The Immediate Effects of the Austerity Program in Greece

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Adjustments in the Public Sector in Europe:
Scope, Effects and Policy Issues
International Labour Office and the European Commission
Crowne Plaza Hotel, Brussels,
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OUTLINE

- Effects
- Context of the Adjustment Program
  - Insolvency (still being) treated as illiquidity
  - Front loaded austerity, no drivers for growth
  - No consideration to social impact
  - No social dialogue
- Prospects

EFFECTS

Industrial Relations

Health

Unemployment

Pensions

Taxation

Growth

Poverty

A word search in the IMF/EC initial documents revealed:

- Equality: not found
- Equity: found (as in banks)
- Social protection: not found
- Protection: found in depositors' protection
  legal protection against privatization
  reducing employment protection
- Vulnerable: (found in an EC document):
  "all will be done while protecting the vulnerable"

INTERNATIONAL MONETARY FUND

Cross-Cutting Themes in Employment Experiences during the Crisis

Prepared by the Strategy, Policy, and Review Department

Approved by Reza Moghadam

October 8, 2010

The analysis suggests a number of policy implications:

- *Policies to support employment are justified during severe downturns but have to be tailored* to the expected duration of the shock and the institutions in place.
- *Policies are also justified to avoid an increase in long-term unemployment* and a drop in labor force participation during severe downturns.
- *Reforms to reduce employment protection gaps in dual labor markets could lead to smoother labor market adjustments*, both by avoiding strict protection for regular contracts and abuse of temporary employees.
- *Wage setting mechanisms work best when allowing adjustment via centralized coordination for economy-wide shocks and firm-level bargains for specific ones*.
- *Crisis-driven labor market policies should give their place to broader structural reforms* in the medium term.

International Monetary Fund (2012), Greece: Request for Extended Arrangement Under the Extended Fund Facility - Staff Report; Staff Supplement.

(Country Report No. 12/57, March 9, 2012)

- *(p. 122) "If the ongoing social dialogue is unsuccessful in identifying concrete solutions, then to achieve this goal the government will take legislative measures in the urgent public interest to allow wage and non-wage costs to adjust as needed ….*

- *(p. 176) Given that the outcome of the social dialogue to promote employment and competitiveness fell short of expectations, the Government will take measures to foster a rapid adjustment of labor costs … At the same time, the Government will promote smooth wage bargaining at the various levels.*

Press conference by Dimitris Daskalopoulos, Chairman of the Board of Directors, Hellenic Federation of Enterprises, 16 November 2010

"The achievement of the fiscal targets in 2010 and 2011 appears to range from doubtful to impossible … If the Mnemonio leads to national divisions, change will become impossible and bankruptcy unavoidable … Collective agreements … are useful, are a way to avoid conflict … Let's leave companies and workers to communicate between themselves and find their own solutions … What we support is derived from Europe, not from African countries where workers are whipped. Europe is envied globally for its system of social protection".

Tongue in cheek?

Strikes Jan. 2011 - April 2012 (incomplete)

Sector	No. Of Strikes	Sector	No. Of Strikes
PUBLIC TRANSPORTATION	102	GENERAL STRIKES - PUBLIC SECTOR	30
PUBLIC HOSPITALS	68	GENERAL STRIKES - PRIVATE SECTOR	16
PHARMACIES	27	PRIVATE SECTOR (OTHERS)	84
EDUCATION	38	ALL WORKERS MILITANT FRONT	12
LOCAL/REGIONAL GOVERNMENTS	31	MEN IN UNIFORM (POLICEMEN, etc.)	22
LAWYERS	95	MINISTRY OF FINANCE	11
SOCIAL SECURITY FUNDS	3	MINISTRY OF INFRASTRUCTURE	8
SOEs	27	MINISTRY OF CULTURE (MUSEUMS)	20
MASS MEDIA	208	MINISTRY OF INTERIOR	1
AGRICULTURAL SECTOR	7	OTHERS (Sectoral Unions)	28
Total number of strikes: 838			
Average number of strikes per month: 52.4			

Health effects (1)

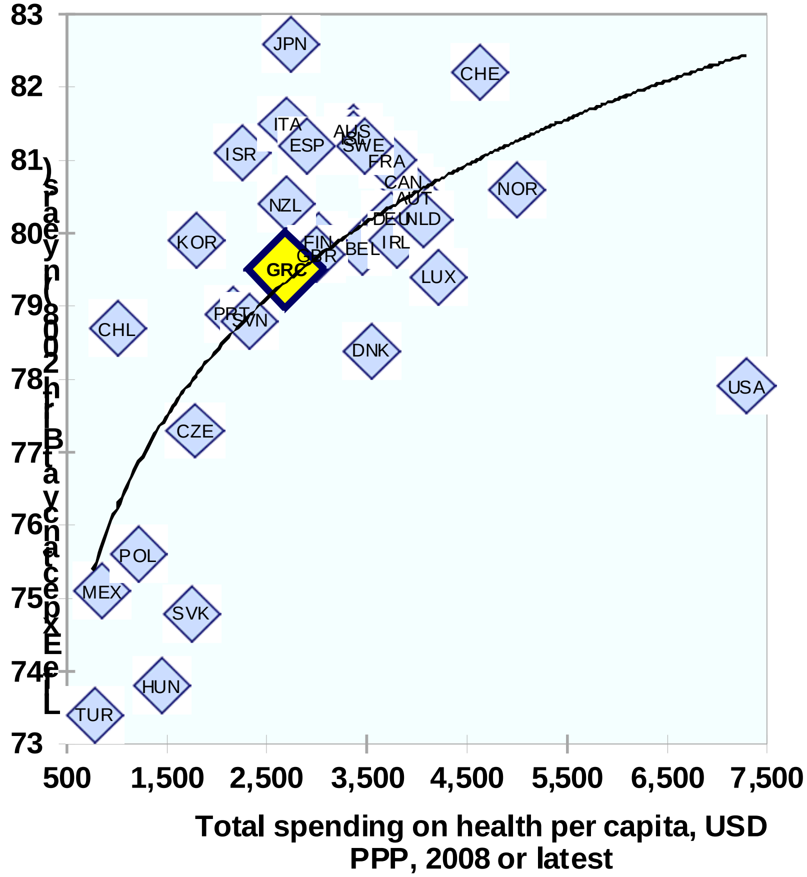
Effects

- Cancer drugs stopped being procured
- 30 per cent reduction in admissions to private hospitals
- 40 per cent cuts in public hospital budgets – 48 percent increase of admissions
- Neighborhood clinics are closing down or reduced opening hours - proportion seeking medical attention from clinics increased from below 5% to 30%
- 40 per cent increase in suicides
- Homicide and theft rates have at least doubled since the crisis
- Heroin use rose by 20% against loss of one-third of street-work programs
- HIV infections increased by 52 per cent
- Greek non-governmental organizations able to meet less than one fiftieth of the demand for needle exchange
- The number of beneficiaries of sickness benefits reduced

