

THE GREEK FINANCIAL CRISIS: INTERNAL IMPACT AND ITS EXTERNAL EFFECTS ON EUROPE

A GÖRÖG GAZDASÁGI VÁLSÁG: BELSŐ ÉS AZ EURÓPÁRA GYAKOROLT KÜLSŐ HATÁSOK

FIRAS NAJIB ZEIDAN PhD Student
Management and Organizational Sciences
Kaposvár University

Abstract

The Greek Debt Crisis started in October 2010 when Greece took the decision to enter the Euro Zone, which is considered to be the second largest economic power in the world after the United States.

The problem increased in Greece between the previous government and the new government with a budget deficit of 13.6% and that its debt was 163% of its GDP.

Based on the above, the problem of this paper revolves around the following question: What are the causes of the financial crisis and what are the internal impact and external effects on the euro area?

1. Introduction

The global economy was under attack since 2008 by an old-returning type of terror under the name of financial crisis. This attack was the number one news headline during these years since it impacted almost everyone. Every country in the globe was affected in a way or another by the crisis which was the result of the housing sector's boom in the US (Stiglitz2009).

European and Asian countries were affected by the crisis due to the integration in their financial markets. The stock market indices in the European Union witnessed sharp declines following the financial deterioration in the US (The Economist 2009).

Greece was facing a poor economic performance and problems in maintaining economic growth and development of the country as a whole, as well the less control of the public expenditure and the increasing rate of debt (Hasaj,2012). Further to the above, their joining to the European Community in 1981 encouraged them to borrow more due to the stability in the interest rate, which lead to a high increase in the value of the debt and it was difficult for them to repay it (International Monetary Fund, European Department, 2017; Economou, C., Kaitelidou, D., Kentikelenis, A., Sissouras, A. & Maresso, A., 2014).

This Crisis increased in the last three years with the Confrontation between the three creditors of Greece: "The European Commissioner, the International Monetary Fund IMF Euro group and the World Bank" and "the new Greek government" (Gibson, Heather D., Stephen G. Hall, and George S. Tavlas, 2012; Al Sayyed, 2015; Mink, Mark, and Jakob De Haan, 2013).

As a matter of fact, the new Greek government headed by Alexis Tsipras, refused to receive the final installment of the amount of € 7.2 billion package which was supposed to

be received by the Greek government, and who refused to extend the bailout program after the end of February 2015 (Al Sayyed, 2015; Mink, Mark, and Jakob De Haan, 2013).

Knowing that the three creditors of Greece (the European Commissioner, the International Monetary Fund IMF and the World Bank) had given Greece two rescue packages between 2011 and 2012 and on 15 August 2015, when according to many negotiations, the European Commissioner and the euro group said that: the Eurozone finance ministers agreed to give Greece a third bailout package which will help and support Greece (Al Sayyed, 2015; Mink, Mark, and Jakob De Haan, 2013).

This project discusses the overall economic situation in Greece. It provides an overview about Greek economy then tackles its different sectors. Then it talks about some actions taken by the government and the ECB European Central Bank and International Monetary Fund IMF in order to strengthen the Greek economical standings and lessen the impact of the crisis (Al Sayyed, 2015; International Monetary Fund, European Department, 2017).

2. Objectives

I would like to highlight the Greek financial crisis and to examine the internal impact and its external effects on Europe, and to find the financial solution to its problem.

Research questions

1) Deals with the Greek Crisis and the causes behind it. What is the reality of Greek economy that led to this crisis?

2) What is the true size of Greece's debt and how can we describe the reality of the crisis today?

3) How can we evaluate the Greek and European atmosphere, after the Greek people rejected the austerity policy?

4) Is the decision to exit the European Union financially sound? How to float banks and the state treasury and get rid of debt?

5) And the questions about What if Greece left the euro area? What are the impacts of Greece's exit from the euro zone if this happens?

