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By

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Abstract

Greece went bankrupt in 2009 presumably because it run an exorbitant public deficit and had accumulated a huge public debt. However, in reality Greece went bankrupt because its model of social and economic organization has been surpassed by European and international developments. To avoid this tragedy, Greece had been given by EEC initially and EU later on enough time to prepare before integrating into the Eurozone. From the treaties it signed Greece ought to have introduced structural transformations to render its economy consistent with the four European freedoms. Instead, time and again successive governments procrastinated and employed all sorts of gimmicks to protect the model of state socialism they had erected on the pillars of the 1975 Constitution. But time and circumstances caught up with their policies and now the cost for confronting the challenges that lie ahead has become enormous. Hopefully, sooner than later, those responsible for the bankruptcy of Greece and the hardships that have befell on the Greek people will discover that their self-interest coincides with that of the country and they will take the lead in the replacement of the present hard core statist model with one based on free and open markets and outward looking entrepreneurship.

[1] This paper has gone through several versions and elaborate discussions with Alexander Skouras, head of the Center for Liberal Studies (KEFIM), and Dr. George Archontas, of the University of Peloponnese. Particularly the latter drafted some early versions of section 2 and sub-section 3.7 and gave me the benefit of an extensive range of challenging comments. I thank them both very much and absolve them from all and any responsibility regarding the views expressed in the paper.

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Preface

When the 2008 international financial crisis washed ashore in Greece in 2009, the private sector of the economy was fairly healthy. According to calculations presented by Bitros (2015), in 2011 the value that the average Greek worker in this sector added to the Gross National Product (GDP) was about 61.000 Euros, whereas the same figure in Germany, the most productive EU country, was about 67.000 Euros. In the same year the average public employee in Greece produced goods and services worth about 25.000 Euros, whereas the productivity of the average civil servant in Germany was much closed to that in the private sector. What these comparative statistics suggest is that, if governments in Greece decided rationally as to how best to weather the crisis that erupted ostensibly because of the public deficit and the huge public debt, the most obvious path was to place the brunt of the adjustment on the public sector by reducing employment, eliminating wasteful expenditures, and carrying out much needed structural transformations so as to bring its productivity on a par with the private sector. This policy would have been strongly economic growth enhancing and in a few years the country would have returned to normalcy.

Instead, the successive post-2009 governments that were elected to confront the crisis chose the opposite policy mix. They proposed to the creditors and unfortunately, under the coaching of the European Union (EU) and the International Monetary Fund (IMF), the latter agreed to pile increasingly taxes upon taxes on citizens and businesses as if Greece's problems could be solved by confiscating private wealth in order to preserve the public sector intact[2] and the old political order in place. The result was that thousands of small and medium size enterprises shut down, unemployment shoot close to 30% and among the young nearly to 60%, joblessness gave rise to a robust brain drain from which it will take years for the country to recuperate, GDP declined by as much as 25%, and guess what, the public debt climbed to 180% of GDP and the Non-Performing Loans (NPLs) skyrocketed, thus perpetuating the uncertainty over capital controls and more generally the stability of the banking sector. Did they know that there was another faster and more effective way out of the tax to death spiral they sponsored? Surely they did. But they did not consider it because it implied the abandonment of the statist model of economic and social organization that they pro-

[2] The investigative report by Kostoulas (2015) is full of statements by researchers and technocrats, some of them closely associated in one way or another with the so-called "memoranda", to the effect: " Let us not kid ourselves, Greek governments of the period 2009-2013 aimed at protecting their clients wherever they were found, in the public sector or for example in select groups of pensioners." And the policy mix in favor of raising taxes rather than cutting public expenditures became far worse under the current leftish government.

moted throughout the post war period.[3]

Having applied the so-called “memoranda” for eight years now, the light out of the long tunnel in Greece’s social and economic crisis looks nowhere near. Rubbing oil to the wounds, the politicians and economists who concocted these shortsighted policies proclaim that they do not understand why Greek and foreign investors shun Greece as an investment destination. Although we observe daily numerous examples of the state’s enmity toward entrepreneurship, they pretend that they do not see how the lack of trust in the country’s leadership keeps the business climate in the negative and the cohesion among citizens in shambles. Nothing will do short of a complete reversal of Greece’s defunct social and economic model on which they have staked their carriers. Therefore, the soonest they relent, the soonest effective governance and institutions will encourage Greek and foreign investors to regain their confidence and with their investments drive Greece to a path of robust economic growth.

Hope dies last. Yogi Berra, famous manager of the football club New York Mets, when it was late in the game and his team was hopelessly behind in the score, used to express the same stance by saying “The game is not over until is over.” The battle to turn Greece into a country in which substantive democracy grounded in the four European freedoms reigns for good started only recently, instigated mostly by the mixed-blessing of the 2009 bankruptcy. Thus, irrespective of past disappointments, with this essay I wish to reiterate that the end game is for Greece to win, provided that reforms like the ones suggested in Section 5 are at last implemented.