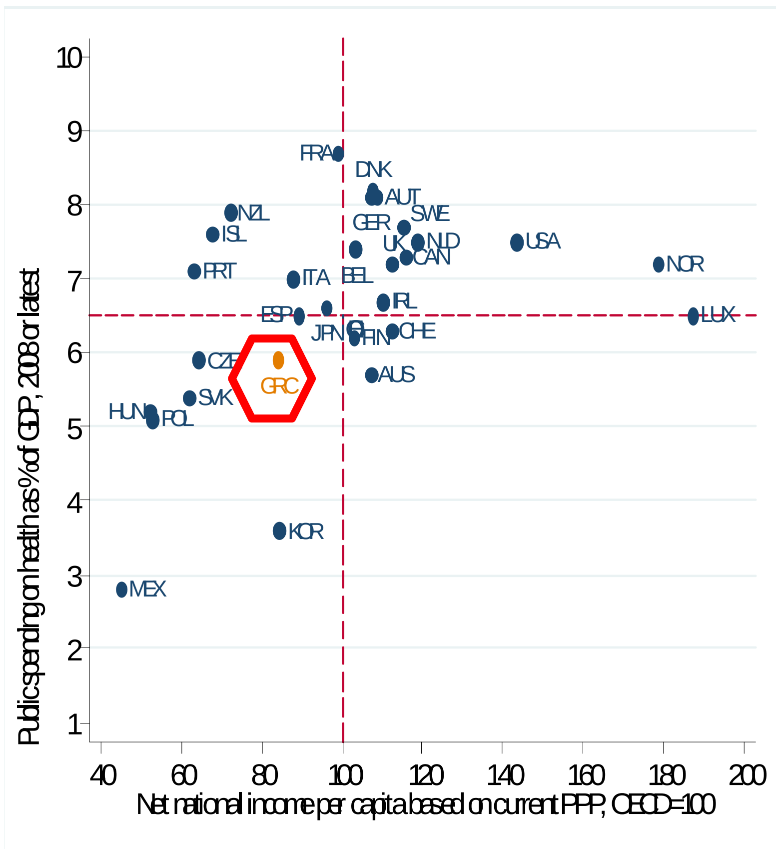
Health effects (2)

Despite the fast increase and corruption in pharmaceutical expenditures, Greece was still an average spender on health

Countries with higher life expectancy spend more on per capita health care

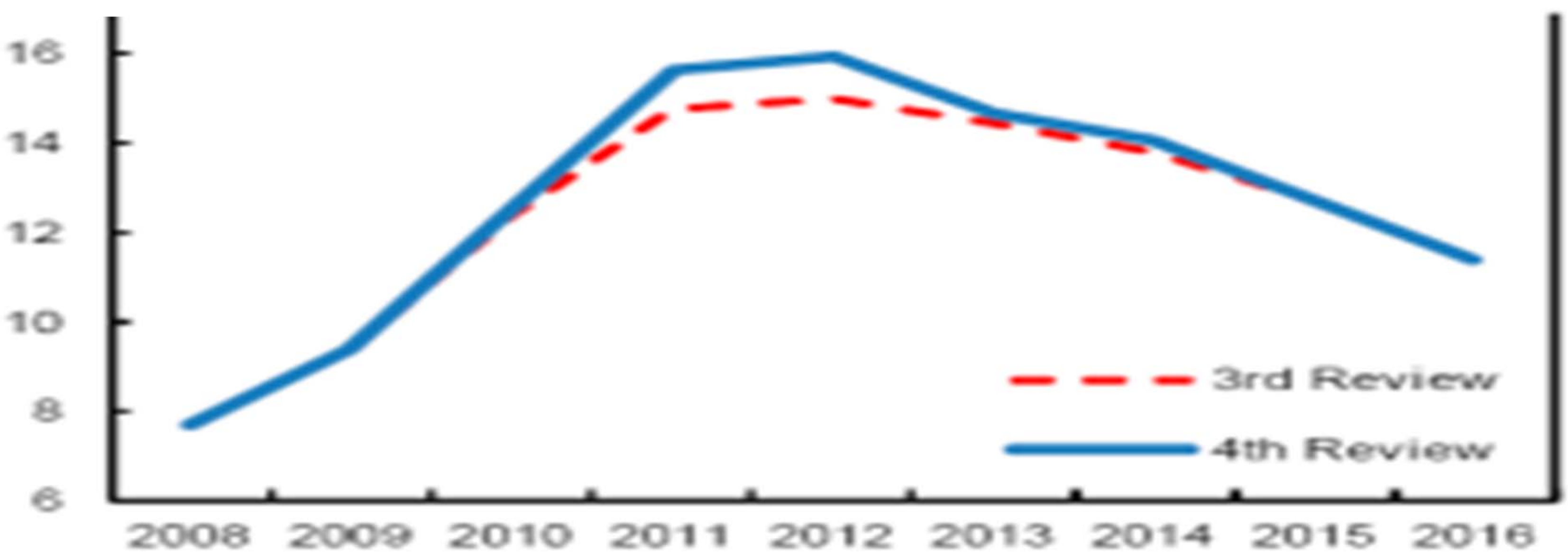


Public Spending on Health vs Per Capita Income (intersention of the 2 lines: OECD avg)