3. Methodology

Primary: Methods Used Qualitative method: analysis of documents and quantitative method: analysis of tables and charts. *Secondary:* Research Papers and reports

4. Literature review

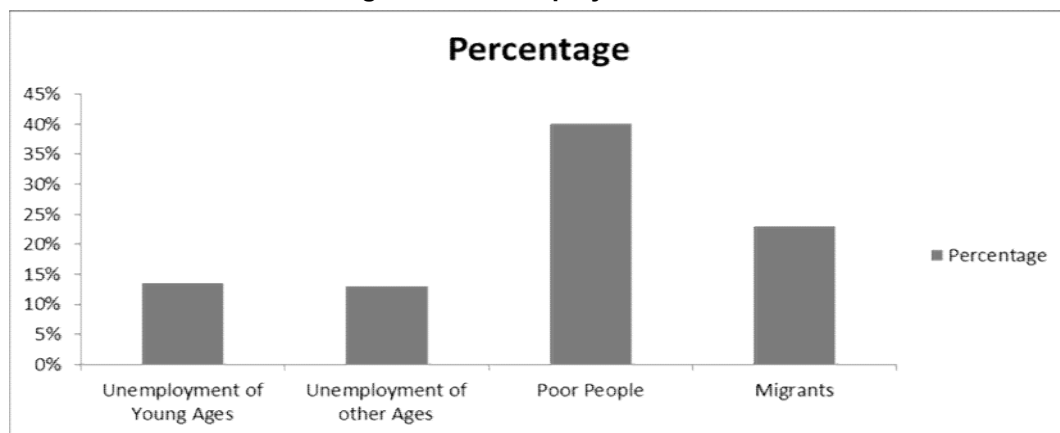
1: Causes of the Crisis

What is the reality of Greek economy that led to this crisis?

Greece is located on the periphery of the European continent, and its economic strength is concentrated in the tourism sector, and in maritime transport (Hasaj,2012). The size of its economy because of the absence of giant commercial and industrial enterprises. Its financial problem began to worsen following the global financial crisis (2008), due to the economic recession. The unemployment rate is about 27 percent, and it is about 50 percent

of the young age groups, which is a very dangerous economic indicator. While some are forced to work in European countries, some migrate to America and Australia, violence increases, and about 40 percent are poor and mostly they are young (Hasaj, 2012; KARANIKOLOS, 2013).

Fig. 1.: Power Employment Chart



Source: The researcher

Regarding the Greek GDP, it is about 242 billion euros, or about 265 billion dollars of the rate of public debt. The GDP fell by about 26 percent between 2010 and 2014. The ratio of public debt to GDP rose from 100 percent (2008) to 163 percent in the first half of 2015. The European debt index should not exceed 60 percent of GDP (International Monetary Fund, European Department, 2017; KARANIKOLOS, 2013; Hasaj, 2012).

Austerity policy has been adopted in Greece since 2010, they reduced the volume of social assistance, and allocations for retirees and to ensure old age (KARANIKOLOS, 2013; Ifanti, A. A., Argyriou, A. A., Kalofonou, F. H., & Kalofonos, H. P., 2013).

Several steps taken by the new government in this regard:

- Take action for the poor, who absolutely reject austerity policy.
- Electricity is restored to hundreds of homes who have been cut off due to defaults on bills or other reasons.
- Determination of the minimum wage.
- Reemployment to a large number of those who were fired before.
- Cancellation of the terms of privatization.

2: The size of the debt and the reality of the crisis

What is the true size of Greece's debt and how can we describe the reality of the crisis today?

– Greek public debt is about 342 billion euros, or 380 billion dollars. In addition, the debts of banks and companies amount to about 160 billion euros, or about 175 billion dollars. Greece's total debt is about 500 billion euros, or \$ 550 billion. The most important creditors are the troika consisting of the European Commission (130 billion euros), the International Monetary Fund (20 billion euros) and the World Bank (53 billion euros) (KARANIKOLOS, 2013; Hasaj, 2012; FEATHERSTONET, 2011; Ifanti, A. A., Argyriou, A. A., Kalofonou, F. H., & Kalofonos, H. P., 2013).

