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ECONOMICS AND POLITICS IN GREECE
An Outsider's Point of View

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I

My talk will be rather off the cuff.

Since some of my remarks may not be to your liking, I would like to begin with a disclaimer. Although I initially came to Athens and the end of September under the auspices of the Fulbright Foundation, as guest professor of economics at the University of Athens, my association with the Foundation and the University ended on March 1. I am currently on my own and am now located in an office which the Bank of Greece has graciously made available to me. I am, however, in no way officially affiliated with the Bank. My comments, therefore, are strictly my own and do not reflect in any way the views of the Fulbright Foundation or those of the Bank of Greece.

Given the subtitle of my talk, "An Outsider's Point of View," I should perhaps say something about myself. I first came to Greece almost 40 years ago in 1954 as a Fulbright lecturer at the University of Salonika. That didn't go too well since I soon came down with a severe case of hepatitis, and after 39 days in the Evangelismos Hospital of Athens I was shipped back to the States as damaged goods. I again came to Greece in 1960 for a brief visit and then in 1964 at the invitation of the Center Union Government of George Papandreou, along with many other professors from other countries, for a conference on the establishment of a third university at Patras. I next returned in 1966 on sabbatical leave and spent a half year in Athens, leaving shortly before the coup of April 1967. I became deeply embroiled in the politics of Greece, then and after the coup. I was persona non grata under the colonels and was unable to return to Greece until 1977, for a brief stay and to renew my contacts here. I came for a longer three-month stay in 1979, at the invitation of the Bank of Greece, to give a series of lectures on monetary theory. And this time I have come for an eight-month stay and will be leaving in seven days on the 24th for Italy and France.

I mention all this to make clear that my views are not those of a tourist. At the same time, I cannot pose as an expert on Greece since my stays were somewhat fractured and of not too long duration. Therefore, what I have to say about the economics and politics of Greece are indeed the views of an outsider.

II

Having said all this, I want to make an important point by running quickly through a history of Greece, with which you are no doubt more familiar than I am. It must be emphasized that Greece is a new and very young country, its long history of well over 3,000 years notwithstanding. After 400 years of Turkish rule it became a free and independent state in 1831, consisting only of the Peleponnese and Mainland Greece up to Lamia, with its capital in Nafplion. In 1834 the capital was shifted to Athens, then a small town with a population of 10,000 gathered around the base of the Acropolis. In 1864 Greece acquired the seven islands in the Ionian Sea. Thessalia was next added to Greece 1881 and Epirus, Macedonia and the Agean Islands in 1912, followed by Thrace in 1923.

Modern Greece as we know it today is therefore a mere 70 years old. But those 70 years have been turbulent ones in which the monarchy and the army put severe limits on democracy even during its brief flareup in the time of Eleftherios Venizelos. Greece went through a brief period of republican government from 1924 to 1935. The return of the King in the referendum of 1935 and his appointment of a general as his prime minister led to the Metaxas dictatorship of 1936-1941, which was followed by the Nazi occupation of 1941-45 and which, in turn, gave rise to a bitter and destructive civil war from

1946 to 1949 after the withdrawal of the Germans and the return of the English only to be superseded by the Americans under the Truman Doctrine. During the civil war large numbers of people were jailed, tortured and exiled to deserted Aegean islands. The 1950s up to 1963 were a time of right-wing, rabidly anti-communist governments which restricted the movements of the returned exiles and blatantly rigged elections and suppressed civil rights. The rise of the relatively liberal government under the Center Union of George Papandreou in 1963 ended in the constitutional crisis of 1965 when the prime minister tried to impose the rights of parliamentary democracy over those of the monarchy and the army. In its distrust of a democratically elected government, the anaktora insisted on naming the defense and interior ministers and concocted the Aspida affair implicating the son of the prime minister. Then came the dictatorship of the colonels from 1967 to 1974.

III

From all this, it emerges that Greece, as a country of freely and democratically elected republican governments, has existed (with the sole exception of 1924-1935) only over the past 19 years; that is, since the return of Karamanlis in 1974 that resulted in the final end of the monarchy in a referendum and a purging of the general staff.

Over most of its history, modern Greece has not had the tranquility or the time to attend to its most pressing needs. At one time or another it has been dominated and controlled by Turkey, England, and the United States, and interfered with by a foreign-imposed, destabliizing and politically meddlesome monarchy. Above all, it has not been able to evolve a stable political substructure that does not depend upon transient parties dominated and limited by the even more transient lives of their charismatic leaders. It is no wonder, therefore, that the economy of Greece is in such a parlous state. Politics and economics are interdependent in all Western countries, but in Greece the relationship is particularly prone to irresponsible acts of political and economic legerdemain.

In the early 1980s four major political earthquakes took place. They were the major capitalist victories of Ronald Reagan and Margaret Thatcher in the United States and Great Britain, and the socialist victories of François Mitterand and Andreas Papandreou in France and Greece. Reagan and Thatcher led the great capitalist counter-revolution that sought to undo, in their view, the quasi-socialist policies of the past 50 years.

Under the fraudulent teachings of monetarism and supply-side economics, both countries promoted a rampant market mentality. They undertook a massive deregulation of their economies in the name of getting the government off the backs of the dynamic cutting edge of capitalism, namely, the much put upon innovating capitalist class, and changed their tax laws radically in favor of the business sector in order to stimulate investment and growth by redistributing income from labor to capital. Both Thatcher and Reagan broke the backs of their trade union movements early in their administrations; in the coal strike in England and the air controllers in the United States.

In France and Greece, on the other hand, there was the promise of a "moral revolution" that quickly degenerated into an orgy of greed, corruption and fraud. It soon became clear that the socialist Left did not have a monopoly on moral virtue. And in the end, ironically, its ideological and intellectual bankruptcy led it to emulate the supply-side policies of Reagan and Thatcher.

Since I want to stress the Greek economy in my talk I will limit myself to two graphic illustrations of the mentality and moral corruption that was encouraged in the United States. The orgy of deregulation under the Reagan-Bush administrations and the apotheosis of "greed" found its most outspoken exponent in Ivan Boesky. Before his fall in the insider trading scandals of 1986, he gave the commencement address at the University of California's Graduate School of Business Administration. Without the slightest trace of embarrassment or whimsy, he told the young men chaffing at the bit that "Greed was good." And from what happened subsequently in the investment banks and brokerage houses of New York and Chicago, it seems they took him at his word. It was also the time when students at Harvard University's Graduate School of Business Administration waved dollar bills over their heads on commencement day in anticipation of the millions to be made in a society where an unbridled free-wheeling mentalité was based on the swinging Cole Porter style of "Anything Goes." As under Louis Philippe's Guizot, the message was clear: enrichissez-vous. This is not far from what is going on in Greece at the moment, where Guizot's dictum has been reinforced by an almost universal attitude of je m'en foutisme.

IV

Before I get into some of the data concerning the Greek economy, I would like to make it very clear that I disavow any responsibility for the accuracy of the data I am about to use. In a country where rampant tax evasion has gravely eroded the tax base of the country and where 40 percent of the economy is underground, one cannot take seriously the official data released by the various ministries and the central bank. All to often, the data from these different sources are contradictory and when revised data are issued (often after a considerable lag), the adjustments are sometimes of monumental proportions (which doesn't add to one's confidence in the data gathering abilities of Greece). As an illustration of the lag in data availability, the latest issue of the Bank of Greece's Monthly Statistical Bulletin is dated June-July 1992, with the latest entries giving preliminary data for 1990. I often think that Greek data gatherers take their time in pushing numbers around on uncomplaining paper.

