cases not only legalised breaches of law but sometimes even directly encouraged non-compliance. This eroded trust between the state and its citizens, spreading a crisis of values that, “imbued the country’s mentality and the institutions” and hampered social justice, “since it is people of low income who are affected more in this environment” (Transparency International Greece, 2012).

The study identified a ‘triangle of interplay’ in Greece linking the executive, the media, and business that weakened resistance to corruption. Former IMF Alternate Executive Director Thanos Catsambas, notes a, “notorious interrelationship of vested (and frequently illegal) interests among the Greek political elite, entrepreneurs, and the barons of the Greek media is well established. There is perhaps no field that better illustrates how deeply ingrained clientelism is in Greek political culture than the media sector. Politicians, media moguls, and entrepreneurs have long been operating as a ‘triangle of power’, where business and political interests are intertwined in what has aptly been referred to by the Greek word diaploki (entanglement)” (Catsambas, 2016).

As an example of diaploki, Catsambas pinpoints the facilitation of loans to media moguls from state-owned banks, the publication in return of supportive editorials and flattering broadcast interviews for Greek politicians, then the granting of business contracts, since media moguls are also often business oligarchs. Catsambas describes how mainstream media thereby became ‘partners-in-crime’. He notes that the crisis showed how the mainstream media was uninformed on economic concepts and on the operational framework of international organisations. “An informed public would make better decisions,” he said. Evidence suggested that in the first years of crisis, Greece’s troubled media sector deteriorated, with a Reporters Without Borders report showing Greece toppled down more than 50 places in the press freedom index in the world media rankings from 2009 to 2014, reaching 99th place in 2014 (Reporters Without Borders, 2014). Media did not do an adequate job in helping communicate the severity of the accumulating macroeconomic and financial imbalances to the public, or the need for policy change.

With regards to businesses, Transparency International noted that only businesses listed on the Athens Stock Exchange met international corporate governance standards, with others operating in an almost completely non-transparent manner. It described worrying issues such as public administration dependence on political parties, broad discretion to exercise public authority, a dysfunctional democracy, absent audits and sanctions, a general lack of transparency, and a weak rule of law. As a result, it reported 92% of the population considered Greek society to be corrupt.

Transparency International Greece showed a large part of the population in the country accepting some general corruption practices, such as giving money to obtain a driver's license; paying tax offices to settle tax debts; bribing public servants to obtain building permits; paying policemen to avoid traffic offence tickets; giving a doctor money in return for better healthcare; and using influence to secure employment for a family member. (Transparency International Greece, 2012).

These widespread practices fall under the concepts of fakelaki, or bribes in little envelopes that affect a large part of the society, and rousfeti, or expensive political favours that infiltrate activity such as hiring decisions and property deals. Also, many ministries had 'special accounts' where normal budgetary transparency rules did not apply.

Interviewers encountered expressions such as, "If we are to do our job, then it does not matter to offer a bribe from time to time…We do not need to comply with the law when nobody is watching. … If my personal interests were not harmed, I would not be bothered by commissions or bribes, even if the transactions were taking place before my eyes." (Transparency International Greece, 2012). The report identified weak civic society culture, and as Walker (2010) noted, procurement corruption cases were rarely resolved because a slow-moving justice system discouraged bribe payers from becoming witnesses and politicians often escaped corruption charges when parliamentary investigations stalled until the statute of limitations expired.

A decayed tax inspection system and a non-transparent tax code paved the way for bribery and tax evasion, which explains why a large share of taxes owed never reached the public coffers. A '4–4–2' system' prevailed in Greece – a reference to a soccer player formation in the defence, midfield, and attack. In tax collection it means 40%–40%–20%, such that if someone owes taxes, 40% goes to the tax controller, the taxpayer keeps 40%, and only the remaining 20% enters state coffers.

Former Finance Ministry General Secretary for Information Systems, Diomedes Spinellis, speaking at a 2011 conference entitled 'Tax Evasion and Social Justice' (keeptalkinggreece.com, 2011) said 4–4–2 was a common tax collection practice even when Greece was in a dire economic position. Spinellis said when the state returned large tax amounts to taxpayers, 8% went directly to the tax official as 'pocket money' – a number corrected to 10% by the then Director of Planning & Control of Financial Crime Units. Former Greek Finance Minister Evangelos Venizelos gave another example of the scale of tax evasion in a speech to the Peterson Institute for International Economics in July 2011: "Just picture this: From €100 billion of income officially declared annually by taxpayers, only €30 billion is taxed by an average rate of 30 percent, which generates around €9 billion. Thus, the average taxation for all the declared taxpayers' income (€100 billion) is only 9 percent" (Venizelos, 2011).