At the meeting between the Greek Prime Minister and German Chancellor Angela Merkel, it was agreed that Greece would make new proposals to resolve the crisis and

close the banks out of fear of massive withdrawals that would create a major crisis for the country and extend the closure if needed. Since the victory of the Radical Left Party (SIRIZA) in the January 2015 parliamentary elections and the arrival of its leader in the new government, interest on Greece's debt and treasury bonds has risen from 14.6 percent to about 18 percent (Al Sayyed, 2015).

As a result of the popular referendum held last June, 61 percent of the votes who supported Tsipras' call to stop austerity, which was adopted by the previous party, and thus showed the attitude of the Greek people who reject austerity. But this equation has changed today, especially after the case has taken a political direction, the Tsipras' party divided into two sections: the first section is in favor of the Prime Minister in his decisions that may be different from the promises he made during his campaign, the second section is still against austerity (KARANIKOLOS, 2013; Al Sayyed, 2015; Ifanti, A. A., Argyriou, A. A., Kalofonou, F. H., & Kalofonos, H. P., 2013).

It should be noted that the adoption of the third rescue package today, came at a high political price paid by Alexis Tsipras, which could lead to early elections (Al Sayyed, 2015).

Internal Impact and External Effect on Europe

3: Fear in other countries

How can we evaluate the Greek and European atmosphere, after the Greek people rejected the austerity policy?

Today, fear prevails in most European countries such as Portugal, Spain, Italy, Ireland and France, especially after the Greek experience of the people's rejection of austerity policy. The fear is that there may be protests up to the end of the revolution, which would open the file of revision (or change) in several financial items approved in the European Union (Ifanti, A. A., Argyriou, A. A., Kalofonou, F. H., & Kalofonos, H. P., 2013; Al Sayyed, 2015).

4: Is the decision to exit the European Union financially sound, how to float banks and the state treasury and how to get rid of debt? (ACIT, 2012)

– Today, the European Union is facing the dilemma of solving the Greek debt crisis as either accepting Greece's bankruptcy or leaving the euro zone. Credit institutions will suffer a big loss, either support it again and keep it in the region, but the crisis will come back after two years and perhaps even less.

The Greek debt crisis has begun to take a political turn, rather than a financial and economic one. While negotiations are under way between the Greek government and the European Union, international insistence on resolving the crisis is evident by several parties, the United States, Russia and China.

It can be said that whatever the outcome of the difficult and complicated negotiations is, it will serve as a temporary solution, given that the Greek debt crisis is intractable and grows annually as snowballs (International Monetary Fund, European Department, 2017). The prospects for a renewed crisis are therefore apparent, including the possibility of returning to the search for Greece's exit from the euro area (ACIT, 2012).

5: What if Greece left the euro area? What are the impacts of Greece's exit from the euro zone if this happens? (ACIT, 2012).

- For Greece, its exit from the Eurozone will entail the following:
- Declaration of Bankruptcy.

- Return to the basic currency (Drachma) and reduce their value to subsequently reduce the value of debt, and scheduling amounts agreed with creditors in national currency.
- Determining the amount that Greece will pay creditors, in order to avoid the seizure of its property abroad.
- Restitution of subsidies, support of wages and pensions of retirees, and assistance to industrialists and farmers with soft loans.
- The restoration of Greece's financial independence, like some non-eurozone European countries.
- To resort to China, Russia and also America to borrow in foreign currency if this cannot be from the troika.
- Devaluation of the national currency (Drachma).

As for the European Union and creditors, the main results of Greece's exit from the euro area are:

- Loss of creditors' portion of the amounts owed to Greece.
- Certain EU countries with financial problems may take the same step and return to the main national currencies (Portugal, Ireland, Italy, etc.).
- The confusion in the financial markets and the currency of the euro.