I have long admired my colleagues at the University of Athens and at the Bank of Greece for their resourcefulness in adjusting the published data and digging deep to find what is at times willfully withheld or distorted. Their diligence is admirable, their imagination unsurpassed. They all deserve the purple heart of economics. But despite their best efforts, what comes out in the end is nothing more than an informed guess. Still, the official data is all we've got plus the diggings of some very competent and inspired Greek economists. For what the data are worth, I base my analysis of the Greek economy on them.

In what follows I will use a series of statistical Tables and charts that I constructed in preparation for my talk. I will, of course, not be able to go into them in any great detail. For those wanting to look at the underlying data in full, my talk and its statistical appendix will be available at the offices of the Fulbright Foundation in Athens.

V

In the election of 1977 PASOK campaigned hard on the theme of "Allaghi" (or "Change"). It represented itself as the champion of the underprivileged. It opposed entry into the common market, membership in NATO, and the U.S. Bases in Greece. It also denounced the social democratic parties of continental Europe as supporters of monopoly capitalism and pledged that PASOK, as a truly socialist party, would bring about "a socialist transformation...of the relations of production." As things turned out, this was nothing more than revolutionary play acting; it was sham and bluster, mirrors and smoke. On coming to power PASOK reversed itself on each of these "transforming" issues. The one thing it did accomplish was to bring about an explosion of public debt.

In the immediate post-coup years of 1975-1980, the total net debt (internally plus externally held debt) averaged about 30% of Gross Domestic Product (GDP). By the 1989 elections, which marked the end of PASOK's eight year stay in power, it had sky-rocketed to 105% -- or 125% if defense department and other off-budget items are included (as they should be). In passing, I should mention that by 1991 the Mitsotakis government increased debt ratio to about 151%.

The servicing of the public debt currently accounts for 34% percent of all government expenditures, as compared to a

6.2% average for all OECD countries (the highest percentage other than Greece being 19%), and over 40% of government revenue. I find this rather remarkable. By way of comparison, even after the profligate debt buildup of the Reagan years in the United States, the ratio for the same period of time increased from 34% to 55%. Projected U.S. interest payments as a percentage of government expenditures for 1993 are 14.3%, and 18.4% of government revenues.

The increase in the U.S. debt ratio is easily explained by a massive supply-side tax cut for the rich on the revenue side, and a vast acceleration of defense expenditures by a John Wayne president in mortal combat with the "Evil Empire" -- which now lays in ruins and attests to the insanity and wastefulness of the Reagan Administration's addiction to a Star Wars scenario.

Now, what accounts for the massive increase in the Greek public debt from 174 billion drachmas in 1975 to 14.6 trillion in 1991, or from 29% of GDP to 131%, not including off budget items? I should point out, before getting into this, that a level of debt greater than a country's GDP is not necessarily a bad thing. At the height of its imperial power, Great Britain's debt exceeded its national income. But this was used to extend its foreign trade world wide, to support a colonial policy designed to assure a reliable source of cheap raw materials, to finance the burgeoning industrial revolution that gave it a such a head start over the continental countries, and to emerge, as a result, as the world's giant superpower in the 19th century.

The moral of this story is that if both public and private debt increases are used to expand the productive base of an economy through an effective capital formation that also results in a substantial increase in the productivity and real income of labor, the debt-income ratio will eventually fall by virtue of an accelerated growth rate. This has not been the case for Greece.

VI

Any increase in the public debt is, of course, the result of successive increases in the government deficit. Debt is a stock; the deficit a flow that increases the stock, much as a running stream increases the body of water in a lake. The official figures on the deficit, net of amortisation, show that in the year immediately after the 1981 elections the net deficit was 175 billion drachmas. By the next elections in 1985 it had increased to 594 billion drachmas, or from 7.6% of nominal GDP in 1982 to 14.4% in 1985. By the elections of 1989, the deficit had risen to 1.6 trillion drachmas or to 20.7% of GDP. The ratio then fell to 18.2% in the first post-election year of 1990. By way of comparison, the U.S. deficit in 1993, even after the budget-busting years of the Reagan-Bush

Administrations, was only 5.3% of GDP.

The deficit is, of course, the result of an excess of government expenditures over and above government revenues. Government expenditures in the 8 years of the soi-disant socialist government increased from 426 billion drachmas in 1980, the year before PASOK came to power, to 3.8 trillion in 1989, or from 28% of GDP to 48%. This sea-surge of government expenditures went for increases in pensions and other income-supporting transfer payments, and on subsidies and grants to social security, farmers insurance, farmers cooperatives, athletic organizations and the church, or what one observer called "parastate centers." One study found that from 1981-82 to 1987-88 pensions rose from 16% to 31% for the lower income classes, from 13% to 23% for the middle income classes, and from 13% to only 14% for the rich. I had one woman tell me that under PASOK her pension increased from 6,000 drachmas a month to 70,000. She added that she had voted for PASOK both times but would not do so again.

On the revenue side of the net deficit we find that government revenues increased from 359 billion drachmas in 1980 to 2.1 billion in 1989, or from 24% of GDP to 27% -- a significantly smaller increase that in the case of government expenditures. This is reflected in the fall of government revenues as a percentage of government expenditures from 84.3% in 1980 to 56.9% in 1989.

Digging a bit deeper, we see that revenues from regressive indirect taxes rose from 221 billion drachmas in 1980, the year before the election victory of PASOK, to 1.4 trillion drachmas at the end of their tenure in 1989, or from 14.5% of GDP to 17.8%. Direct, or more progressive taxes, on the other hand, rose from 104 billion drachmas in 1980 to 581 billion in 1989, or from 6.8% of GDP to 7.4% in 1989. Still another way of looking at things is to consider the increase in the ratio of indirect to direct taxes from 2.1 in 1980 to a peak of 2.6 at the end of PASOK's 1987 austerity program, which was quickly abandoned as the elections of 1989 approached. The ratio settled at 2.4 in 1989.

Overall, the PASOK government depended more on indirect than on direct taxes as a source of government revenue. This, of course, fell hardest on the poor and least of all on the tax-evading rich -- a strange development for a party that labels itself "socialist." In effect, what the socialists gave with one hand to the lower income classes by way of income-supporting transfer payments, they took back with the other in the form of higher indirect taxes.

VII

In trying to explain these variations in the revenue and expenditure sides of the deficit, Greek economists often refer to the "political trade cycle" in Greece. In the general economic literature this usually refers to the willingness of governments to undertake the necessary economic policies to guarantee that a massive drop in real income and employment does not take place (which would pose a threat to the ruling establishment), while at the same time being unwilling to continue to support a recovery to the point of full employment. As a result the business cycle peaks below its full employment potential at a politically tolerable level of unemployment that is sufficient to discipline an otherwise unruly labor force by the fear of the sack. The net result is a growth recession consisting of submerged recovery peaks; that is, the economy turns down into a recession before having reached its full employment potential.

That, however, is not what a "political trade cycle" means in Greece. In Greece in addition, as we have seen, to increased subsidies and income-supporting transfer payments just before elections, thousands upon thousands of people are added to the public payroll (perhaps one should use the word "trough" in this connection). The "political trade cycle" in Greece is, in other words, a euphemism for irresponsible government behavior. For example, if we straddle the election years of 1977, 1981, 1985, and 1989, we find that the debt-income ratio increased by 9 percentage points from 1976 to 1978, by 10 percentage points from 1980 to 1982, by 7 percentage points from 1984 to 1989, and by 16 percentage points from 1988 to 1990. For non-election periods, the rise in the debt-income ratio averages about 2 percentage points.