1. The root causes of Greece’s malaise

In the postwar period prior to 1974 Greece achieved: high economic growth rates (≈ 7%), enviable price stability (<2.5%), which enhanced the international competitiveness of Greek products and services and maintained the balance of payments under manageable control, remarkable reduction of unemployment (<2.5% in the 1970s), improvement and expansion of social services, and all with very limited public debt (<12.5% of GDP in 1974). After 1974 and up to 2008, economic growth fell to about one third (≈ 2.4%), the unemployment rate, which more than doubled

[3] To substantiate this statement, it is worth mentioning that on December 9, 2012, the Sunday edition of the well respected and widely read Greek newspaper *Kathimerini* devoted a whole page to an article by Bitros (2012). In line with its title, this article explained what had gone wrong, particularly after 1974, and proposed a full-fledged program of reforms and policy initiatives which would have spared Greece from its never ending tragedy within a reasonable time span. But it was met with indifference and scorn because ostensibly it was of a “neo-liberal” bent.

in the period 1980-2000 (≈ 6%), in the decade of 2000 nearly quadrupled (≈ 9%), the explosive deficits in the balance of payment were contained only thanks to the huge EU aid, and the budget deficits pushed public debt to an unsustainable ratio (≈ 125% of the GDP in 2009).[4]

Due to this extraordinary reversal, friends of Greece everywhere as well as experts wonder: What ever happened and from the phase of spectacular economic expansion in the two decades to 1974 Greece regressed and now stands on the verge of an open bankruptcy?

Some economists have attributed this development to Greece's accession in 1981 to full membership in the EEC. But the evidence is that:

- Most relevant indices started worsening from 1974 on, whereas import duties declined only gradually after 1984.
- Frequent devaluations of the drachma delayed but did not halt the ominous downward trend in the main sources of economic growth, and,
- In order to cope with the gradual opening up of its markets to European competition, Greece received significant amounts of financial assistance through EEC's Mediterranean Programs.

Hence, the accession was not the culprit and, moreover, if Greece had elected to continue as an associate member-country, quite likely she would have gone bankrupt much earlier.[5]

By focusing in this essay mainly on the economy, the objective in the present section is to explain why the root causes of Greece's malaise lie in the fundamental contradictions between Greece's postwar statist model of social and economic organization and the European aspirations of the great majority of its people.

1.1 The Greek statist economic model

When the usefulness of Greece's association with the European Economic Community (EEC) was debated in the late 1950s, the issues regarding exports were neither the only ones nor the most important. The main focus of the debate was on the structural reforms that Greece would have to adopt in order to integrate smoothly within the 22 years of adjustment that were provided

[4] For the documentation of these data, see Bitros, Karayiannis (2013, pp. 197-247).

[5] How closed to bankruptcy Greece came in 1985 and 1989 can be glimpsed from several sources. For example, regarding the cliff-edge precariousness of public finances and debt in 1989, see the well documented article by Papandropoulos (2017).

for in the agreement.[6] To ascertain that this was the case, here is how Papandreou (1962), renowned Professor of Economics and advisor to the Greek government at the time, summed up the challenges that Greece confronted:

> *Greece has recently concluded an Association Agreement with the European Common Market with the prospect of full membership some 22 years hence. It is fair to say that, given the terms of the association, Greece has a small margin of time in which to achieve the structural transformations needed for survival in the European Common Market. (p. 25)*

Moreover, regarding the nature and range of the "structural transformations" that were needed, Papandreou advised:

> *There is a pressing need to streamlining the presently cumbersome "system" of government regulation of economic activity. In some sense there is "too much" government on the Greek economic scene, while there is too little research and too little planning, and the organizational apparatus for the execution of various plans is practically absent. The mosaic of fiscal credit and market regulations which are subject to abrupt changes without notice can hardly be expected to encourage private investment activity of the right kind. (p. 103)*

> *Where the market mechanism, the competitive process is allowed to perform the resource-allocation task, it ought to be allowed to work. The rewards for success should be high—but so should be the penalties for failure. The barriers to entry—which in Greece reach unusual heights—ought to be lower if not removed. "Saturated" lines of endeavour and "closed" professions ought to be exposed to the rigors of the competitive process. (p. 104)*

> *It is essential to come to understand that an efficient export sector cannot be grafted upon an inefficient economy. Greece's low capacity to export is a symptom of structural weakness, of resource misallocation, of missing links in the distribution chain—and should be handled as such. Special measures, such as preferential credit and fiscal treatment for export-oriented firms, while of doubtful effectiveness in the short-run, are often distinctly harmful in the long-run. (p. 105)*

Yet when the same Papandreou took over as Prime Minister of Greece in 1981, not only he forgot what he advised back in the 1960s, but his successive governments enacted policies that pushed Greece further into a statist country with social and economic organization based on precept of central planning and administrative controls. For example, Gwartney, Lawson (2006) find that from 1980 to 2008 Greece with respect to: (a) property rights protection fell to

[6] The agreement was partially frozen for 7 years (1967–1974) at the initiative of the EEC Commission as a reaction to the military regime that assumed power in Greece in 1967. It was re-entered into force upon the restoration of parliamentary democracy in 1974. Subsequently, Officially Greece became a full member of the EEC in 1979 and of the European Monetary Union (EMU) in 2000.

the 50th position from the 25th; (b) the conditions for commerce, mainly towards third countries, tumbled to the 80th position from the 39th; and (c) state regulations in credit markets, labor markets, and enterprises, slipped to the 90th position from the 72nd. Moreover, it is noteworthy that on the basis of price controls and barriers to entry in product and services markets, Mylonas, Papaconstantinou (2001) find that in 1998 Greece ranked as the most illiberal country in the European Union.

To conclude, those[7] who shaped Greece's postwar political and economic order promoted an institutionally mired democracy with a relatively large and inefficient public sector in conjunction with a relatively small, inward looking, and predominantly state-controlled private sector. Over the decades this order grew closer to a collectivist state, rather than a democracy based on free markets as mandated by the treaties Greece signed with the European Union (EU). The key to understanding the nexus of forces that morphed into the malignant status quo that led Greece to bankruptcy, it is not hard to identify.