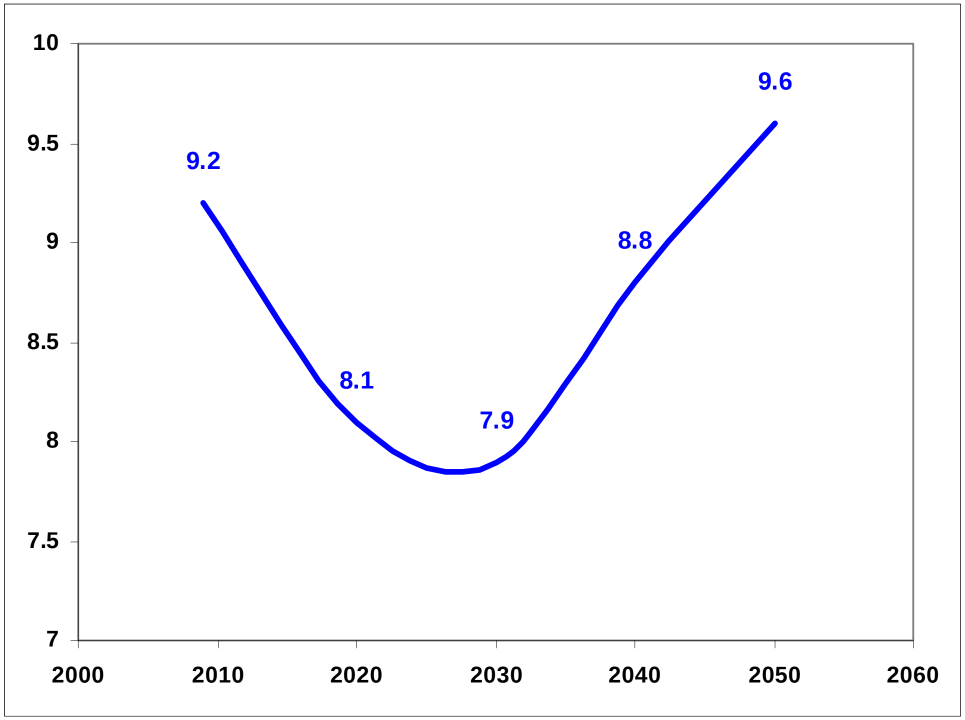


Unemployment: Troika Projections and Actual

Actual latest: 23%
(for youth: 51%)



Front-loaded reduction in pension expenditure (% of GDP) (despite increase in the number of pensioners)



But social protection in Greece is mainly through pensions

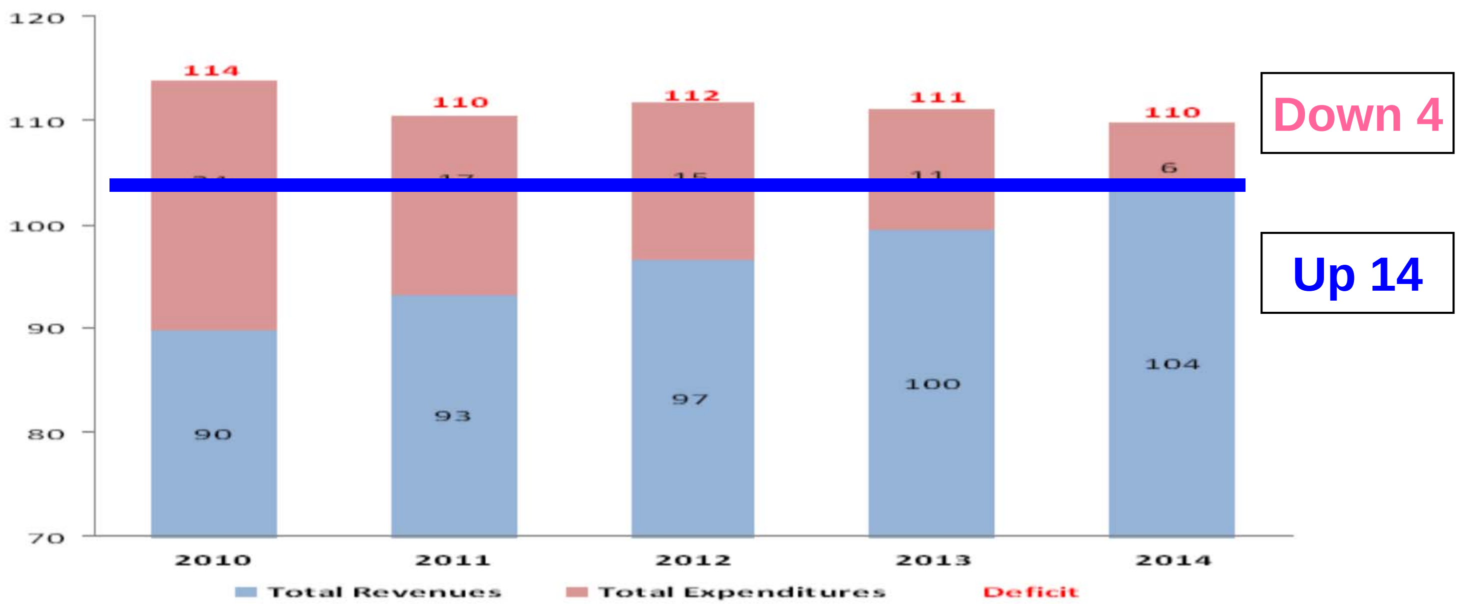
Table 14: Poverty Reduction Impact by Benefits Categories in 2000						
	Pensions	Family Benefits	Sickness/ Disability/ Unemployment	Social Assistance	Other	
Belgium	-15.6	-4.7	-4.9	-0.1	-0.5	-88%
Denmark	-11.5	-2.2	-5.1	-0.3	-2.9	
Germany	-18.2	-4.9	-4.1	-0.5	-0.5	
Greece	-16.7	-0.8	-1.4	0	-0.1	-2.3%
Spain	-12.7	-0.4	-4.0	0	-0.2	
France	-16.9	-3.6	-3.8	-0.2	-2.4	
Ireland	-6.1	-2.8	-5.4	-0.2	-0.8	
Italy	-19.4	-0.5	-2.0	0	-0.1	
Luxembourg	-16.6	-6.0	-4.1	-0.3	0	
Netherlands	-14.7	-3.4	-4.3	-1.4	-0.7	
Austria	-15.6	-6.7	-2.9	0	-0.5	
Portugal	-11.1	-0.9	-2.5	-0.3	-0.2	
Finland	-12.4	-5.6	-11.3	-0.5	-2.8	-62%
UK	-14.0	-4.3	-3.9		-3.8	
Average	-14.4	-3.3	-4.3	-0.3	-1.1	-9%