I have already referred to the fall in the ratio of government revenues to government expenditures during and after election years. This is obviously the result of the political manipulation of the tax system during election years. It is widely agreed that tax evasion is rampant in Greece, especially by the non-salaried professional, business, and real estate owning classes. During election years tax enforcement and collection is greatly relaxed thereby resulting in a significant loss of already limited government revenues. And when in a post-election year an attempt was made recently to impose an urban real estate tax, there was such an uproar that the proposal was quickly withdrawn and the socialist minister who made the proposal, as point man for the government, was unceremoniously dumped, and it has apparently become a national sport to bomb local tax offices. As one observer has commented, there is an election strategy in Greece that "undermines the moral fabric of tax compliance." In passing, it should be mentioned that there is no effective property tax in Greece nor a tax on wealth. In giddy moments, I can't help but think that the Greek budget could be easily balanced and the public debt completely done away with, in the matter of a few years, by simply ticketing all the illegally parked cars in

Athens -- even if this were to be restricted only to those cars parked on sidewalks and straddling pedestrian cross-walks.

Apart from the unprecedented level of tax evasion in Greece and the regressivity of the tax structure, there is the related problem of the distribution of income. One economist who made a study of this problem was puzzled by his major finding that under the pre-1981 conservative governments, which unfailingly favored capital, the distribution of income became more equitable, while under the post-1981 socialist government of PASOK (which would have been expected to favor labor) the distribution of income worsened. I was a bit surprised at his surprise. The increased reliance of PASOK on indirect taxes along with other supply-side policies, which increased capital and rental incomes by more than the income of labor, goes a long way in explaining this apparent anomaly.

At this juncture, since I am being a bit hard on the socialists, I should confess that I regard myself as one, which explains my distress with the policies of PASOK. The Greek socialist party came in with a towering mandate from the people in 1981 and, as in Mitterand's France, it frittered it away in incompetence and scandals. It could have instituted the badly needed reforms in Greece but it failed miserably to do so. Their accountability is so much the greater because one does not expect these needed reforms to come from the Right. The irony is that unlike the recent humiliation of the socialists in France, PASOK is on the brink of another electoral victory in 1994, if not sooner.

VIII

Closely related to the debt problem is the rate of inflation in Greece. The annual rate of inflation, for the 18 year period from 1955 to 1972, averaged 3.6% and never entered the double-digit range. For the next 18 years, from 1973 to 1990, however, there has been a double digit rate of inflation for every one of those years averaging 17.7% per year and ranging from a low of 11.8% in 1975 to a high of 23.7% in 1982.

With respect to the rate of inflation, most economists nowadays take a monetarist position and attribute the inflation rate to the annual growth rate of the money supply, which closely matches year-by-year the rate of inflation in Greece. I do not accept this as an explanation. The causal arrow does <u>not</u> run from the money supply to the price level, or nominal GDP; the exact opposite is the case. To begin with, the price level, given the degree of monopoly (k) in the economy, is some markup over unit labor cost, or the total wage bill divided by total output (W/Q), i.e., $P = k(W/Q)$. Unit labor cost, to state the matter in a different way, is the ratio of the money wage rate (w) and the average productivity of labor (A), i.e., $P = k(w/A)$. If the wage rate exceeds the productivity of labor, prices will rise by some multiple of the increase in the (w/A) ratio. This increase in unit labor cost generates an increase in nominal GDP which, in turn, leads to an increased demand for money. Moreover, monetary policy, in the conventional Western sense, does not exist in Greece. The central bank validates bank loans to the private sector <u>ex post facto</u> by increasing the money supply to accommodate the needs of trade. Technically speaking, the "banking principle" prevails in Greece with the causal arrow running from the banking system's asset side to its liability side. This is another way of saying that there is a full accommodation (or nearly so) of increases in the demand for money by the central banking authorities; which, in turn, means that the money supply in Greece is largely <u>endogenous</u>.

I recall the 1979 Charissopoulos Report on the financial structure of Greece, about which I published at the time a rather scathing critique. The problem then was the dominance of the government-run Currency Committee, which gave the marching orders to the central bank, and the mandatory placement of new government debentures to cover the deficit with the banking system. The complaint then was over the absence of a capital market and the tendency of nonbank corporations to finance their needs by ever-renewable short-term bank loans, which in many cases simply wound up in numbered Swiss bank accounts with the Greek public left holding the bag in case of a bankruptcy. The resulting debt-equity ratio in Greece is one of the highest in the world. The problem of this high Greek debt-ratio was clearly addressed at least 40 years ago by the American economist Howard Ellis and was updated later by Dimitrios Halikias, who later served as Governor of the Bank of Greece under the PASOK government. Although the government now sells Treasury bills directly to the public, the major proportion still goes directly to the banks, and the central bank "policy" (if that is what it can be called) continues its accommodating role. I should point out, in passing, that the average maturity of the public debt in Greece is about two years which, with the recurrent government deficits each year, means that new debt is floated on top of a constant churning of existing government securities.

If I am correct in arguing that prices are not a function of the money supply but that the money supply is a function of the price level, then the solution to the problem of inflation in Greece lies in an effective incomes policy which increasingly restricts money wage increases via collective bargaining to the productivity of labor. The PASOK government tried this, though not too successfully, in its stabilization policy of 1985-86 but quickly reversed itself in the face of labor unrest and the approach of new elections. In its own fumbling way, the Mitsotakis government, under pressure from the common market, is also trying to restrict the money wage rate.

I do not have the time to get into any detail on the nature and necessity of an effective incomes but I should point out that an incomes policy by itself is not sufficient to solve the problem of inflation. There is a further need for an effective credit policy to deal with potentitially destabilizing financial innovations. In short an effective incomes policy <u>and</u> an effective credit policy must first be in place and then backed up by the traditional Keynesian tools of contracylical monetary and fiscal policy. Perhaps I will have the opportunity to elaborate on this in the question-and-answer period following my talk.

I would, however, like to make one observation in view of the impending PASOK victory in the next election. Over 50 years ago, a young and brilliant British economist, E.F.M. Durbin (who died trying to save a drowning child) argued in association with one of the leaders of Fabian Socialism in England, George Bernard Shaw, that socialism would ultimately have to confront organized labor and bring it to heel. They argued that if socialism were to be captured by the trade union movement (as was the German S.P.D. when it sided with Eduard Bernstein's revisionism over the more radical position of Rosa Luxemburg), it would be transformed into a labor party, which is another species altogether.

With European unemployment currently over 11% and the

European Confederation of Trade Unions sending its people into the streets in mass demonstration in Holland and Belgium, the pressure on any party that calls itself socialist will be enormous. But since contemporary socialism, in Greece as elsewhere, is bereft of any coherent ideological system or political program to address this matter, I would expect a great deal of turbulence and labor unrest in Greece in the near future and the capitulation of the Greek socialist party to the demands of labor -- which means the continuation of double-digit inflation, continued increases in the debt-income ratio, and the mounting inability of Greece to meet the European Monetary System's (EMS) rather stringent requirements under the Maastricht Treaty.

IX

Finally, I turn to the Maastricht Treaty and its implications for Greece. Greece's entry into the Common Market (and its re-entry to NATO after a lapse of about 5 years) is to be evaluated primarily in political terms -- as lessening the chances of another military coup d'état, or aggression by Turkey or Bulgaria, both of which have expansionist aims in Thrace and Macedonia which have been further heightened over the issue of Skopje Macedonia. That I think is rater obvious. On a broader scale, the importance of the Common Market, and

Greece's continued membership in it, has become even greater with the fall of the Soviet Union and the fracturing and dissolution of its neighboring client states in Eastern Europe.