1.2 The "national goal" of joining the Eurozone

While serving as head of the main opposition party after 1974, Papandreou had taken a highly anti-American and anti-European stance. It is not an exaggeration to say that actually his party won the elections in 1981 by him proclaiming that the EEC and NATO "represented the same evil syndicate", and by threatening to take Greece down to a Third-World socialist path.

In this political context, Papandreou inferred that: (a) Greece commanded certain geopolitical advantages that he could leverage in return for EEC accommodation to his socialist policies; (b) since the EEC had condoned the strongly interventionist policies of the previous so-called "liberal" governments, no objections to transgressions from the mandates of the Treaty of Rome would be raised, and (c) given the wide gap in living standards that existed and the cost Greece would absorb by opening her markets to European competition, a strong case could be made for renegotiating the terms of the 1979 Accession Agreement, as well as asking for generous financial assistance.

The EEC authorities refused to renegotiate the Accession Agreement but gave in pretty much in all other demands made by Papandreou's governments in the 1980s. Thus, a precedent

[7] The term "those" refers here to a group of specific politicians and intellectuals who, with their ideas and decisions from the high government posts they occupied in their lives, influenced markedly the course of events in the post war period in Greece. For four of them, the interested reader may wish to see Bitros, Karayiannis (2011).

of ill-conceived EEC concessions was established, which lasted until successive governments made a series of mischievous errors that destabilized public finances, drove the competitiveness of Greek products to nadir, and finally in 2009 led to the country's imminent default. At that precise juncture, as it became demonstrably clear that no Greek leader would dare undermine the national goal of integrating into the Eurozone, the foreign creditors led by EU gained the upper hand and started to dictate the terms for shifting Greece's social and economic order towards a more sustainable European standard.

Appraised from this standpoint, the three "memoranda" imposed on Greece so far aim to bring about the "structural transformations" Papandreou was talking about in the early 1960's. By implication, either EU will succeed in turning Greece into a genuine free market based democracy or the European project may unravel in the face of the great Moral Hazard Greece's statist model poses for the wider European community of nations.

1.3 The non sequitur of Greece's statist model in the EU setting

All formative EU treaties, i.e. from the 1957 Treaty of Rome to the 1986 Treaty of the Single European Market and the Growth and Stability Pact of 1997, are based on the quest for four freedoms. That is, the free and uninhibited movement of workers, products, services and capital. Therefore, all member-states are obliged to abide by them and to strive for their timely implementation.

In the case of Greece, due to historical and geopolitical circumstances, EU authorities condoned, mostly tacitly but at times also explicitly, numerous digressions from these freedoms. For example, the 1975 Constitution of Greece abounds in provisions that are in conflict with one or more of these freedoms, and hence, it ought to have been considered a stumbling block in the 1979 Accession Agreement. It did not. But now that the balance of negotiating power has shifted in their favor the EU authorities cannot pretend that they do not see the non sequitur between the Greek statist model and the four freedoms. For it is clear that by allowing Greek governments to escape in various degrees and forms from the country's European obligations, the pressure for reforms is defused in favor of the status quo.

2. Coping with the crisis: A poor prescription, poorly executed

Greece has managed for the time being to escape defaulting and exiting the Eurozone and it has even begun to show some signs of stabilization. However, its economy has been in limbo for 8 years now. So the question whether this poor performance is due to the adopted policy mix or its poor implementation is mostly a rhetoric one, since both have contributed to the final result, which translates into too slow recovery and too high economic and social costs.

2.1 Lack of trust and the general aversion to change

Skalkos (2016) aptly notices that Greece falls into the “blocked society” category coined by Giddens (2007), where vested interests and aversion towards “structural transformations” undermine any reform effort. Notably, even though 74% of Greeks that participated in the November 6, 2015, European Commission's Eurobarometer survey stated that they viewed favorably the implementation of reforms in the economy, nearly every single one implemented met with both widespread and intense resistance. This can be attributed to lack of social capital, ideological barriers, and the institutional architecture prevailing in Greece. Following the system of analysis presented by Acemoglu and Robinson (2011), decades of extractive institutional structures have eroded impersonal trust, implying as a result that any proposed change is viewed not only as a zero-sum game, but as an effort to covertly promote the interests of groups having strong ties with the political system.

2.2 Reforms without an owner: Law making vs. actually implementing

Another decisive factor has been the reluctance of successive Greek governments to assume ownership of the reform programs. Presenting the “memoranda” as externally dictated, and hence that they are to be implemented only half-heartedly, if not just nominally, and remain open “renegotiation”, has been the default political practice effectively of every Greek government since the beginning of the crisis. This attitude, coupled with statements by foreign officials, as for example by the EU's Economic Commissioner Pierre Moscovici, who recently stated that the Greek program is “a democratic scandal”,[8] has fueled widespread disbelief that the reform programs could actually help Greece regain its economic momentum in a socially fair way.

2.3 A mixed blessing: Assessing the effects of the “memoranda” period

In view of the above, Greece’s recovery performance can be characterized as a mixed blessing at best, mired by two main problems: Choosing to tax instead of implementing spending cuts, and focusing excessively on the debt instead on competitiveness and growth.

2.3.1 Taxing instead of spending cuts: economic and social effects

The crisis in Greece erupted mainly because of excessive public deficits in conjunction with a

[8] Moscovici: “L' Italia contenga il debito Sì al ministro delle Finanze Ue.” Corriere della Serra, September 3, 2017.

huge and unsustainable public debt. To confront these problems, successive Greek governments have had the option to choose between raising taxes and spending cuts. All chose to place the emphasis of the policy mix on the former than the latter because taxing disperses costs among the general public and thus renders it most politically viable. As documented by the Budget Bureau of the Greek Parliament, the percentage allocation in favor of tax revenues rather than spending cuts reached 94% / 6%.[9]

It is worth noting that the tax burden is such that the Center for Liberal Studies (KEFIM) has estimated that the Tax Freedom Day for Greeks in 2017 was as late as July 23.[10] This overtaxing has undermined recovery and growth and it has given rise to deep felt social problems, with Eurostat data showing that 22.2% of the population in 2015 was "severely materially deprived".