Sources: World Bank: Social Safety Nets and Lessons from the European Experience

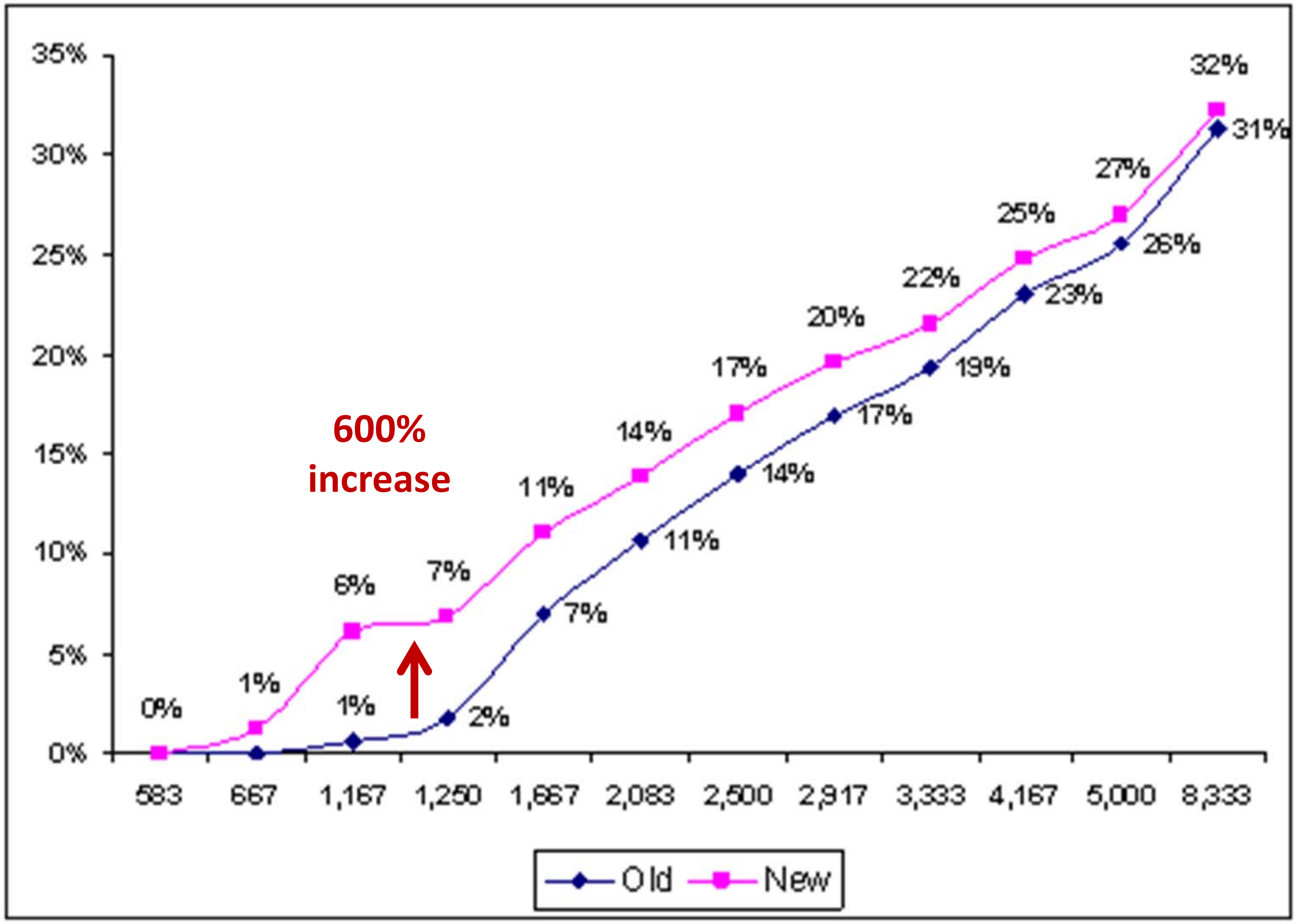
Taxation (1)
Deficit reduction: Taxes to Increase More than Expenditure Cuts

(Me Lagarde, 24 May 2012: “There is tax collection that has to happen … the fiscal consolidation that has taken place in Greece is very remarkable … Taxes have to be collected”.

http://www.imf.org/external/np/tr/2012/tr052212.htm



Taxation (2)
Changes in average tax rates for a family with one child



Tax whom?

One-in-three registered companies closed (?)