In this post-cold-war period, the United States has emerged as the sole unchallenged and unchallengeable giant superpower. This I consider a dangerous development, especially if the U.S. government were to be captured, after Clinton, by the extreme right-wing forces obsessed with a baptist-belt messianic approach to the problems of the world. The only counterbalancing possibilities are China, which will take some time to emerge as an effective balancing force to the United States, and a united Europe under the mantle of the common market. And it behooves Greece to be a part of it. But the problems facing Greece in terms of the Maastricht Treaty are grave.

I will first describe the main features of the Maastricht Treaty in broad terms and then look at its implications for Greece. By January 1994 the second phase of the Treaty on European Unity is to be promulgated. The transitory European Monetary Institute (EMI) of Phase 2 will give way to the European System of Central Banks (ESCB) and the European Central Bank (ECB). The business of the ECB will be to establish "an open market economy with free competition, favoring an efficient allocation of resources." And this is to be done with a minimum of interference from outside political forces. The primary objective of the ECB will be "to maintain price stability," and no national central bank or any community government shall seek in any way to impose its will on the ECB. Complete political independence of the community central bank is to be guaranteed and respected under the Maastricht Treaty. This move towards a community-wide monetarism repudiates the notion that in a democratic society when responsibility <u>for</u> something increases, responsibility <u>to</u> must also be increased.

The target of the ECB is to be the community-wide price level or, as others have suggested, the community-wide level of nominal gross domestic product. In either case, what is being followed is a form of Volckerian "pragmatic" monetarism. Fiscal policy to promote full employment is not to be coordinated on a community-wide basis; that will be left to the discretion of member states. Still, national fiscal policies will be constrained by two considerations: (1) the ratio of the planned or actual government deficit to gross domestic product is not to exceed 3 percent, according to the Protocols attached at the end of the Maastricht Treaty, and (2) these same Protocols require that the ratio of government debt to gross domestic product is not to be greater than 60 percent.

Significantly, there is no mention of an incomes policy to control nominal wages or a credit policy to guide the flow of credit in the overall economy of the common market. The private market mechanism is to prevail unencumbered by government interference. It is significant that the socialist government of France announced in 1993, before its collapse in the March elections, that the Bank of France was henceforth to be insulated from all political interference and influence, as in the case of the Deutsche Bundesbank. And there is no reason to believe that the new conservative Baladur government will reverse this policy decision. Presumably, the two major central banks of Europe are to dominate the ECB despite its broader configuration under the Maastricht Treaty.

There is to be, in short, no demand management in real terms, i.e., no planned rate of real economic growth or any unemployment rate target. There is, furthermore, an implicit assumption that the community-wide velocity function, that is, the underlying financial structure of the European Union, will be stable and well-behaved. If, as a result of community-wide deregulation and liberalization, a wave of financial speculation and innovation takes place (as was the case in the United States during the 1980s) the community will be faced with marked shifts of the velocity function that will counteract and make a mockery of ECB monetary policy and its target of price-level stability. The Financial Sphere could well engage in "stealing" resources for the Industrial Sphere. What I am arguing is quite simple: there is no easy fix, no gimmick that can avoid the need for a community-wide coordination of all facets of economic policy -- an incomes policy and a credit policy adequately supported by the traditional Keynesian tools of monetary and fiscal policy. I consider this a fatal flaw in the Maastricht Treaty.

Yet, this is the Treaty that the Greek parliament ratified and that Greece will have to live under. What are its implications for Greece? First, it will have to reduce the actual government deficit-GDP ratio from 20.7% in 1990 (the latest available figures although the 1992 figures, I have been told, will probably be in the range of 12 to 15 percent) to 3% -- which it has never attained in all of the 20 years since the fall of the colonels. Next it will have to bring down the debt-GDP ratio from a soaring 150 percent (including off-budget items) to 60%, which was last attained 13 years ago, just before PASOK came to power.

In order to meet these two Maastricht Treaty requirements, the government will have to impose an unemployment-raising austerity program far more severe than the current one of the New Democracy Party. As it is, the current austerity program of the Mitsotakis government, with elections hovering on the horizon, will most probably be reversed in keeping with the "political trade cycle" that is so particularly Greek.

Next, major changes will have to be introduced in the financial sphere. The Central Bank will have to be cut loose from the policy-setting Currency Committee and the government will no longer be able to finance its deficits through the banking system. On the inflation front, Greece will have to move from its chronic double-digit inflation rates to no more than 1½ percentage points of the three best performing member states in terms of price stability. That means, given the 3 lowest inflation rates in 1991 and 1992, the Greek inflation rate should not exceed 4.7%. To grasp the magnitude of the problem one need only consult the latest July 1992 Monthly Statistical Bulletin of the Bank of Greece. From 1985 to July of 1992 the Consumer Price Index (CPI) for the European Community rose by 36.5%, or at a 4.4% growth rate over that 7-year period. For Greece, for the same 7-year period, the CPI increased by 200.9% (or more than doubled) yielding a growth rate of 17.1%. The lower inflation rate based on the three lowest European Community members would, moreover, have to be a sustainable rate of inflation, not a one-year flash in the pan.

The Maastricht requirements on deficit and debt ratios and the rate of inflation are a tall order for Greece. Of course, an extension of the 1997, or at the latest 1999, deadline for Phase 3 governing the ESCB and the ECB may be granted for Greece and Portugal, but then Greece will not be in a position to reap the major benefits of the Economic Union under the Maastricht Treaty, and there is the further danger of the European Community becoming a two-tier system of rich and poor members.

More immediately, Greece will have to start moving now to overhaul its financial structure. The banking system will have to be liberalized and deregulated. This needs badly to be done but there are dangers in doing so if it is overdone or done too hastily without sufficient forethought. The banking and monetary system of Greece is primordial. To limit the maximum value of the currency unit to 5,000 drachmas borders on the absurd. I had one banker justify this to me by saying that if larger denominations were to be issued, the Greek people would lose confidence in their currency. I found that a startling argument: the higher the denomination the less value it and all other pieces of currency would have! I have watched people come into banks with briefcases stuffed with bundles of 5,000 drachma notes, and I have watched others similarly go out. One could retire quickly in this country by high-jacking these briefcase holders either on their way in or on their way out. As it is, bank robbers have declared open season on the banks themselves, which obviously hold more cash than any briefcase could. If bank security guards and electronic equipment will now be installed, as required by law, I would expect the briefcase carriers to become substitute targets. Then, too, there is the absence of personal checking accounts which requires endless standing on lines to pay one's rent and utility bills at banks and post offices. Greece is, indeed, a satchel-cash economy and I suspect this has a lot to do with tax evasion and the underground economy. The inefficiencies this system entails are, from my point of view, mind boggling.

With deregulation, however, comes the possibility of uncontrolled and spontaneous financial innovations and the upward shifting of Greece's velocity function thereby making a mockery of the monetary policy of a now independent central bank. The Greek velocity function has been stable largely because of the endogeneity of the money supply. The moderate banking deregulation that was instituted about 1987 resulted in a sharp rise in velocity from 5.2 in 1984 to 6.8 in 1989. Full deregulation could see it rise even more sharply thus making the central bank's ability to meet the requirements of the new ECB all that more difficult.

There is another aspect of the Maastricht Treaty that needs looking into. With the opening up of the European Community's borders on January 1, 1993, capital and labor are free to move from one country to another. Labor will not move so freely largely because of language and cultural differences, not to mention the spate of ugly racial and ethnic incidents in the main, more economically advanced countries of the Economic Union. The equilibrating mechanism will therefore have to rely more heavily on capital movements. But before this can be done on a significant level, Greece will have to invest heavily in improving its infrastructure -- its telephone system which is unbelievably bad, roads, sewage treatment plants, underground garages in greater Athens, and a greatly expanded and modernized urban transportation system far beyond the extension of the metro system now under way.