Furthermore, as expected, overtaxing has fueled the already extensive tax evasion, since according to research by Germany's Institute for Applied Economic Research (IAW), the Greek shadow economy stands at 21.5% of GDP.[11]

2.3.2 Focusing on the debt vs. focusing on competitiveness and growth

The need to address the debt sustainability problem cannot be denied nor underrated. But placing the whole focus on the debt question, and using it as a means to convey a hard-lined stance towards the EU and IMF has overshadowed the importance of strengthening competitiveness and growth through "structural transformations".

While some labor reforms have been implemented, and several closed markets and professions have been opened to competition, Greece ranks 61st in the World Bank's Doing Business 2017 Index, falling three places compared to 2016.

As a result, in the aftermath of the 2015 annus hornbills, Greece realized 0% annual GDP growth in 2016, and the estimates for 2017 speak of a very low growth rate, and in any case inadequate to spur a faster and sustainable return to the pre-2009 level of per capita incomes.

3. Continuing challenges

The structure of a market economy, and therefore its propensity to grow or regress, is strongly influenced by which institutions administer the functions of the state, what mechanisms ensure

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[9] Hellenic Parliament, State Budget Office, "Quarterly Report (January – March 2017), May 2017, p. 16.
[10] Prodromos Pyrros, Tax Freedom Day – Greece, 2016-2017, KEFIM "Markos Dragoumis", 2017.
[11] http://www.iaw.edu/index.php/aktuelles-detail/734.

the enforcement of checks and balances among them, how well protected are individual freedoms and property rights in the law and in practice, how large and effective is the public administration, how rampant is corruption, etc. Eight years now into three consecutive years of so-called "memoranda" and a very significant downward adjustment in the living standards of its citizens, Greece does not have much to show in terms of changes in its institutional set-up which has been responsible for the bankruptcy of the country. As a result, most of the hard challenges lie ahead and they will have to be confronted before the business climate changes for the better.

The objective in this section is to focus briefly on a select number of such challenges so as to highlight their nature and foreshadow the difficulties that are involved in turning around the present status quo.

3.1 Too much government that governs badly

Hard data about how large the employment in the public sector has always been, started to appear slowly through studies by various researchers and reports by national commissions, which were appointed to study the problem and propose measures to solve it. One of these studies found that the number of civil servants in 1961 was over 260.000, in 1971 over 320.000 and in 1981 more than 500.000, whereas the census that was conducted in 2010 showed that their number had swelled to 768.000.[12] But the situation over the years was even worse because these data counted only those who worked for the state in legislated positions and left out all others who worked in the wider public sector (e.g. in state-owned enterprises) as well as those that work on a contractual basis. If all are added to the number of civil servants, to the experts in this area it would not come as a surprise if the numbers of those who work in the public sector exceed presently 900.000 or 22% of the labor force.[13] By contrast, Germany employs in the three levels of government, i.e. local, state and federal, roughly 11% of its labor force. Does this comparison demonstrate anything? It does big, because it reveals a gross misallocation in Greece's labor force since, although it lags significantly behind Germany in per capital income, Greece has almost two times the percentage of Germany's labor force working for the least productive sector of the economy.[14]

[12] For the sources and the documentation of these data, see Bitros (2015, pp. 149-153).
[13] According to the Hellenic Statistical authority the labor force in Greece in 2016 comprised 4,071million people.
[14] It is worth noting that in 1987 in an interview published in the newspaper "To Vima," Papandreou, then Prime Minister of Greece, corroborated this gross misallocation by stating "Now we have about double the number of the personnel required in order to provide the necessary state services."

This obvious misallocation is associated with a wide range of pathologies that beset governance in Greece. To save space, I summarize what I would like to emphasize in words by means of Table 1. On reflection, the comparison of the four key indices between Germany and Greece leaves no doubt as to the conclusion that in Greece the government is excessively large and that it governs badly.

Table 1: Quality of institutions and governance in 2015

Governance Score	Government Effectiveness[1]	Regulatory Quality[2]	Rule of Law[3]	Control of Corruption[4]
Germany	1.74	1.67	1.78	1.82
Greece	0.25	0.40	0.24	–0.13

Notes:

1. Government Effectiveness (GE) reflects perceptions of the quality of public services; the quality of the civil service and the degree of its independence from political pressures; the quality of policy formulation and implementation; and the credibility of the government's commitment to such policies.
2. Regulatory Quality: Regulatory quality captures perceptions of the ability of the government to formulate and implement sound policies and regulations that permit and promote private sector development.
3. Rule of Law: reflects perceptions of the extent to which agents have confidence in and abide by the rules of society, in particular the quality of contract enforcement, property rights, the police, and the courts, as well as the likelihood of crime and violence.
4. Control of Corruption: reflects perceptions of the extent to which public power is exercised for private gain, including both petty and grand forms of corruption, as well as "capture" of the state by elites and private interests.

