Greece's third memorandum of understanding: the last robbery before the Grexit?

Roxana

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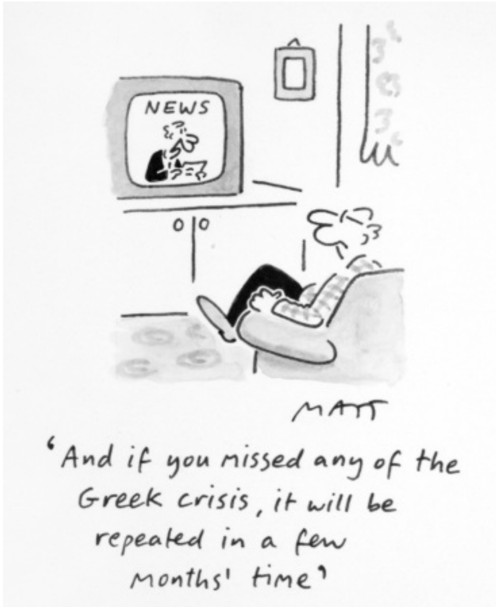
Matteo Barberi, 24 August 2015

The Greek dispute remains the main topic of the European and non-European talks and discussions. This blog does not represent an exception with several articles focusing on Greece published over the last weeks. In the last article the author Leo Hoffman-Axthelm was asking himself if we were risking the European project for a few billion euros.



More than a month after an answer arrived. On the 14th of August European and Greeks authorities agreed on a three-year ESM stability support programme for Greece up to 86 billion euros; a third bail out as the press is referring to it.

To celebrate the achievement of such agreement, President Jean-Claude Juncker stated: *"The message of today's Eurogroup is loud and clear: on this basis, Greece is and will irreversibly remain a member of the Euro area"*. It resounded like a threat. Certifying again the failure and the incompleteness of the euro's architecture, the agreement has been reached within the Eurogroup, a body that is ruling Europe but is not even enshrined in the European treaties, and has no defined authority.

Rather than a final answer the deal probably just bought some extra time before making the final choice between a deeper integration and the dismantling of the Euro area. This post will look at the main contents of the agreed Memorandum of Understanding (MoU) for the bailout, its economic sense and chances of succeeding[1].

Already on page 1 of the MoU, things are immediately made clear:

"The Government commits to consult and agree with the European Commission, the European Central Bank and the International Monetary Fund on all actions relevant for the achievement of the objectives of the Memorandum of Understanding before these are finalized and legally adopted. […] The conditionality will be updated on a quarterly basis."

Here we go, again. The Greek government commits not to take any decision or to legislate without the troika's explicit permission or approval. Once more, sovereignty is suspended in Greece.

The detailed actions agreed in the MoU are grouped into four "pillars".

1. *"Restoring fiscal sustainability: Greece will target a medium-term primary surplus of 3.5% of GDP to be achieved through a combination of upfront parametric fiscal reforms, including to its VAT and pension system, supported by an ambitious programme to strengthen tax compliance and public financial management, and fight tax evasion, while ensuring adequate protection of vulnerable groups".*

There is so much included in the first "pillar", but in two words it means additional austerity. The same brilliant formula which in the years of the troika's assistance resulted in the GDP collapsing by 27% and unemployment rising to 29%. Not to mention the legacy of the humanitarian crisis, the public health disaster, and to count the number of suicides.

This time fiscal policy relies on the VAT reform (a tax regressive per definition whose rise will just reduce consumptions and depress salaries) and on the raise of other taxes (luxury tax, corporate income tax). To achieve fiscal sustainability the economy needs to grow, while these measures will just depress the economy even more.

In the context of "sustainability", pensions will be cut (including the already tiny pensions of small farmers) with the natural result of killing the internal demand even more (in a country where pensioners spend a large chunk of their pension on health care). In addition to that, the Greek government is required to legislate in order to bypass the Greek Court ruling on the constitutionality of pension measures of 2012[2]; constitutionality has to be put aside. No to forget that in 2010 and 2012 the retirement age already increased and the pensions were cut, in a system that is not that generous after all. No doubt the Greek pension system needs some revisions and reform but this has to happen over a long period.

According to the MoU: *"The trajectory of the fiscal targets is consistent with expected growth rates of the Greek economy as it recovers from its deepest recorded recession."* One might legitimately wonder if these are the same biased economic forecasts that regularly characterized the troika's programmes. Will they have accounted for the endogeneity of the surplus or at least corrected the size of the fiscal multipliers this time?

2. *"Safeguarding financial stability: Greece will immediately take steps to tackle Non-Performing Loans (NPLs). A recapitalisation process of banks should be completed before the end of 2015, which will be accompanied by concomitant measures to strengthen the governance of the Hellenic Financial Stability Fund (HFSF) and of banks".*

Here the story repeats itself in a tragicomic way: the same failure of the 2013 recapitalization is designed. Greek taxpayers will bear the costs of the recapitalisation and provide funding for the banks, but no institution (as a bad bank) is designed to cope directly with the NPLs. it is unlikely that credit will start again to flow. The requests to *develop a credible strategy* and follow the *best practices* are pretty vague and it is unlikely that it will help to restore liquidity and capital in the banking system.