There is still another type of investment that has been largely neglected. Greek expenditures on social welfare and education are the lowest in the Economic Community. Investment in human capital is woeful. Its university system is in need of a major overhaul and the salaries of professors and teachers are pitiful. A full professor in a university at the top of his career earns about $18,000 a year, which means he is forced to do outside consulting or even hold down a second job -- perhaps in the underground economy. I find this appalling. There are no graduate faculties in Greece. Virtually all professors have earned advanced degrees abroad. And the quality of Greek higher education carries little weight internationally. Greek young people are badly served. A particular bone of contention is that the Greek government is the only one that does not contribute to its local the Fulbright Foundation -- which has done so much with its limited resources, to send bright young Greek students to the U.S. for graduate training.

There is clearly something very wrong with Greek priorities. One way of finding the funds for these badly needed expenditures would be to increase the tax base by strong tax reinforcement and attacking the problem of the underground economy by making it harder to avoid income reporting -- especially by the real estate holding rich and non-salaried business men, lawyers, and doctors, among others.

X

I am afraid my talk has been overlong and overly pessimistic, so I would like to end my discourse on a note of hope. This time, in my eight-month stay in Athens, I have met and spoken to many young intellectuals and economists. They are very much aware of the problems of Greece and, to use Cherneschevskly's famous and purloined phrase, of the need to determine What is to be Done" There are also cadres within PASOK (and I hope in the New Democracy Party) who would like to turn things around and open the parties up to a freer discussion and exchange of ideas.

It is time, as has happened in the United States with the election of President Clinton, to sweep away the ideologically and morally bankrupt old guard. To borrow from Michel Rocard, Greece needs to ignite a political big bang based on a stable party structure, with the members of parliament nominated and elected by their particular electoral districts, not by aging charismatic leaders who, like the Lord High Executioner in the Mikado, have their little (electoral) lists and who quickly become obstacles to progress or dissent. And without dissent there can be no progress.

Thank you for your attention. I am now open to questions, statements, attacks, and brickbats.

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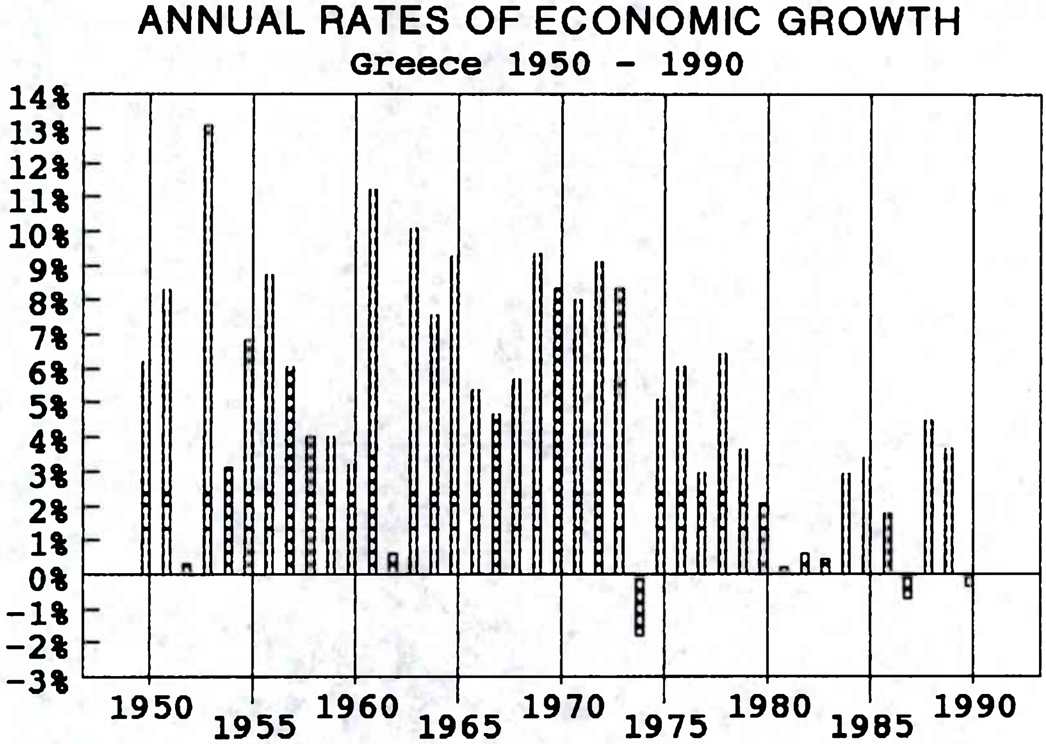
A P P E N D I X

Billions of drachmas; Real GDP in 1970 prices

YEAR	NOMINAL GDP	ANNUAL GROWTH RATE	REAL GDP	ANNUAL GROWTH RATE	RATE OF INFLA-TION	M1	ANNUAL GROWTH RATE	V
1950	30	20.2%	74	6.2%	14.0%	2.6	11.8%	11.540
1951	36	19.1%	81	8.3%	10.9%	3.2	22.7%	11.209
1952	38	4.2%	81	0.3%	3.9%	3.6	10.5%	10.572
1953	49	30.8%	91	13.1%	17.7%	5.2	46.8%	9.417
1954	57	15.2%	94	3.1%	12.1%	6.1	17.9%	9.204
1955	65	14.7%	101	6.8%	7.9%	7.7	24.8%	8.461
1956	75	15.9%	109	8.7%	7.2%	8.7	12.8%	8.690
1957	80	6.9%	116	6.0%	0.9%	10.3	18.7%	7.830
1958	84	4.0%	120	4.0%	0.0%	11.2	9.3%	7.456
1959	87	4.1%	125	4.0%	0.1%	13.1	16.2%	6.675
1960	93	7.0%	129	3.2%	3.8%	15.5	19.0%	6.004
1961	105	12.5%	144	11.2%	1.4%	17.8	14.8%	5.884
1962	111	5.7%	145	0.6%	5.1%	20.5	15.0%	5.410
1963	123	11.3%	159	10.1%	1.2%	23.6	15.2%	5.228
1964	139	12.3%	171	7.5%	4.8%	28.2	19.3%	4.921
1965	158	13.9%	187	9.2%	4.7%	32.3	14.7%	4.885
1966	175	10.7%	197	5.3%	5.3%	35.9	10.9%	4.875
1967	188	7.8%	206	4.7%	3.1%	43.4	21.1%	4.340
1968	203	7.5%	218	5.7%	1.9%	45.2	4.2%	4.479
1969	229	13.0%	238	9.3%	3.7%	49.0	8.2%	4.676
1970	258	12.7%	258	8.3%	4.4%	54.3	10.9%	4.749
1971	287	11.4%	279	8.0%	3.4%	61.8	13.8%	4.651
1972	330	14.8%	304	9.1%	5.7%	76.1	23.1%	4.339
1973	428	29.8%	329	8.3%	21.4%	93.1	22.5%	4.598
1974	507	18.5%	323	-1.8%	20.3%	111.5	19.7%	4.551
1975	593	16.9%	340	5.1%	11.8%	128.9	15.6%	4.602
1976	729	22.9%	360	6.1%	16.8%	160.0	24.1%	4.555
1977	845	15.9%	371	2.9%	13.0%	187.0	16.9%	4.516
1978	1,017	20.4%	395	6.4%	14.0%	228.6	22.2%	4.448
1979	1,254	23.4%	409	3.6%	19.7%	264.5	15.7%	4.743
1980	1,524	21.5%	418	2.1%	19.4%	313.1	18.4%	4.867
1981	1,860	22.1%	418	0.2%	21.9%	385.9	23.3%	4.819
1982	2,311	24.2%	421	0.6%	23.7%	471.2	22.1%	4.903
1983	2,733	18.3%	422	0.4%	17.9%	535.7	13.7%	5.102
1984	3,363	23.0%	435	2.9%	20.1%	651.6	21.6%	5.161
1985	4,137	23.0%	449	3.4%	19.6%	797.4	22.4%	5.188
1986	4,873	17.8%	457	1.7%	16.1%	879.7	10.3%	5.539
1987	5,465	12.1%	454	-0.7%	12.9%	843.4	-4.1%	6.479
1988	6,578	20.4%	474	4.5%	15.9%	973.2	15.4%	6.759
1989	7,822	18.9%	491	3.7%	15.2%	1,264.9	30.0%	6.184
1990	9,215	17.8%	490	-0.4%	18.2%	1,583.4	25.2%	5.820