Source: http://info.worldbank.org/governance/wgi/index.aspx#reports

3.2 Poor protection of property

With the possible exception of a small number of legal experts, very few in Greece know how the so-called "conservative" or "liberal" governments under Constantinos Karamanlis overturned property rights in the 1970s. In Bitros (2014) the story is told in Greek to make as many citizens as possible aware of what happened and what we should do. According to one expert writing in 1988:

> *Never before has a conservative bourgeois government shown such contempt for the inviolable of private property.*

In particular, Article 106 in the 1975 Constitution, and not only, opened Aeolus sac. In addition to providing for the central planning of the economy, it offered the institutional pretext for the expansion of the state deep into the economy by using nationalizations and funds from the state-controlled banking sector. For example, in the second half of the 1970s, Karamanlis government carried out several nationalizations, including the S. Andreade's large conglomerate group of companies, comprising banks, industrial enterprises, shipyards, hotels, insurance companies, etc. Unfortunately this was not a onetime small scale isolated industrial policy. It continued into the 1980s under Papandreou's governments and it was never reversed despite the treaties the country signed with EU and the explicit references in them to the four European freedoms. Much to our surprise, until the hell of bankruptcy opened loose in 2009, the EU authorities stood by as simple observers.

In the bibliography in Greek pro-market researchers cite the above mentioned instances as an indication of the "socialmania" that Article 106 unleashed in all economic sectors and activities. But these well-known examples hide its destructive influence on small property owners and entrepreneurs. Because jointly with article 17, 106 became the instrument for thousands of small property expropriations by public expropriating agencies which did not even have the necessary expropriating funds. The untold story of these citizens, who have had the misfortune to lose sovereignty over their properties for decades, has to come to light in order to comprehend how poorly property rights are protected in Greece.

Frequently, we read in the Greek press various all weather analysts who say that they do not understand why Greek and foreign investors shun Greece as an investment destination. They sound pretentious. For, besides that they themselves would not invest their own savings, they are afraid for their careers to say that the culprit is the soviet style property regime that has been erected on the foundations of Greece's mired democracy.

3.3 Slow and haphazard application of the rule of law

Pretty soon we will be writing about the story of a small property owner who in 1992 had the misfortune to buy a piece of land to build a high class restaurant in Tripoli. The local authorities expropriated his land for the "public interest" reasons they submitted at the time to justify their decision. The owner of the land contested their claims in the courts and after several years and a lot of expenses he was exonerated. Even though the courts did not condemn the township of Tripoli to indemnify him for his legal expenses, at least he could go ahead with his plan to open a restaurant business. But alas, the then Mayor of Tripoli and the Municipal Council had other ideas. They declared his property once again under expropriation on the grounds of another set of reasons, and thus a new court case started for the owner.

It is now 25 years since the above conflict begun and this small property owner has lost his property and all his court expenses. The same could happen to any property owner and for an extensive list of reasons, including objections from the archeological service. Credible sources from the township of Athens tell me those similar cases of small property owners who lost their properties in the chaos of the judicial procedures number in the thousands. And only god knows how many are in the same situation all over Greece.

From the above it follows that, aside from the poor protection of property rights, the courts are terribly slow in resolving civil conflicts in a timely and effective manner. The third column in Table 1 above reports the index for the Rule of Law in 2015. In addition to the protection of property rights and the courts, this index reflects the perceptions to which citizens have confidence in and abide by the rules of society, in particular the quality of contract enforcement, the police, and the likelihood of crime and violence. We observe that Greeks do not have much confidence in these very crucial institutions.

3.4 Regulatory Environment

Through various administrative arrangements, the governments in Greece intervene systematically in the free competition among citizens, so that markets determine prices and remunerations that are above the prices of competitive equilibrium, thus resulting in the arbitrary and unfair transfer of income and material welfare from citizens who are entitled to them, to others. For an example, consider the concessions Greek governments have granted to labor unions and closed professions through the 1975 Constitution. They even legislated that in order to exercise their professions, doctors, architects, economists and what else you have must register with their corresponding professional societies. The unfair transfer of rents to these professionals springs from the usual practice that they collude and force the governments to introduce and implement regulations that favor them at the expense of consumers.

State subsidies and ostensibly job saving forays of the state into the economy, rarely yield the results for which they are intended. All they accomplish is to transfer income from the tax paying citizens and consumers to the owners of the supported activities. In Greece we have numerous examples of ill-conceived government interventions on behalf of organized minorities and rent seeking clients of the political parties. But none has been more disastrous for what it cost to citizens than the establishment early in the 1980s by Papandreou's first government of the Organization for the Restructuring of Businesses Enterprises. From the 67 large but failed concerns that registered with the organization, after billions of wasted taxes and additions to the national debt, only two enterprises survive to-day and these are terribly loss making and heavily indebted. I mention this case in the hope of alerting the experts of creditors to currently circulating ideas about repeating the same errors by the present leftish government. As Smith (**1776**, 468) stressed long time ago, many state regulations in the domain of the economy are not based on rational choice but depend on the "skills of this treacherous and cunning animal, commonly named ruler or politician."

In short, acting in the direction that the 1975 Constitution foreshadowed, Greek governments destroyed deliberately through systematic interventions in the market of products and services all incentives for the development of independent and outward looking entrepreneurship. Simply they were bent on establishing a model of state socialism, in which private agents would be subservient to their plans and investment choices. Therefore, it should come as no surprise that the index of regulatory quality for Greece in Table 1 lags so far behind that of Germany. On account of the evidence presented in Bitros (2017), Germany has and Greece has not a free market based democracy and it will take long and persistent efforts to turn the situation around.