5. Conclusions

- It is better for Greece to return to financial independence, provided that the necessary measures are taken to remove all irregularities and mistakes committed in the past years, which led to the financial and economic crisis intractable. Greece's exit from the Eurozone is the first step in resolving its complex financial crisis, and for restoring its financial independence and with declaring bankruptcy, which is the second step in building its financial structure and starting again on a stable financial and economic basics.
- Greece is a service based economy and it is not as safe as it might be. Foreign aid, tourism, remittances, services, constitute a large part of the income of the economy; these are volatile and risky factors to rely on. The size of its economy is small because of the absence of giant commercial and industrial enterprises. Despite the guarantees from different types of donors, it might be a good idea for Greece to expand its economy further based on more reliable bases.
- From the indicators and the charts below Greece's Balance of Payment revealed a deficit in the years 2011, 2012, 2013, 2014, 2015, 2016 and 2017 and an increase of external debt (percent to GDP) continued to rise from Euro 188.2 M in 2011 to Euro 239.2 M in 2017. This led to the decreasing of Foreign Direct Investment FDI (percent to GDP) inflow to Economy, which led to a decline in the Economic growth and more fiscal deficits of Greece. It confirms that Greece cannot be expected to grow out of its debt problem even with full implementation of reforms and reliefs.
- About the restricting and baseline scenario. Debt seems unsustainable amounting to 170 percent of GDP by 2020, and 164 percent by 2022, and it will raise more to reach around 275 percent of GDP by 2060, where the cost of debt is going to rise overtime.

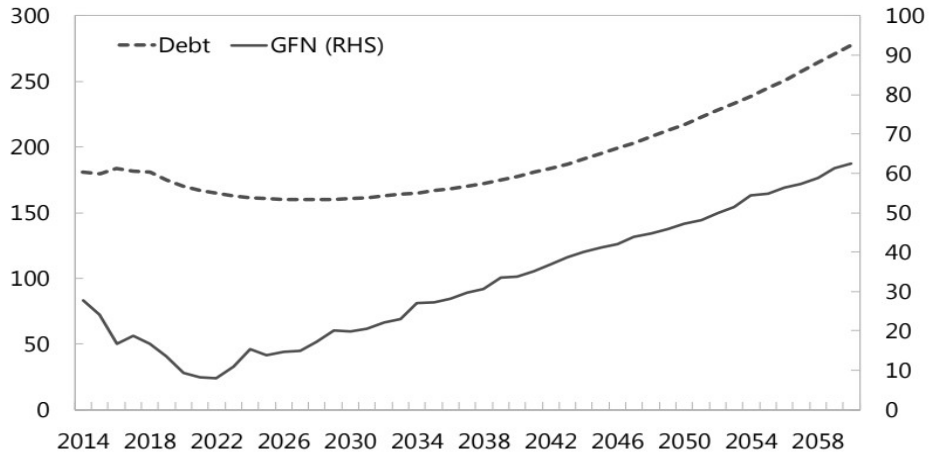
- About questions 3, 4 and 5 and about these conclusions concerning debit increase overtime my opinion is the possibility of returning to the search for Greece's exit from the euro zone.