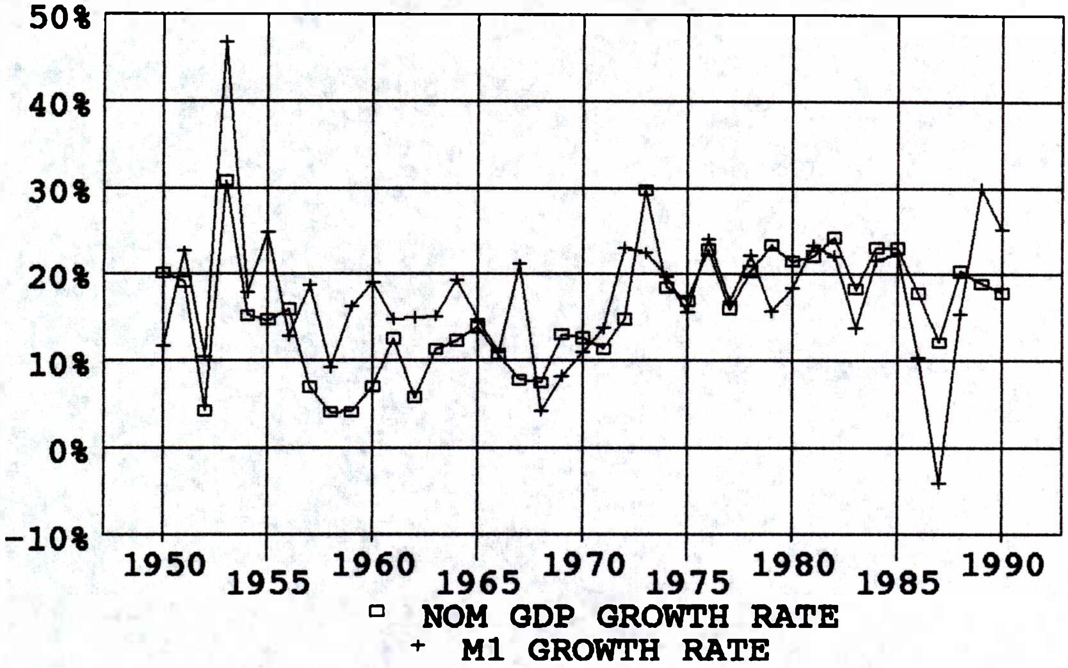
Coup d'Etat: 1967; Elections: 1974, 1977, 1981, 1985, 1989

SOURCE: Bank of Greece

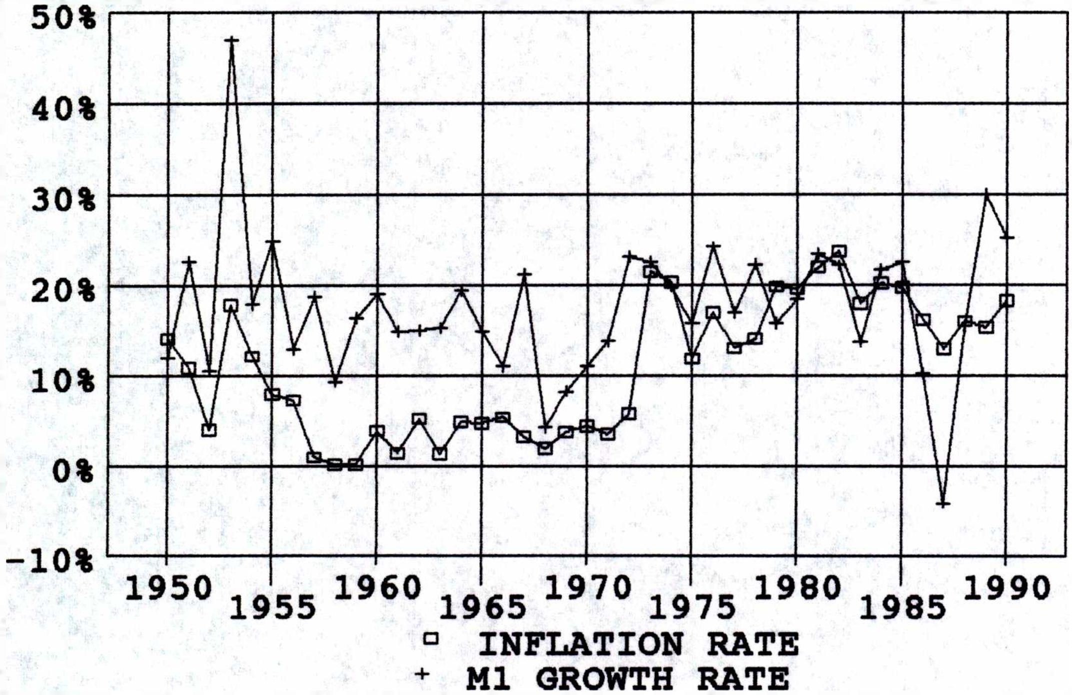


NOTE: Post-1967 Coup Elections: 1974, 1981, 1985, 1989

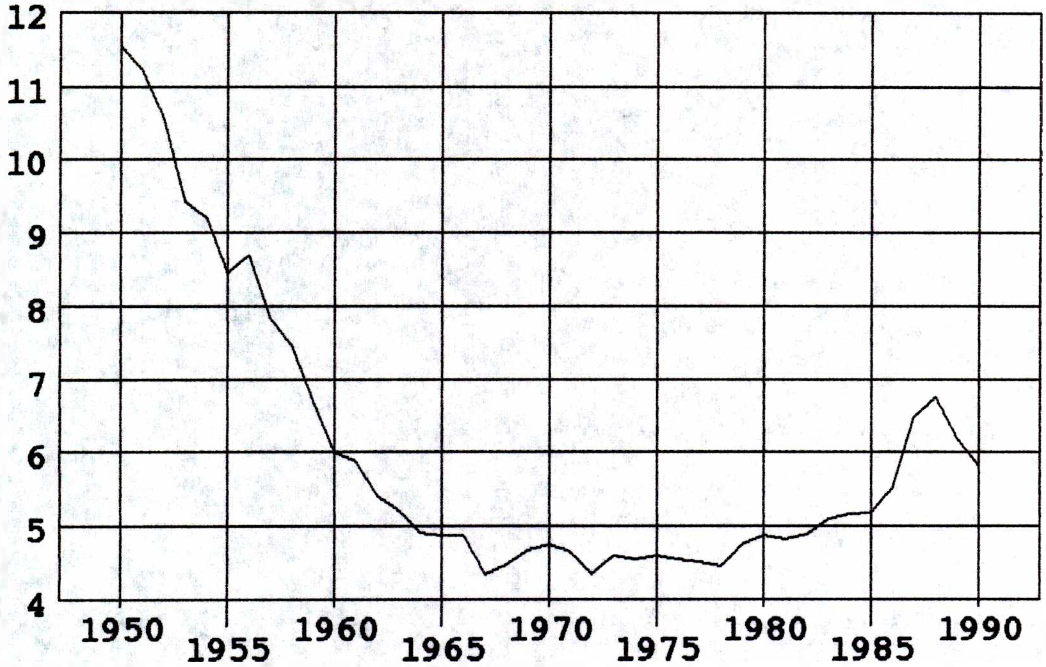
NOMINAL GDP AND M1 GROWTH RATES
1950-1990