3.5 Excessive rigidities in product and labor markets

One of the great advantages of the free market economy is that it adjusts quickly and with the greatest possible efficiency to endogenous and exogenous shocks that happen or are expected to happen. By contrast, the public sector, due to its structure, responds with long lags and typically in asymmetric ways because, when the government decides to intervene to correct a problem, it takes long to act and in the meantime the markets in question have changed since the problem was first noticed. So the remedy may worsen than improve the situation. By implication, as the state sector in Greece expanded, the rigidities in its operation spread throughout the economy, with the consequence that the latter lost its flexibility to return to equilibrium after some shocks.

The expansion of the state spread rigidities to the economy through still another channel. This is the activities of the powerful labor unions, which managed to extract from governments job security and horizontal pay scales and privileges. These, on the one hand, provided little or no incentives to increase productivity through greater work effort in the state sector, and on the other, they set the standards for the demands of the labor unions in the private sector, thus reducing its competitiveness and growth potential. In particular, as the state sector grew and turned into one of the main employers in the economy, it was to be expected that it would stir up incentives for civil servants and other government employees to form labor unions and to raise their bargaining power.[15] This development, in conjunction with the realization that governments in

[15] From the provisions about the labor unions in the 1975 Constitution the intention of the constitutional legislators is patently clear. They decided to encourage the setting up of labor and trade associations so that the state could control them. Thus, governments, labor unions and trade associations became intimately involved in a game

representative democracies are generally weak and the managements in state-owned enterprises and organizations are usually appointed by governments, converted labor unions in the narrow and the wider state sector into mechanisms of stirring turbulence in the economy and unfortunately always in one direction. That is, in the direction of constantly increasing the unit labor cost and disassociating it from the productivity of workers in the state sector. Moreover, if this hardening of labor markets were not enough, it spread to the private sector via a deliberate policy of replacing individual contracts by collective ones, not at least at the level of the enterprise, but at the level of the particular industry or sector. Thus, after many decades during which governments introduced or sanctioned the introduction of rigidities in the labor markets, it is no surprise that the experts of creditors have concluded that wages are no longer formed competitively and that the governments need to introduce measures to increase the flexibility in the labor markets.

Finally rigidities were introduced through various highly invasive industrial policies. For example, in peacetime and while the country served as full member in the EEC, many goods and services were classified as "necessities in scarcity" and their prices were set administratively. Rent control in the housing market, pharmaceuticals, the fees of doctors, lawyers, notary publics and hundreds of other professions were set in this manner. As a result, in all such cases the affected markets were dichotomized into "official" and "parallel or underground" and lost their ability to yield their first best results for the economy.

In the last 8 years, under pressure from the creditors and EU, Greek governments have started somewhat to relent and open up selected markets to competition. Particularly labor markets have acquired considerable flexibility and product markets are slated for heavy reforms in the directions suggested by the experts of the Organization for Economic Cooperation and Development (OECD). However, as the love affair of citizens and politicians with the prevailing model of state socialism does not appear to lose traction, at least for now progress is slow.

3.6 The demographic problem

The rate of growth of an economy is the rate of change in the Total Factor Productivity (TFP) of its productive factors. In turn, TFP is defined as a weighted average of the ratio of output to labour input and the ratio of output to capital input. This explains why the rate of growth of the labor force, its composition in terms of younger and older workers, the level of their education

among the so-called "social partners" and responsibility for the fate of democracy and the country was diffused to oblivion.

etc., are all very significant determinants of labor productivity. By implication, the return to robust economic growth, whenever the business climate improves, will depend also on the structural transformations of Greece's labor force. And unfortunately the prospects are not bright.

One reason is that the population of Greece is on a downward trend, implying that as it declines, the average age of the work force increases, and the ranks of retired persons are swelling. The consequences are cause for serious concerns because, given that new knowledge and skills enter into the economy through the incorporation in the labor force of younger generations of workers, as their numbers shrink, so do the prospects for strong labor productivity gains in the future. But if labor productivity is held back, the contributions of the working population to the retirement funds decline and the latter cannot cover the expenditures for the pensions of the retired people, whose life expectancy continues to increase. This sequence of onerous trends renders the demographic problem in Greece a time bomb with a not very long burning fuse. Something has to give and do so quickly to reverse the decline in the population.

Moreover, the problem worsens because of two other developments associated with the country's bankruptcy. The first of them has to do with the robust brain drain that has been observed in recent years. Due to the decision by Greek governments to safeguard the employment in the public sector, most of the fiscal adjustment fell on the private sector with the average unemployment rate shooting close to 30% and among the young nearly to 60%. As a result the joblessness forced many primarily younger people and particularly educated and experienced professionals to leave the country. The second problem is that a large percentage of older workers who lost their jobs have entered into the ranks of permanently unemployed, whereas many others retired, thus adding to the problems of the retirement funds.[16]

From all the above it follows that Greece is in deep trouble and that what is needed is a complete overhaul of its statist productive model. A hard but speedy approach to this effect would be to embrace the reforms described briefly in the last section.

3.7 Populism and the threat of authoritarianism

Since 1974, when the so called "Colonels' Junta" authoritarian dictatorship collapsed, Greece has been enjoying an unprecedented long period of democracy, to which the pressure of the EEC/EU

[16] Even though it is not of the present to analyze in detail, it should be noted that the demographic problem in conjunction with the adverse effects of the economic crisis on the structure of employment and the finances of the retirement funds have raised serious questions about the sustainability of the pension system.

institutional acquis has contributed decisively. Yet the shallowness and the ineffectiveness of institutions in charge of the rule of law still present serious challenges.