Evidence has emerged of a striking increase in tax evasion around election time suggesting the increases stemmed from government decisions on matters such as the intensity of transaction auditing (Skouras and Christodoulakis, 2011). Some sharp increases in the 2009 deficit have been attributed to falling revenues in the months before the October 2009 elections.

Widespread patronage also existed. A 2012 analysis by Pappas and Assimakopoulou shows the scope and reach of patronage in Greece has been the highest in Europe, mainly the result of "individual political entrepreneurs thriving inside parties using state-related resources for individual political gains". This means costs burdening the public purse with salaries for unnecessary civil servants and bureaucratic inefficiencies associated with poor management, where political patronage trumps merit.

Former Prime Minister Papandreou reportedly stated: "if you can employ any of your voters in the public service, you'll do that", a point echoed by former Finance Minister Stefanos Manos, "When I'm in Government, I will make sure your daughter gets hired somewhere" (Walker, 2010). In the months before the October 2009 elections, the government added thousands of redundant public positions. Examples included schools with teachers in administration because no classrooms existed for them, even a school where teachers outnumbered students. At that time, no one really knew just how many people worked in Greece's public sector (Walker, 2010).

Inefficiencies were widespread in the Greek economy and the cost of such practices have been enormous, wasting financial resources, distorting competition, harming the system of moral values, and consolidating tolerance of illegalities.

Greece's public sector have in the words of the 2006 Nobel laureate in economics, Edmund Phelps, been "rife with clientelism (to gain votes) and cronyism (to gain favours) – far more so than in other parts of Europe" (Phelps, 2015). As examples, Phelps notes public pensions relative to wages are nearly twice as high in Greece as in Spain, that government favours business elites with tax-free status, and some state employees receive salaries even though they fail to actually go to show up work. Successive Greek governments brought waves of party patronage hires into the public sector. "The Greek state has come to look like a sedimentary rock, each layer of which represents a particular government period" (Pappas, 2010).

A 2010 Brookings study by Daniel Kaufmann discussed by Walker (2010) lists ways corruption affects the fiscal outcome (see also Kaufmann, 2010). These include creative tax avoidance schemes, keeping a tax code unduly complex with numerous discretionary exemptions, bloated bureaucracies, less productive public investments, an excessively large wage bill and an informal or shadow economy estimated at 27% of GDP from 1999 to 2010, amongst the largest in the EU (Schneider and Buehn, 2012).

According to Walker, Kaufmann estimates bribery, patronage, and other forms of corruption deprived the Greek state of at least 8% of its GDP a year while the OECD estimated Greece lost 2.5 to three percentage points of GDP revenues through tax evasion alone, more than any other euro area member.

Analysing the correlation between corruption indicators and fiscal deficits across 40 countries, Kaufmann's 2010 study showed that if Greece achieved Spain's level of corruption control it would have recorded a smaller budget deficit of about 4% of GDP on average over the preceding five years. And if Greece's public sector had been as clean as in Sweden or the Netherlands it might have recorded budget surpluses over the past decade (Walker, 2010). The study suggests that simply adhering to Spanish standards in this area would have meant Greece could have fulfilled the Maastricht budget deficit criteria when it was admitted to the euro area.

Corruption also increases the cost of doing business. Evidence demonstrates a strong relationship between a country's corruption and its global competitiveness index. Competition and new business ideas weaken when facing widespread vested interests, any emphasis on solidarity at the expense of competition, or a culture that supports established businesses with subsidies and contracts but not potential newcomers. The World Bank's Doing Business report says Greece has been one of the most difficult countries in Europe in which to start a business, a problem largely unchanged during the first years of the crisis. It ranked number 152 out of 178 countries in 2008 and still lay at 146 out of 185 countries monitored in 2013 (World Bank, Doing Business Database).

The way these damaging practices and values persisted was a key factor in explaining the Greek economic and financial crisis, its prolonged duration, the short-lived nature of any successes, and the derailment of the first international support programme.

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