Fig. 2.: Greece: Selected Economic Indicators

Population (millions of people)	10.9				Per capita GDP (€'000)	16.2	
IMF quota (millions of SDRs)	1,101.8				Literacy rate (percent)	97.7	
(Percent of total)	0.46				Poverty rate (percent)	35.7	
Main products and exports: tourism services; shipping services; food and beverages; industrial products; petroleum products; chemical products.							
Key export markets: E.U. (Italy, Germany, Bulgaria, Cyprus, U. K.), Turkey, U.S.							
	2011	2012	2013	2014	2015	2016 (proj.)	2017 (proj.)
Output							
Real GDP growth (percent)	-9.1	-7.3	-3.2	0.4	-0.2	0.4	2.7
Employment							
Unemployment rate (percent)	17.9	24.4	27.5	26.5	24.9	23.2	21.3
Prices							
CPI inflation (period avg., percent)	3.1	1.0	-0.9	-1.4	-1.1	0.0	1.2
General government finances (percent of GDP)							
Revenue	44.1	45.9	48.0	46.8	47.8	49.3	47.4
Expenditure	54.4	52.4	51.6	50.8	51.2	51.6	49.7
Fiscal overall balance	-10.3	-6.5	-3.7	-4.0	-3.4	-2.3	-2.3
Fiscal primary balance	-3.0	-1.4	0.4	0.0	0.2	0.9	1.0
Public debt	172.1	159.6	177.9	180.9	179.4	183.9	180.8
Money and credit							
Broad money (percent change)	-14.6	-5.3	2.7	-0.4	-16.9	1.6	...
Credit to private sector (percent change)	-3.1	-4.0	-3.9	-3.9	-3.6	-3.1	0.7
3-month T-bill rate (percent)	9.2	9.2	4.8	2.8	4.5	3.1	...
Balance of payments							
Current account (percent of GDP)	-10.0	-3.8	-2.0	-1.6	0.1	0.0	-0.1
FDI (percent of GDP)	0.2	-0.4	-1.5	0.1	0.5	-1.6	-0.8
Reserves (months of imports)	-1.0	-1.1	-0.8	-1.0	-1.3	-1.3	-1.2
External debt (percent of GDP)	188.2	237.0	237.3	238.5	251.1	245.7	239.2
Exchange rate							
REER (percent change)	0.7	-3.1	-0.8	-2.1	-4.9	0.6	0.0

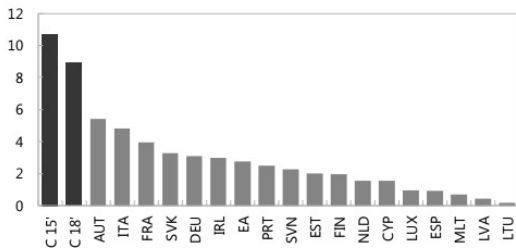
Sources: Elstat; Ministry of Finance; Bank of Greece; Bloomberg; World Bank, World Development Indicators; IMF, International Finance Statistics; IMF, Direction of Trade Statistics; and IMF staff projections. 1/ Data according to ESA-2010 methodology

Greece: GG Debt and GFN-- Baseline, 2014-2060 (Percent of GDP)



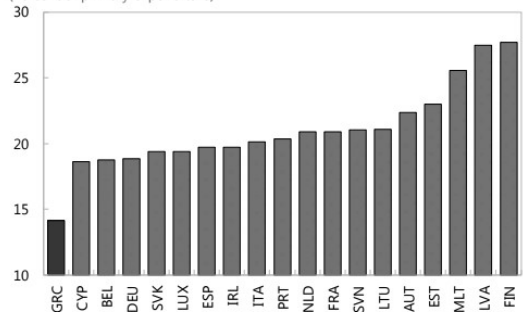
Source: IMF staff estimates.

State Transfers to the Public Pension System (Percent of GDP)



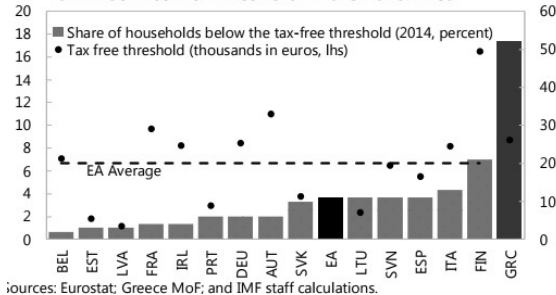
Sources: 2012 and 2015 Aging Reports; and IMF staff calculations.
Note: State transfers are defined as difference between pension spending and actual contributions, excluding third-party revenues and non-contributory state transfers.

General Government Expenditure on Goods and Services, 2015 (Percent of primary expenditure)



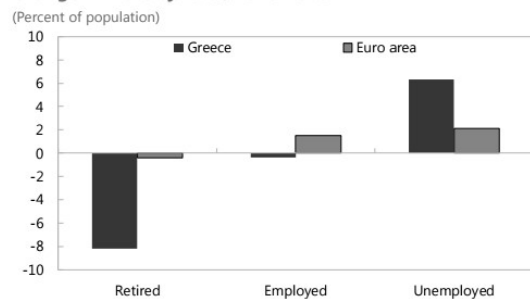
Sources: Eurostat, and IMF staff calculations.