As Pappas (2014) notes, Greece's democratic practice in the post 1974 period has been characterized by

> *"… both the political class and the voting public indulging in the particularistic interests of externalizing the costs at the expense of institutions."*

The deep-rooted and extensive rent-seeking has eroded impersonal trust in the institutions, thus creating in effect various zero-sum games and social cascades that: (a) facilitated in the initial period political bargains with pressure groups especially through easy borrowing and depreciating of the drachma, and (b) later on rendered close to impossible the implementation of necessary reforms in the fiscal, industrial and purely institutional fronts.

The "tragedy of the commons" that resulted led to an acute crisis of legitimation when the financial crisis hit. This was felt most pointedly in the general election results, where the "anti-systemic" parties both on the right and the left of the political spectrum made unprecedented gains, while even the mainstream, moderate parties often tried to one-up on unfeasible promises about "ending austerity", "tearing up the memoranda" etc. In turn, these results reflected a widespread radicalization as seen in massive anti-austerity protests and the emergence of the so-called movement of "Aganaktismenoi" (Indignant citizens), which peaked between 2010 and 2012.

It is notable that in the 2016 Timbro Authoritarian Populism Index, Greece ranked 2nd among European nations, just below Hungary, in electoral support for authoritarian and totalitarian parties, with more than 55% of the votes going for those parties.[17] Furthermore, remarkable has been the emergence of the extreme right Golden Dawn Party, which won 6.99% of the votes in the latest September 2015 general election and 18 out of a total of 300 parliamentary seats.[18]

While it is true that mass protests have greatly declined especially since the September 2015 elections, the risk of a new emergence of populism and authoritarianism that could mitigate Greece's recovery efforts should not be underestimated.

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[17] 2015 Timbro Authoritarian Populism Index, p. 22.
[18] http://ekloges.ypes.gr/current/v/public/index.html, Last accessed, September 3, 2017.

4. What to do

The path to the current crisis began in the 1950s, when Greek leaders decided to establish a state-driven economic development model with emphasis on import substitution. As a result, unlike so different countries like e.g. Germany, Taiwan, Singapore and South Korea, which found their way to high and sustainable economic growth by adopting free market models based on exports, the ambitions, the plans and the prospects of Greek entrepreneurs were nurtured in the country's narrow and state-controlled markets.

Two opportunities to change course presented in the 1970s. The first was the return to democracy in 1974, after 7 years of military rule, and the second coincided with the accession of Greece to full EEC membership in 1979. Both were missed because: (a) public choices continued to be dominated by the ideas and policy recommendations of politicians and economists who favored the model of centrally administered society and economy, and (b) the Greek entrepreneurs, who could have made the difference in the exemplary way they have dome in tourism and particularly in ocean shipping, remained bootstrapped to ill-conceived government initiatives. That is why now, in the aftermath of the 2009 bankruptcy and its onerous social and economic consequences, I do not see any other way out from an all but certain low growth equilibrium trap than taking ownership of a package of "structural transformations" that will liberate and mobilize the Greek entrepreneurial dynamism. The objective in this section is to lay out some general guidelines for a corpus of such reforms.

4.1 Reforms in the public sector

In Greece governments have used the public sector to advance their chances for re-election. They have done so by dispensing all sorts of favors to party supporters and organized minorities. As a result, throughout the post war period this sector has employed a disproportionate share of the labor force, civil servants have low human capital and are selected and promoted to a large extent by non-meritorious criteria, the services offered are low quality, costly and opaque, etc.

Prior to 1974 there was not much antagonism among political parties and politicians were not particularly pressed to outbid each other in providing public jobs and contracts for votes. Also, labor unions were non-existent and strikes were forbidden and, while the sector operated inefficiently, at least it got the job done.[19] But after 1974 it became the battle ground of fierce party antagonisms and over time it grew excessively large and grossly inefficient. Moreover, the governments, as well as the public administration and the state-owned enterprises and organizations in their own ways, became unfriendly, if not outright hostile, towards entrepreneurship.

This trend begun in 1975 with the introduction of a new constitution, which among other provisions and authorizations: blurred further the separation of state powers; extended the hold of political parties over the public administration; eroded critically property rights; replaced individual by collective wage agreements; expanded the power and privileges of labor unions and provided for the funding of their activities from general taxation; created a host of artificial social rights through which citizens lost their sovereignty and mutated to party clients, etc. In other words, the 1975 constitution offered the required institutional pretext to introduce into the presumed regime of a market based democracy the policies of a largely confused state socialism.

By implication, confronting the discouragement that the above arrangements exert on entrepreneurship, small scale reforms like the ones imposed by the so-called "memoranda" will not do. Rather what is required are "structural transformations" like the following:

Reforms of most urgent priority

- Article 106 of the 1975 Constitution, which almost negates property rights to citizens, creates insurmountable uncertainty to both local and foreign investors. Hence, at the earliest possible, it should be abolished.
- Terminate all outstanding cases of private property expropriation for "public interest", if the indemnification funds are not securely available by the expropriating public authorities, and forbid repetition of expropriating procedures for any reason, for the same property, and for a period of five years, within which the owner maintains full rights.
- Eliminate the uncertainty posed by the archeological service to investors, by delimiting its domain to particular land sites and zones.

[19] According to Article 11, paragraph 4, of the 1952 Constitution, the strikes by civil servants and employees in the service of organizations operated by the state for the public interest were forbidden. On this, see Svolos (1972, p. 253). In the 1975 Constitution, Article 22 allowed strikes on the part of civil servants under the restrains that would be set by a law that would be enacted by the parliament. Yet, as stressed by the daily *Estia* (2013), such a law has never been enacted.