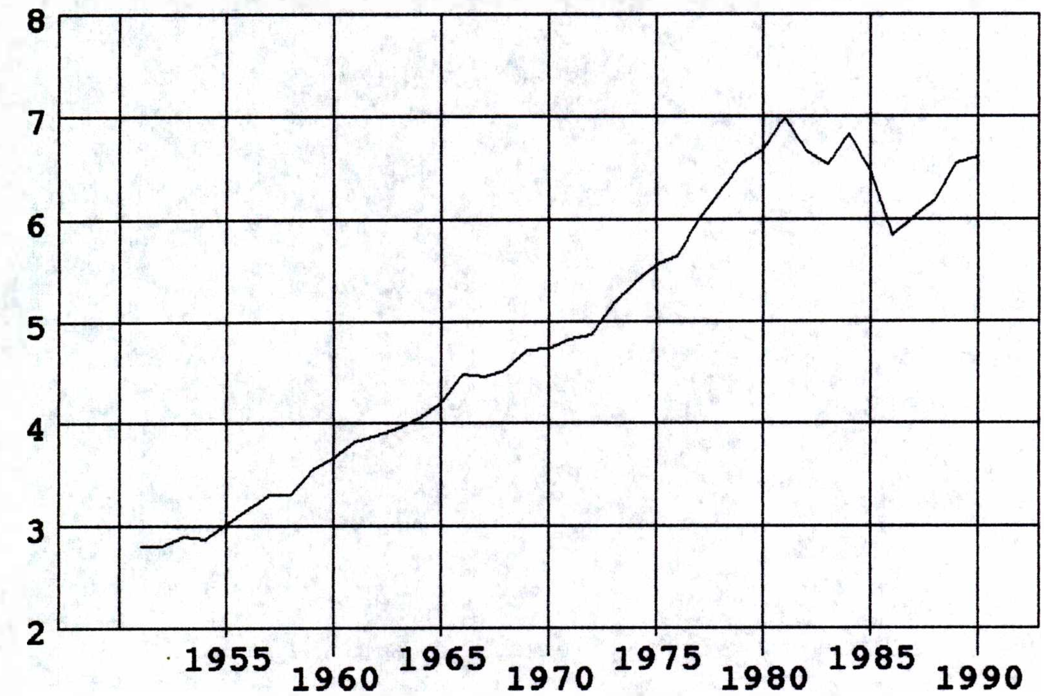
PRICE LEVEL AND M1 GROWTH RATES
1950-1990



GREEK INCOME VELOCITY OF MONEY
1950-1990



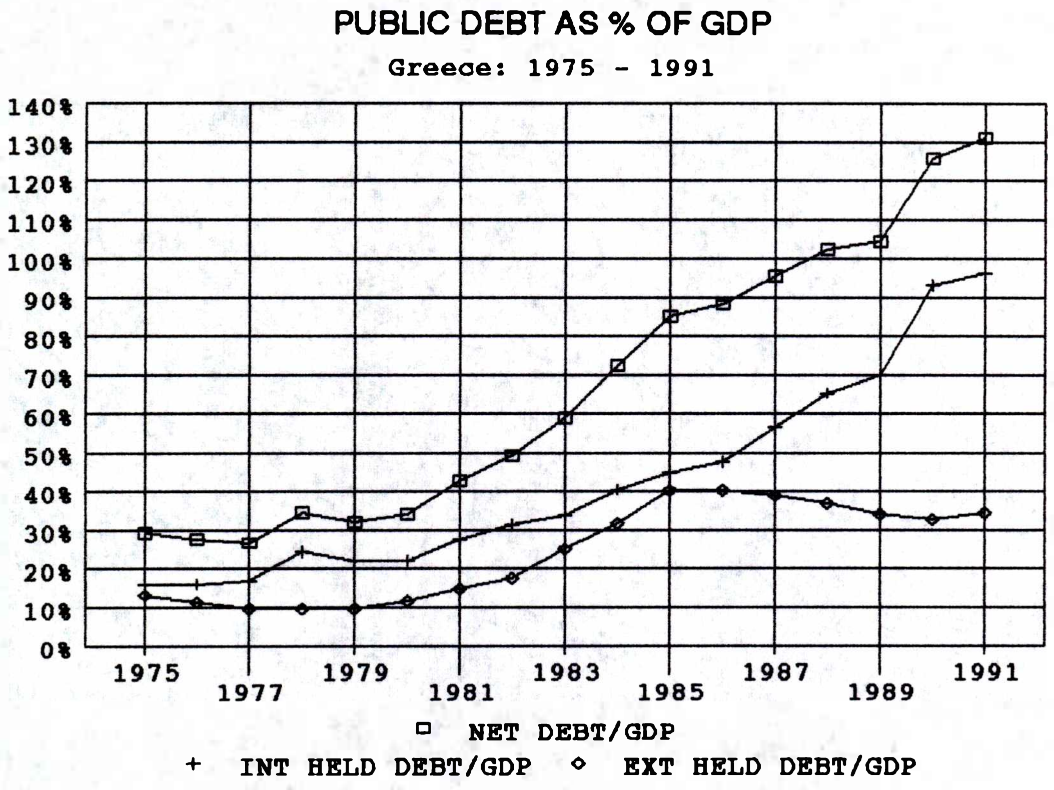
U.S. INCOME VELOCITY OF MONEY
1951-1990



(Billions of drachmas)

YEAR	NOMINAL GDP	ANNUAL % CHANGE	INTERNAL PUBLIC DEBT	ANNUAL % CHANGE	% GDP	EXTERNAL PUBLIC DEBT	ANNUAL % CHANGE	% GDP	TOTAL NET DEBT	ANNUAL % CHANGE	% GDP
1975	593	16.9%	94	---	15.9%	80	---	13.5%	174	---	29.4%
1976	729	22.9%	118	24.8%	16.2%	84	5.5%	11.6%	202	16.0%	27.7%
1977	845	15.9%	144	22.2%	17.0%	82	-2.1%	9.8%	226	12.1%	26.8%
1978	1,017	20.4%	252	74.9%	24.8%	100	21.6%	9.9%	352	55.5%	34.6%
1979	1,254	23.4%	280	11.0%	22.3%	124	23.9%	9.9%	404	14.7%	32.2%
1980	1,524	21.5%	339	21.3%	22.3%	182	46.3%	11.9%	521	29.0%	34.2%
1981	1,860	22.1%	516	52.1%	27.7%	281	54.7%	15.1%	797	53.0%	42.8%
1982	2,311	24.2%	729	41.3%	31.5%	412	46.7%	17.8%	1,141	43.2%	49.4%
1983	2,733	18.3%	927	27.1%	33.9%	688	67.1%	25.2%	1,615	41.6%	59.1%
1984	3,363	23.0%	1,364	47.2%	40.6%	1,073	55.9%	31.9%	2,438	50.9%	72.5%
1985	4,137	23.0%	1,857	36.1%	44.9%	1,671	55.6%	40.4%	3,527	44.7%	85.3%
1986	4,873	17.8%	2,330	25.5%	47.8%	1,970	17.9%	40.4%	4,299	21.9%	88.2%
1987	5,465	12.1%	3,090	32.6%	56.5%	2,140	8.7%	39.2%	5,230	21.6%	95.7%
1988	6,578	20.4%	4,308	39.4%	65.5%	2,439	14.0%	37.1%	6,746	29.0%	102.6%
1989	7,822	18.9%	5,495	27.6%	70.3%	2,689	10.3%	34.4%	8,184	21.3%	104.6%
1990	9,257	18.4%	8,631	57.1%	93.2%	3,035	12.9%	32.8%	11,666	42.5%	126.0%
1991	11,109	20.0%	10,723	24.2%	96.5%	3,854	27.0%	34.7%	14,577	25.0%	131.2%