Tax receipts down 40 percent so far this year

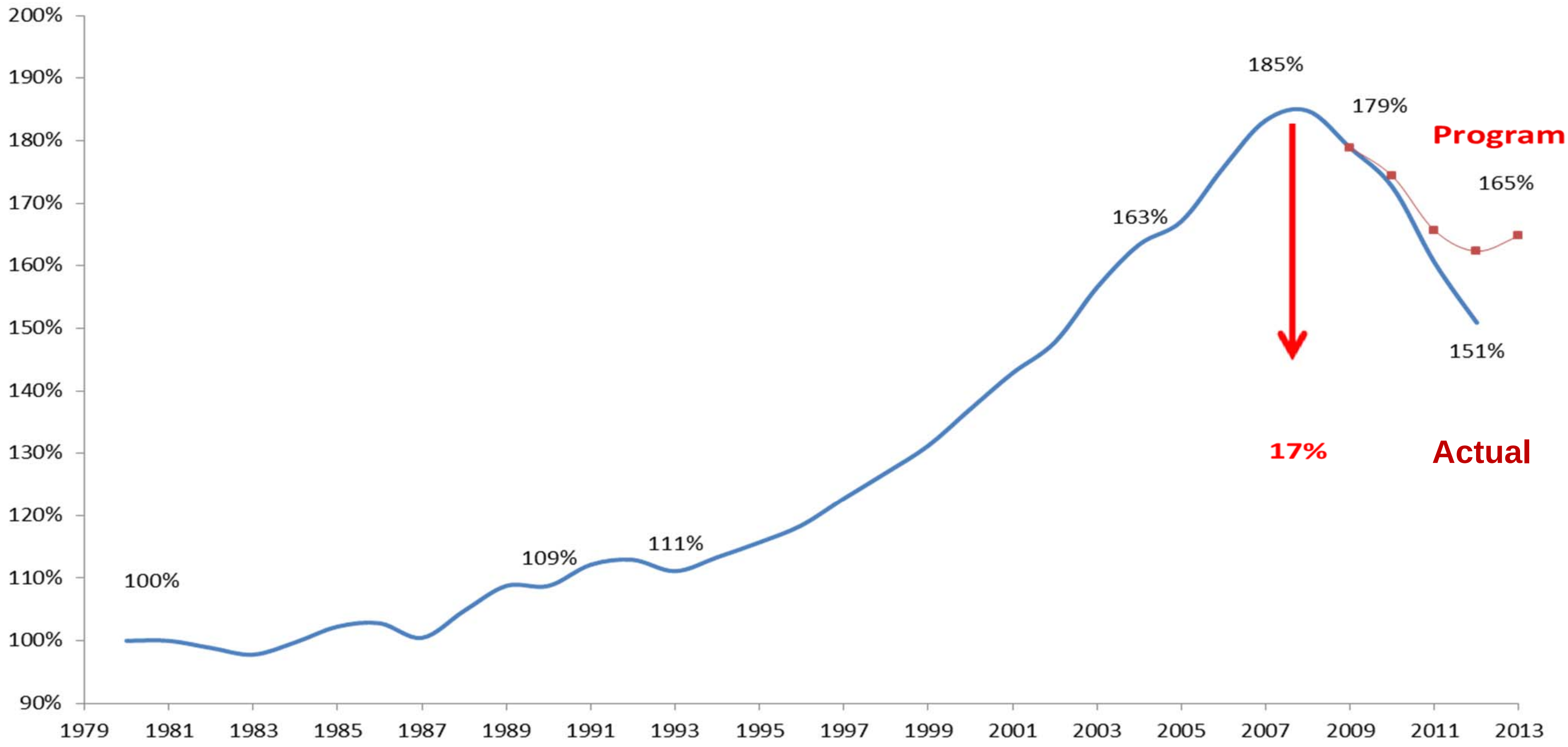
Table 6. Small & Medium Enterprises in Greece compared to the EU27			
	GREECE		EU27
Business Category	Number of business	% of TOTAL Business	% of TOTAL Business
Very Small	719,952	96.5	92.1
Small	22,832	3,1	6,6
Medium	2,893	0.4	1.1
Total SMEs	745,677	99.9	99.8
Large	563	0.1	0.2
TOTAL Business	746,240	100.0	100.0
EMPLOYMENT	Number of employees	% of Total Employees	% of Total Employees
Very Small	1,447,218	57.6	29.8
Small	438,792	[illegible]	[illegible]
Medium	264,427	10.5	16.8
Total SMEs	2,150,438	85.6	66.9
Large	362,055	14.4	33.1
TOTAL Employment	2,512,493	100.0	100.0
VALUE ADDED	In billion euros	% of Total Value Added	
Very Small	27	35.3	21.6
Small	16	[illegible]	[illegible]
Medium	12	15.8	17.9
Total SMEs	55	71.7	58.4
Large	22	28.3	41.6
TOTAL VALUE ADDED	77	100.0	100.0

Size of the Shadow Economy

Since we know successful debt reduction is mainly through growth *and* growth has stalled, is it the time to formalize the informal?

Table 16: Size of the Shadow Economy, 2011		
Country	% of GDP	€ in € billions
Bulgaria	32.3	12
Romania	29.6	38
Croatia	29.5	14
Lithuania	29.0	9
Estonia	28.6	4
Latvia	26.5	5
Cyprus	26.0	5
Malta	25.8	2
Poland	25.0	94
Greece	24.3	54
Hungary	22.8	24
Italy	21.2	337
Portugal	19.4	33
E.U.	19.2	1907
Spain	19.2	208
Belgium	17.1	63
Czech Rep.	16.4	25
Slovenia	16.0	9
Slovakia	16.0	11
Norway	14.8	50
Sweden	14.7	57
Denmark	13.8	33
Germany	13.7	352
Finland	13.7	26
Ireland	12.8	20
France	11.0	220
Britain	11.0	190
Netherlands	9.8	60
Austria	8.0	24
Luxembourg	8.2	4

Direct adjustment effects versus recession induced effects: Positive economic growth by 2012 ? (GDP index 1981=100)



First year changes in poverty rates by employment of head of household

Employment status	Poverty rate (%) in 2010	Change (in pp)
Unemployed	64	13
Pensioners	29	4
Private sector self-employed	21	5
Private sector employee	16	4
Private sector professional	4	0
Public sector/SOEs	1	1

PROSPECTS

For how long things will be going down?

Table 17: Peak to Trough Effects of Financial Crises:
Global Average Based on Major Episodes Since 1899

	EFFECT (percent)			DURATION (in years)		
	AVG	MAX	(County, Year)	AVG	MAX	(County, Year)
Unemployment increase*	7	23	(USA 1929)	4.8	11	(Japan 1992)
GDP	-9	-29	(USA 1929)	1.9	4	(Argentina 2001)
Public debt increase**	86	275	(Colombia 1998)	measured over 3 years		

* In percentage points

** The increase in public debt is measured over the 3 years following the crisis and is mainly due to the collapse of the tax base and ambitious countercyclical fiscal policies, not the costs of bail outs or recapitalization of the banking system