Reforms in the medium run (next 3-5 years)

- Decentralize decision-making by introducing substantive elements of subsidiarity across local, regional and national levels.
- Abolish employment tenure across the board as well as legal impediments to the assignment and mobility of civil servants.
- Establish transparent and uncompromising systems for the selection, promotion, and dismissal of civil servants.
- Reduce public sector employment, for example, to 11% of the labor force as in Germany.
- Privatize all public services that we know they can be performed better and at much lower cost through competitive market processes (e.g. garbage collection and management).
- Setup an independent public authority for the identification and registration of all citizens who are in true need of some state support and establish systems for catering to their needs under full transparency, accountability and fraud control.
- Reduce government expenditures, for example, to the average percentage in GDP reported in the last five years by that member-state in the Eurozone that stands last on the basis of this criterion.

Reforms in the longer run (next 5-10 years)

The 1975 constitution, as revised and amended, should be replaced by a simpler and less loquacious one centered squarely on three principles, Namely, limit the power of the state so as to protect civil liberties, embrace the four European freedoms, and encourage individual responsibility. A representative sample of reforms which would be consistent with these principles would include:

- Strict separation of state powers as well as the reinforcement of checks and balances to safeguard their independence;
- Term limits in all cases of elected officials, loosening up of conditions for recalling them on account of due process, and insulation of public administration from falling prey to politicians and organized minority interests;
- Abolishment of state monopoly across all economic activities that demonstrably can be performed more efficiently by the private sector.
- With the exception of subsidy schemes to general education and basic research, withdrawal of the state from all levels of education, as well as various channels of mass com-

munication like television, radio station, and other social media.

- Neutrality of the state vis-a-vis labor and trade organizations by transferring all regulatory functions to independent competition authorities.
- Constitutional safeguards regarding the stability and predictability of public policies.
- Public debt limits that can be lifted only after a decision by a high majority in the parliament.

To be sure, under the present circumstances, initiatives in the above fronts would be considered socially and politically untenable. However, as various tough constraints in the living standards and the life styles become binding, even hard reforms as the suggested ones will become feasible.

4.2 Reforms in the product and labor markets

As things stand at present the private sector cannot be expected to provide the required spark to place the economy on a high growth path. Under the continuing illiberal regime of capital controls, the overhang of the huge private debt and the uncertainty that looms from the lack of social consensus on the way forward, individuals and enterprises would be quite irrational to undertake the volumes of investments necessary to ascertain the return to a healthy business climate. Rather to the contrary, the constant flow of bad news in the local and in the international press about the gimmicks the current leftish government employs to signal its distrust to big time investments discourages even the most daring investors. Consequently, it will take considerable time before the business climate becomes hospitable and inviting. But when it does the conditions for doing business in Greece should be simple, transparent and stable. A business regime with these properties may be established by means of the following indicative reforms:

Reforms in the short run (next 3-5 years)

- Revoke all remaining direct price controls on products and services.
- Open up all remaining state monopolies to actual and potential competition.
- Open up all remaining closed professions and abolish the obligation to register in trade organizations and professional societies in order to acquire the right to provide a service or exercise some profession.
- Render permanent the current temporary respite of collective agreements at all but the enterprise level of economic activity.
- Let the following issues be resolved through negotiations at the enterprise level with-

out interference from the state: (a) minimum wage; (b) conditions for recruiting employees (probationary period of employment, individual or collective contract, fixed or indefinite term of work assignment); (c) firing of employees (massive layoffs, timing of warning, severance pay, consultation procedures prior to notification of redundancies); and (d) determination of working time (overtime, part-time, shift work, work on public holidays).

- Abolish all barriers to entry into and exit from all economic activities and lower drastically the number and the cost of required state permits.

Reforms in the longer run (next 5-10 years)

- Complete the soonest possible the plan for land uses, including the demarcation of sites and zones of archeological interest.
- Establish codes specifying in advance all conditions for the protection of the environment, particularly with regard to fishing, quarrying and in general the natural resource extracting industries.
- Organize one stop services for coordinating and monitoring prospective investment projects.

As part of the "memoranda" Greek governments have agreed to a very long list of structural reforms known as the "OECD tool kit." A few of them have been implemented, whereas most have been relegated to the future. But the future is now and the soonest the Greek people take ownership of these reforms, the soonest the economic growth prospects of the country will brighten.

4.3 Sum-up

The tragedy Greece is going through did not happen fatefully. It was made fateful by politicians and intellectuals who did not believe in the social merits of a free market economy. Even now that the country is under the supervision and guardianship of its creditors, successive governments procrastinate and refuse to take ownership of the free market reforms to which they are forced to agree. However, they have no choice but to repent because no Greek leader would dare risk an open bankruptcy and lead Greece to exit from the Eurozone. Sooner than later they will discover that their self-interest coincides with that of the country and they will take the lead in the replacement of the present hard core statist model with one based on open markets and outward looking dynamic Greek entrepreneurship.

On their part, EU authorities are understandably eager for a quick turnaround in the economic indices in Greece to justify to the citizens of the other member-states that the loans they have advanced to Greece are well spent. I advise that they show patience and persistence in staying the course of pressing for deep "structural transformations" because the changes taking place in Greece constitute in essence a behavioral regime change.[20] The statist state of mind and life styles that have taken hold over the span of several decades are not easy to change in a few years. That is why a better measure of progress in Greece would be a composite index of freedom like the one published by Heritage Foundation. Once this index and its sub-indices start improving the case of making Greece a freer country will have been won.

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[20] According to the public opinion survey published by the new Greek think tank Dianeosis (see Georgakopoulos (2017)), Greeks are turning away from big government and embracing market-friendly policies as they seek jobs and growth. These are certainly promising signs of change.

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