Governance and control of the HFSF and the banks will be in the troika's hand. As per the second pillar of the MoU, the Greek government has accepted an unprecedented oversight of its financial sector; as the memorandum says: *"all measures, legislative or otherwise, taken during the programme period, which may have an impact on banks' operations, solvency, liquidity, asset quality etc. should be taken in close consultation (with the troika)".* The Greek government commits not to legislate on anything without the creditors' express permission.

3. *Growth, competitiveness and investment: Greece will design and implement a wide range of reforms in labour markets and product markets (including energy) […].There will be an ambitious privatisation programme".*

Making the Greek labour market more flexible to the troika's assent is hard even to imagine. And wasn't the IMF stating that "labor market regulation is not found to have statistically significant effects on total factor productivity"? Do people at the IMF read their own studies?

The request "*to preserve the on-going privatisation process"* it is also hard to believe considering that the previous round of privatisation has not been endorsed by the European competition commission. A new independent fund will manage valuable Greek assets and monetize them through privatisation; under the supervision of the relevant European Institutions, airports, seaports, energy systems, land and property will be sold, shutting the door to any future possibility for utilising public assets to generate investment, revenues and repay the debts. While I am writing, Greece has just agreed to sell to a German company the rights to operate 14 regional airports . The same Greek government that had opposed privatisation has now committed to it. Not to mention that the thesis that privatisations may support investment and growth is disputed at all the level, even by the very same institutions of the troika.

4. *A modern State and public administration shall be a key priority of the programme.*

The key words of the fourth pillar are de-politicizing, downsizing and wages cutting. A strategy that keeps riding the myth of the excessive size and inefficiency of the Greek public sector. Greece did not have more employees in the public sector than the other EU countries (neither in terms of the labour force, nor in terms of total employees; ILO and OECD data). As well as the ratio government expenditure/GDP in Greece was lower than the EU-27 average, and lower than some “virtuous” countries like –among others- France, Austria, Belgium, or Germany (AMECO Data). And moreover, in the period before the crisis Greece was one of the countries with the highest growth in productivity not only in the Eurozone, but the entire OECD (OECD statistics). However since the Greek public sector was the one to blame for the crisis, total public sector employment declined over 25% between 2009 and 2014 (EC). Beside all this being well known, the MoU calls for additional cuts in the public sector.

Social safety nets, education, research, guaranteed minimum income, health care measures, are mentioned here and there in the MoU but not a single euro has been budgeted for any of these. All in all, the MoU represents at the same time a tangible sign of the previous failures, the will of safeguarding unilateral interests, and a self-defeating strategy. Lastly it endows an even greater role for the troika than in the past.

Two questions naturally come to the mind of anyone reading the MoU. Has nothing been achieved by the Greek government over the past years? Will this work out this time?

As for the first question, the OECD calculated that Greece is the country that has done the most since 2007 to reform its economy; nothing to add. As for the second question, a negative answer is straightforward. As long as it addresses the wrong causes of the crisis, there is no deal able to put an end to it. Greece and the euro area did no enter a crisis because of public debts, inefficiencies in the public sectors, generosity of pension systems, or because the rigidity of the labour markets; or even worse because the laziness of the southern European workers. The ECB explained clearly that the crisis of the peripheral countries is not related to any of the previous but it is due to an abnormal increase of private debt, driven by a thoughtless flow of relatively cheap financing.

Such irresponsible lending, the balance of payments euro-crisis, and the austerity measures, have a common root in the Euro and the EMU; it is the single currency to play the most important role. The reason why the countries of the north have lent recklessly to those of the south is the elimination of the exchange rate risk. The reason why balance of payments cannot adjust and macroeconomic imbalances in the euro area persist, is the impossibility of adjustments through the nominal exchange rate. The reason why countries are forced to austerity measures is that when the exchange rates cannot adjust themselves to the external accounts, a country needs to cut its income. Everyone recognizes the previous but few are candid enough to call for the dismantlement of the euro.

The bottom line is that reforms cannot pay off as long as Greece (as well as other countries) is chained to the euro. Any realistic plan for re-boosting growth and employment in Greece necessarily needs to pass through an adjustment of the exchange rate. Once again, it is the IMF to suggest it! Leaving behind the single currency is not sufficient by itself, but it is a necessary condition to restore democracy and economic growth in all the euro area. [i]

[1] Greece’s former finance minister Yanis Varoufakis drafted his full annotated version of Greece’s Third MoU. Reading it shows the shame of the deal in its entirety. https://varoufakis.files.wordpress.com/2015/08/mou-annotated-by-yv.pdf

[2] On the 10th of June, the Greek’s top administrative court, the Council of State, ruled that the 2012 cuts violated Greek law and the European Convention on Human Rights because they deprived pensioners of the right to a decent life.