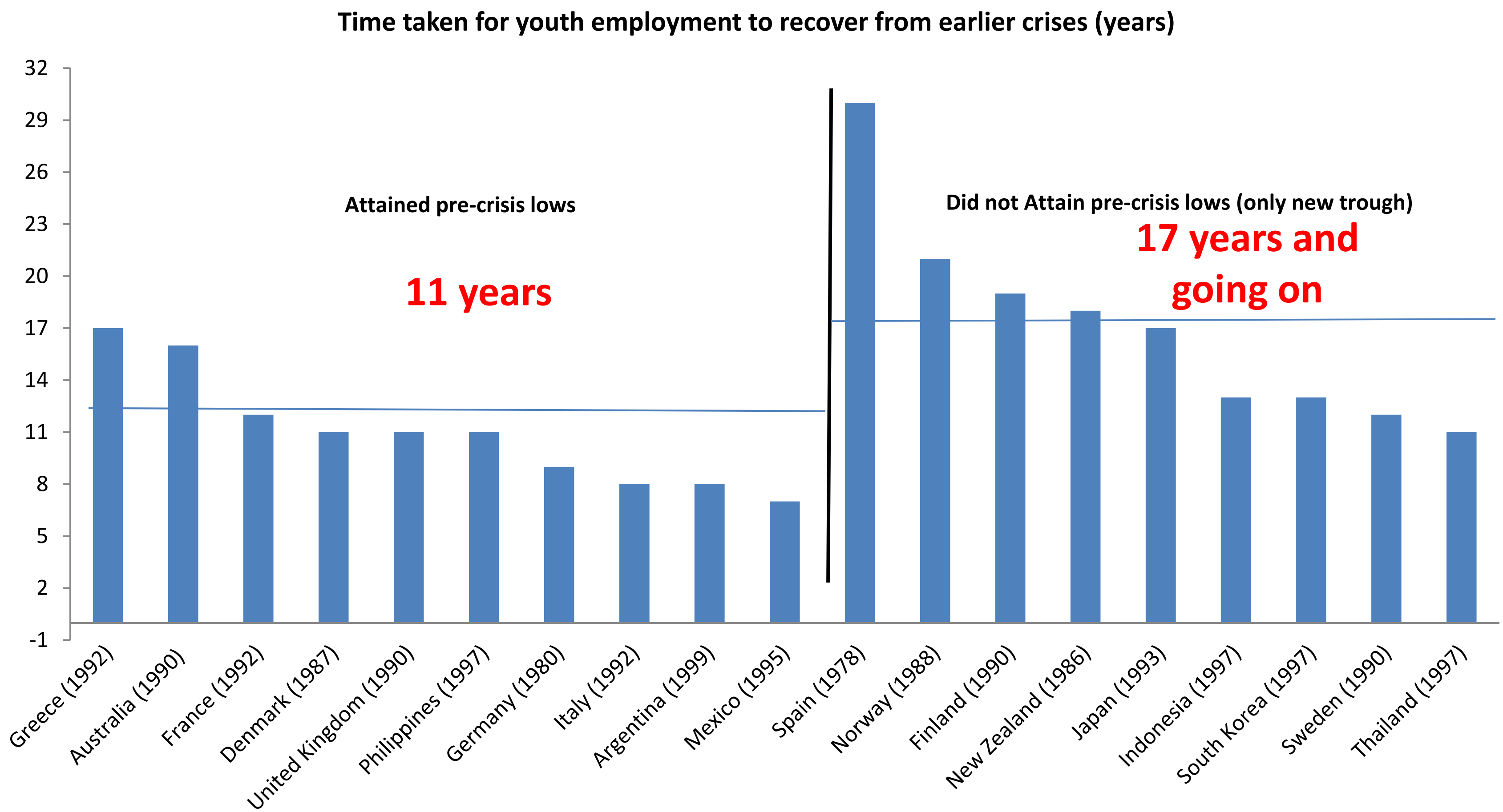
Source: Tzannatos (2009) adapted from Reinhart and Rogoff (2009)

Triple

Almost there

Double

And from the ILO (WoW, 2010)



After all the adjustment so far,
has the insolvency been addressed?

Debt Dynamics

Expected assistance and debt/deficit reduction from the various adjustment programs 2010 (Actual) – 2020 (Forecast)				
	2010	**Assistance 2010-2020**		**2020**
Debt	**€329 bl** 145% GDP	€110 bl	EC/ECB/IMF agreed in May 2010	**€300 bl** 120% GDP
		€109 bl	EC/ECB/IMF agreed in July 2011	
Deficit	11% GDP	€30 bl	EU direct contribution agreed in Oct 2011	**Less than** 3% GDP*
		€106 bl	PSI 53% haircut, agreed in Feb 2012	
		€355 bl	**TOTAL**	