Tax-Free Income Threshold in the Euro Area



Sources: Eurostat; Greece MoF; and IMF staff calculations.
Note: Share of exempted households for Greece is calculated based on 2016 income tax declaration (2015 declared incomes) using thresholds legislated in 2016. For other euro area countries, the share is based on 2014 Household Budget Survey data and 2015 tax-free thresholds.

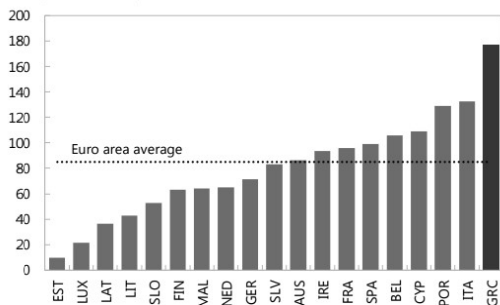
Change in Poverty Rate, 2010-2015 (Percent of population)



Source: Eurostat. Note: Persons at risk of poverty are those living in a household with equivalized disposable income below 60 percent of the national median.

General Government Debt, 2015

(Percent of GDP)

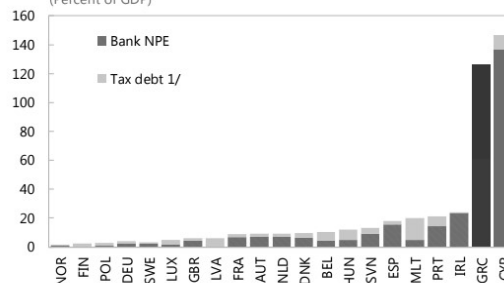


Sources: Eurostat; and Haver Analytics.

Sources: Eurostat; Greece MoF; and IMF staff calculations.
 Sources: Eurostat; Greece MoF; and IMF staff calculations.
 Note: Share of exempted households for Greece is calculated based on 2016 income tax declaration (2015 declared incomes) using thresholds legislated in 2016. For other euro area countries, the share is based on 2014 Household Budget Survey data and 2015 tax-free thresholds..

Private Sector Arrears

(Percent of GDP)

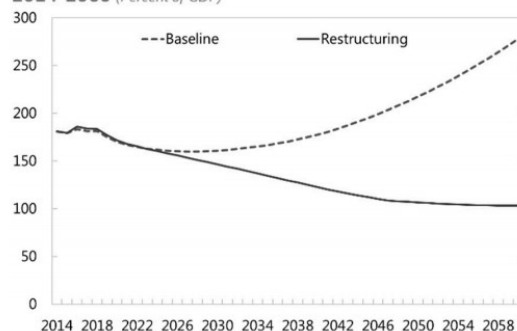


Sources: EBA 2015 June Report; Eurostat; OECD; and IMF Staff Calculations.
 1/ Data for Greece are estimates as of end-November 2016 and include social security contribution debt.

Source: Eurostat. Note: Persons at risk of poverty are those living in a household with equalized disposable income below 60 percent of the national median.

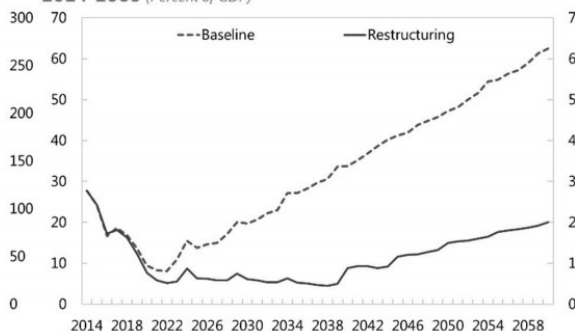
Debt Restructuring Scenario, 2014–2060

Greece: GG Debt-- Restructuring Scenario, 2014-2060 (Percent of GDP)