ELECTION YEARS: Oct 1977; Oct 1981; June 1985; June 1989



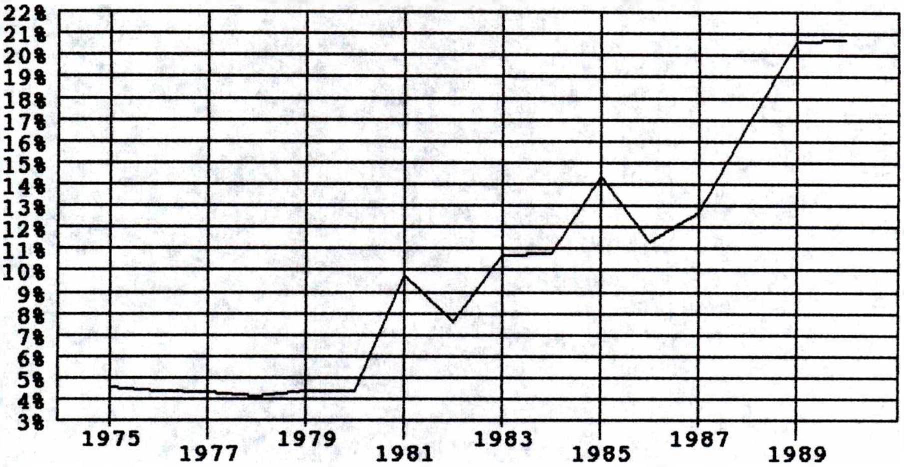
NOTE: Election Years 1977, 1981, 1985, 1989

(Billions of drachmas; expenditures net of amortisation)

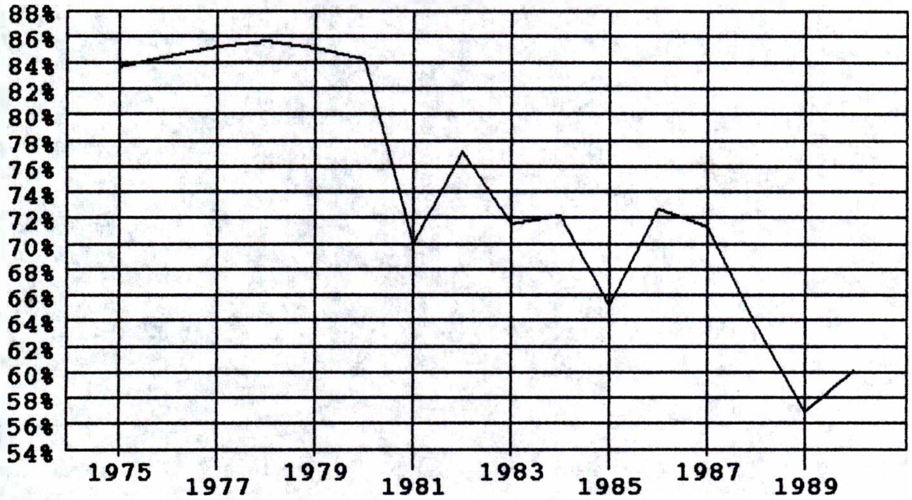
YEAR	NOMINAL GDP	REVENUES	NET EXPEND	NET DEFICIT	% GDP	REV/NET EXPEND	INDIRECT TAXES	DIRECT TAXES	IND/DIR RATIO
1974	507	105	125	20	3.9%	84.2%	68	28	2.408
1975	593	138	165	27	4.6%	83.6%	92	29	3.142
1976	729	175	207	32	4.4%	84.5%	114	47	2.408
1977	845	210	247	37	4.3%	85.2%	140	48	2.930
1978	1,017	249	291	42	4.1%	85.6%	168	62	2.730
1979	1,254	314	370	55	4.4%	85.1%	207	81	2.559
1980	1,524	359	426	67	4.4%	84.3%	221	104	2.114
1981	1,860	424	606	182	9.8%	69.9%	265	124	2.145
1982	2,311	590	765	175	7.6%	77.1%	375	175	2.140
1983	2,733	736	1,028	293	10.7%	71.6%	478	201	2.378
1984	3,363	934	1,295	361	10.7%	72.1%	595	253	2.350
1985	4,137	1,114	1,709	594	14.4%	65.2%	722	303	2.384
1986	4,873	1,465	2,017	552	11.3%	72.6%	972	386	2.515
1987	5,465	1,728	2,423	695	12.7%	71.3%	1,157	440	2.631
1988	6,578	1,936	3,037	1,101	16.7%	63.7%	1,266	520	2.436
1989	7,822	2,135	3,751	1,616	20.7%	56.9%	1,391	581	2.396
1990	9,257	2,888	4,806	1,918	20.7%	60.1%	1,877	822	2.283

ELECTION YEARS: 1974, 1977, 1981, 1985, 1989

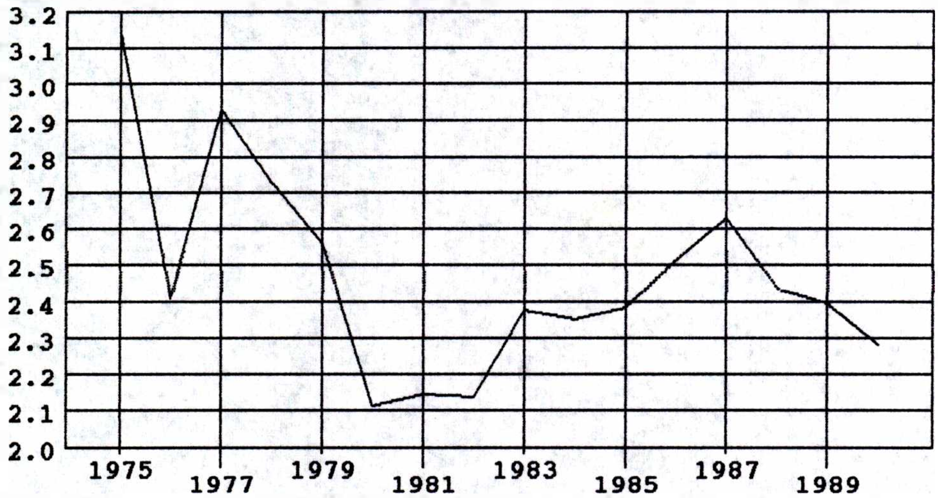
NET DEFICIT AS PERCENTAGE OF GDP
Greece: 1975 - 1990



GOVT REVENUE AS % OF NET EXPENDITURES
Greece: 1975 - 1990



RATIO OF INDIRECT TO DIRECT TAXES
Greece: 1975 - 1990



NOTE: Election Years 1977, 1981, 1885, 1989