June 2012

Economic data

% change on year ago

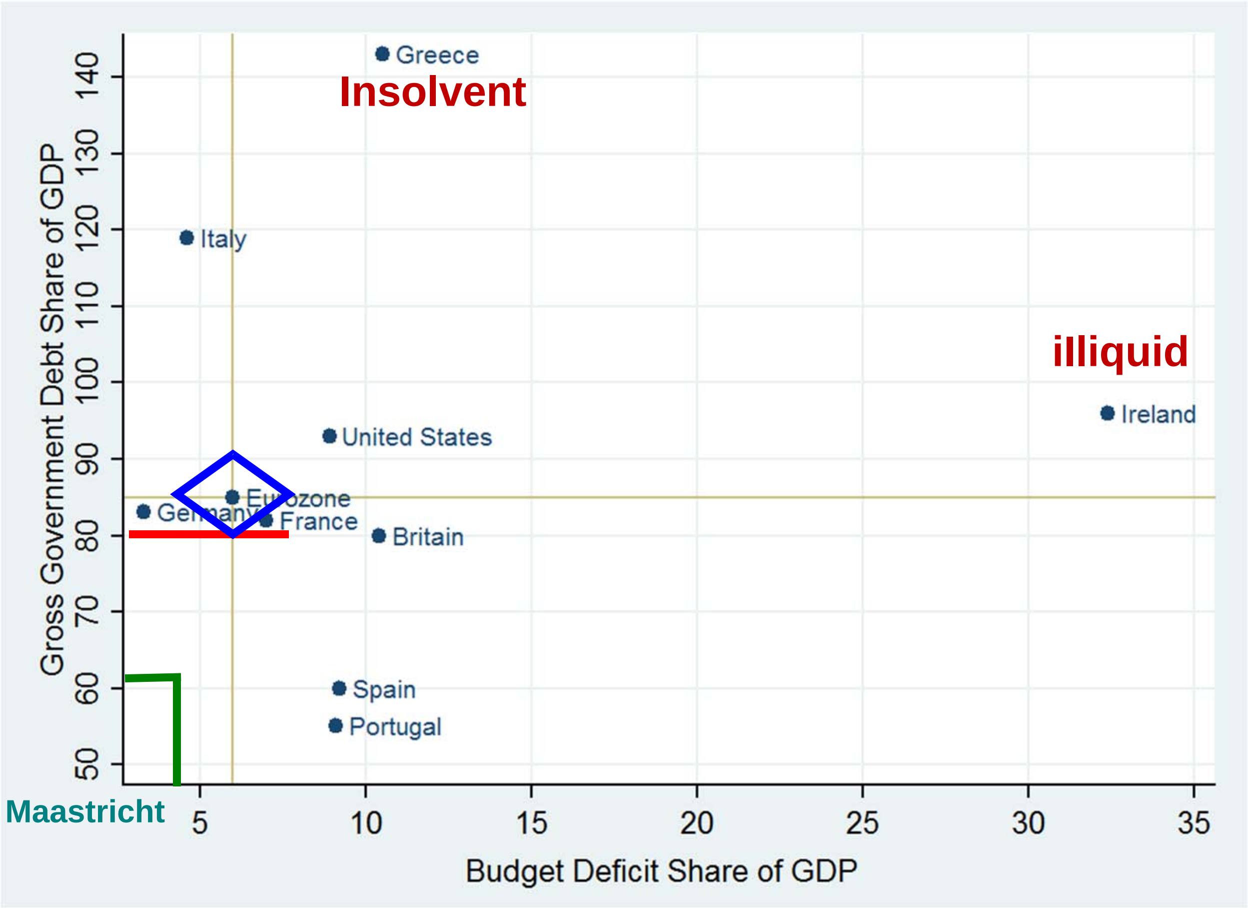
	Gross domestic product latest	qtr*	2012†	Industrial production latest	Consumer prices latest	2012†	Unemployment rate, %	Current-account balance latest 12 months, $bn	% of GDP 2012†	Budget balance % of GDP 2012†	Interest rates, % 10-year gov't bonds, latest	Currency units, per $ May 30th	year ago
United States	+2.1 Q1	+2.2	+2.2	+5.2 Apr	+2.3 Apr	+2.3	8.1 Apr	-473.4 Q4	-3.2	-7.6	1.63	-	-
China	+8.1 Q1	+7.4	+8.3	+9.3 Apr	+3.4 Apr	+3.7	4.1 Q1§	+197.6 Q1	+2.3	-2.1	2.85§§	6.36	6.48
Japan	+2.7 Q1	+4.1	+1.8	+13.4 Apr	+0.5 Apr	nil	4.6 Apr	+99.4 Mar	+1.6	-8.1	0.82	79.0	80.9
Britain	-0.1 Q1	-1.3	+0.4	-2.6 Mar	+3.0 Apr	+2.8	8.2 Feb††	-46.3 Q4	-1.6	-7.7	1.83	0.64	0.61
Canada	+2.2 Q4	+1.8	+2.1	+1.3 Feb	+2.0 Apr	+2.1	7.3 Apr	-49.0 Q4	-2.3	-3.5	1.79	1.03	0.98
Euro Area	nil Q1	+0.1	-0.5	-2.2 Mar	+2.6 Apr	+2.3	10.9 Mar	+11.8 Mar	-0.1	-3.5	1.26	0.81	0.70
Austria	+1.9 Q1	+7.9	+0.5	+0.8 Mar	+2.3 Apr	+2.3	4.0 Mar	+8.0 Q4	+2.9	-3.8	2.26	0.81	0.70
Belgium	+0.5 Q1	+1.2	-0.1	-4.0 Mar	+2.8 May	+2.6	7.3 Mar	-3.7 Dec	+0.5	-3.1	3.18	0.81	0.70
France	+0.3 Q1	+0.2	+0.3	-0.9 Mar	+2.1 Apr	+2.3	10.0 Mar	-61.6 Mar	-2.0	-4.4	2.48	0.81	0.70
Germany	+1.7 Q1	+2.1	+0.7	+1.5 Mar	+1.9 May	+2.1	6.8 Apr	+202.2 Mar	+4.8	-1.3	1.26	0.81	0.70
Greece	-6.2 Q1	na	-7.1	-8.6 Mar	+1.9 Apr	-0.1	21.7 Feb	-25.5 Mar	-6.9	-7.8	29.10	0.81	0.70
Italy	-1.3 Q1	-3.2	-1.7	-5.8 Mar	+3.3 Apr	+3.1	9.8 Mar	-59.4 Mar	-2.5	-2.2	6.06	0.81	0.70
Netherlands	-1.1 Q1	-0.6	-0.8	+0.7 Mar	+2.4 Apr	+2.2	6.2 Apr	+76.4 Q4	+7.6	-5.1	1.78	0.81	0.70
Spain	-0.4 Q1	-1.3	-1.7	-10.4 Mar	+2.1 Apr	+1.9	24.1 Mar	-51.8 Feb	-2.8	-5.9	6.43	0.81	0.70
Czech Republic	+0.3 Q4	-3.9	+0.3	-0.7 Mar	+3.5 Apr	+3.3	8.4 Apr§	-6.3 Q4	-2.1	-3.3	3.27	20.7	17.2
Denmark	+0.4 Q4	-0.4	+0.7	-2.3 Mar	+2.3 Apr	+2.2	6.2 Mar	+19.7 Mar	+5.4	-3.5	1.27	6.00	5.22
Hungary	-0.7 Q1	-5.1	-0.8	+0.6 Mar	+5.7 Apr	+5.7	11.5 Apr§‡‡	+2.0 Q4	+1.8	-2.7	8.53	243	188
Norway	+4.3 Q1	+5.7	+0.9	+1.0 Mar	+0.3 Apr	+1.2	3.0 Mar‡‡	+70.7 Q4	+13.8	+13.3	2.05	6.07	5.44
Poland	+4.4 Q4	na	+2.6	+2.8 Apr	+4.0 Apr	+3.5	12.9 Apr§	-22.6 Mar	-4.1	-4.0	5.47	3.55	2.78
Russia	+4.9 Q1	na	+3.5	+1.3 Apr	+3.6 Apr	+4.8	5.8 Apr§	+110.3 Q1	+3.9	-0.9	8.71	32.8	28.1
Sweden	+1.5 Q1	+3.1	+0.7	-6.5 Mar	+1.3 Apr	+1.6	7.8 Apr§	+37.8 Q1	+7.1	-0.1	1.41	7.24	6.23
Switzerland	+2.0 Q1	+2.8	+0.5	-1.4 Q4	-1.0 Apr	-0.4	3.1 Apr	+94.4 Q4	+13.3	+0.3	0.63	0.97	0.85
Turkey	+5.2 Q4	na	+3.5	+2.4 Mar	+11.1 Apr	+9.5	10.4 Feb§	-71.8 Mar	-8.8	-1.9	9.24	1.85	1.60
Australia	+2.3 Q4	+1.7	+3.0	+2.1 Q4	+1.6 Q1	+2.6	4.9 Apr	-32.8 Q4	-2.9	-0.7	3.06	1.03	0.94
Hong Kong	+0.4 Q1	+1.6	+2.6	-2.2 Q4	+4.7 Apr	+4.0	3.3 Apr‡‡	+12.9 Q4	+6.5	+1.0	1.07	7.76	7.78
India	+5.3 Q1	-1.0	+7.1	-3.5 Mar	+10.4 Apr	+7.7	9.8 2011	-59.0 Q4	-3.1	-5.7	8.52†††	56.1	45.1
Indonesia	+6.3 Q1	na	+5.9	+0.8 Mar	+4.5 Apr	+5.3	6.3 Q1§	-3.8 Q1	+0.2	-2.2	na	9,485	8,544
Malaysia	+4.7 Q1	na	+4.0	+0.6 Mar	+1.9 Apr	+2.4	2.9 Mar§	+29.7 Q1	+12.6	-5.3	3.55	3.16	3.02
Pakistan	+4.2 2012**	na	+4.0	-3.6 Mar	+11.3 Apr	+10.1	6.0 2011	-2.8 Q1	-3.3	-6.1	13.40†††	93.5	85.8
Singapore	+1.6 Q1	+10.0	+3.1	-0.3 Apr	+5.4 Apr	+4.2	2.1 Q1	+53.2 Q1	+20.7	+0.1	1.49	1.29	1.23
South Korea	+3.0 Q1	+3.7	+3.0	nil Apr	+2.5 Apr	+2.8	3.5 Apr§	+27.0 Apr	+1.9	+2.7	3.73	1,176	1,080
Taiwan	+0.4 Q1	+2.8	+2.8	+8.4 Feb	+1.4 Apr	+2.0	4.2 Apr	+41.9 Q1	+8.1	-3.7	1.24	29.8	28.8
Thailand	nil Q1	+52.1	+6.0	+0.5 Apr	+2.5 Apr	+3.2	0.7 Feb§	+6.5 Q1	-0.2	-2.5	3.52	31.9	30.3
Argentina	+7.3 Q4	+3.2	+3.8	-0.5 Apr	— ***	—	7.1 Q1§	nil Q4	+0.1	-0.6	na	4.47	4.09
Brazil	+1.4 Q4	+1.3	+3.3	-2.1 Mar	+5.1 Apr	+5.3	6.0 Apr§	-51.6 Apr	-2.6	-2.7	3.08†††	2.01	1.60
Chile	+5.6 Q1	+5.7	+4.5	+0.5 Mar	+3.5 Apr	+3.9	6.5 Apr§‡‡	-4.2 Q1	-2.7	+1.8	na	518	467
Colombia	+6.1 Q4	+5.4	+5.1	-1.6 Mar	+3.4 Apr	+3.4	10.4 Mar§	-10.0 Q4	-2.2	-1.7	7.01	1,829	1,822
Mexico	+4.6 Q1	+5.3	+3.5	+3.1 Mar	+3.4 Apr	+3.7	5.0 Apr	-7.1 Q1	-1.3	-2.4	7.75	14.1	11.6
Venezuela	+5.6 Q1	+2.2	+4.7	+2.3 Mar	+23.8 Apr	+22.9	8.6 Apr§	+26.7 Q1	+7.1	-6.7	12.24	4.29	4.29
Egypt	+5.2 Q1	na	+3.0	+26.5 Mar	+8.8 Apr	+10.4	12.4 Q4§	-5.4 Q4	-1.5	-10.4	na	6.04	5.95
Israel	+3.3 Q1	+3.0	+2.1	-1.4 Mar	+2.1 Apr	+1.9	5.4 Q4	+0.2 Q4	-1.0	-3.7	4.37	3.88	3.45
Saudi Arabia	+6.8 2011	na	+5.0	na	+5.3 Apr	+4.7	5.4 2009	+174.4 Q4	+23.6	+12.5	3.68	3.75	3.75
South Africa	+2.1 Q1	+2.7	+2.8	-2.8 Mar	+6.1 Apr	+5.4	25.2 Q1§	-13.7 Q4	-4.6	-5.2	7.75	8.50	6.95