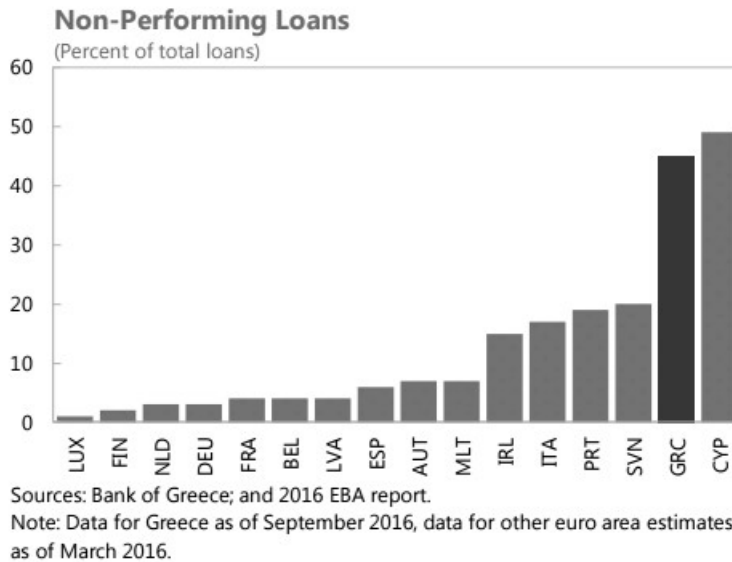


Source: IMF staff estimates.

Greece: GFN -- Restructuring Scenario, 2014-2060 (Percent of GDP)



- Taxpayers in the highest income decile pay about 60 percent of personal income tax revenue, while 53 percent of wage earners and 85 percent of farmers are exempt.
- Persons at risk of poverty are those living in households with an equalized disposable income below 60 percent of the national median after social transfers.
- The significant reduction in Greece's poverty rate among retirees during the crisis continues a trend that started well before the crisis due to a rapid increase in pension spending during the boom years.



References

- Heather D. Gibson, Theodore Palivos, and George S. Tavlas Special, July 2013, The crisis in the euro area, an analytic overview.
- Gibson, Heather D., Stephen G. Hall, and George S. Tavlas (2012): “The Greek financial crisis: Growing imbalances and sovereign spreads.” *Journal of International Money and Finance* 31.3 (2012): 498-516.
- Hasaj, Bendi, (2012): Government Debt Crisis in Eurozone Case, Studies: Greece and Italy What can Kosovo learn from the Eurozone crisis? Thesis, Rochester Institute of Technology.
- Albanian Centre for Competitiveness and International Trade (ACIT) Tirana (2012): Study on the Economic Impact of the Greek Crisis in Albania.
- International Monetary Fund. European Dept. February 7, 2017, Greece: 2017 Article IV Consultation-Press Release; Staff Report; and Statement by the Executive Director for Greece.
- Al Sayyed, May (2015): Greek economic crisis. How Greece was implicated, and which is the way out of the crisis? Report. <https://www.arageek.com/2015/07/11/greek-economic-crisis.html>
- FEATHERSTONET, KEVIN (2011): he Greek Sovereign Debt Crisis and EMU: A Failing State in a Skewed Regime.
- KARANIKOLOS, Marina, et al. (2013): Financial crisis, austerity, and health in Europe. *The Lancet*, 2013, 381.9874: 1323-1331.
- Ifanti, A. A., Argyriou, A. A., Kalofonou, F. H., & Kalofonos, H. P. (2013): Financial crisis and austerity measures in Greece: their impact on health promotion policies and public health care. *Health policy*, 113(1), 8-12.
- Mink, Mark, and Jakob De Haan (2013): “Contagion during the Greek sovereign debt crisis.” *Journal of International Money and Finance* 34 (2013): 102-113.
- Economou, C., Kaitelidou, D., Kentikelenis, A., Sissouras, A., & Maresso, A. (2014): The impact of the financial crisis on the health system and health in Greece. *Economic crisis, health systems and health in Europe: country experience*. Copenhagen: WHO/European Observatory on Health Systems and Policies.