Source: Haver Analytics. *% change on previous quarter, annual rate. †*The Economist* poll or Economist Intelligence Unit estimate/forecast. §Not seasonally adjusted. **Year ending June. ††Latest 3 months. ‡‡3-month moving average. §§5-year yield ***Official number not reliable; The State Street PriceStats Inflation Index, Apr 25.73%; year ago 25.89% †††Dollar-denominated bonds.

The Adjustment …. Subordinate, Spasmodic & Sporadic

- **DID NOT HAVE CLEAR OBJECTIVES**
  - Illiquidity or <u>insolvency</u>? (Balance between conditions in Greece and the EU)
  - Fiscal, financial, **PLUS** private sector adjustment
- **WAS NOT TECHNICALLY SOUND**
  - No <u>*prior*</u> expenditure, functional or social reviews
  - Cut public expenditures *versus* <u>expenditure switching</u> *versus* <u>tax increases</u>
  - <u>No drivers of growth</u> (public infrastructure, domestic demand, health, etc.)
  - Role of private sector including <u>the informal/shadow economy</u>
  - <u>Adding measures</u> rather than sequencing
  - Lack of capacity *versus* <u>“Greece does not honor her obligations”</u>
  - Time horizon (2012?!)
- **IS NOT SOCIALLY ACCEPTABLE**
  - Demolition of employment relations
  - Horizontal wage cuts, no cut off point for the poorest
  - Regressive taxation
  - Closed *versus* protected professions
  - No protection of the poorest and vulnerable

Insolvency Treated as Illiquidity
(Debt/Deficit ratios)



Eurostat/ US Office of Management and Budget Quoted from "In European Crisis, Little Hope for a Quick Fix", New York Times 30/09/11

Conclusion:
Is Greece a special case?

Greece seems to be now within the <u>"new normal"</u> in Europe:

- High and rising sovereign indebtedness
- No room for monetary policy (no functional banks, zero interest rates)
- Excessive fiscal consolidation
- Weak financial systems
- Low growth –high and rising unemployment
- For how long?

John Lipsky

Acting Managing Director, International Monetary Fund
"The Challenges of Economic Policy Cooperation", Kurt Viermetz Lecture
The American Academy, Berlin 21 June 2011.

- "The post-2008 crisis increase in debt-to-GDP ratios of 25-30 percentage points would require fiscal adjustment over the next twenty years to first stabilize and eventually return public debt to pre-crisis levels relative to GDP"

Thank you