GREECE'S SUDDEN FALTERING ECONOMY: FALLING COMPETITIVENESS AND INSTITUTIONAL WEAKNESS IN A HIGH GDP GROWTH RATE CONTEXT (1995-2008)*

Professor Theodore Pelagidis,
University of Piraeus, Greece
London School of Economics, Hellenic Observatory, Britain

Four factors led to the strong growth of Greece's economy during 1995-08:

1. Greece's economy accession to the eurozone together with the creation of competitive credit and capital markets as well as the macroeconomic stability that followed the EMU accession.
2. The shipping and tourism industry boom (plus the real estate to a lesser extent)
3. the improvement resulting from productivity enhancing infrastructure especially in the Athens, 'Olympic Games', greater area that were financed largely by the EU structural funds but also by private sector partnerships.
4. the satisfactory deregulation of the telecommunications industry and some other infrastructure

However, at the same time, the poor performance regarding competitiveness is documented by:

1. The persistent deficit of the current account in double-digit numbers (12-14% of GDP),
2. The persisting inflation differential with the euro zone (around 1.5-2.0% during 2008), which is observed for both goods and services.
3. The unattractiveness of Greece to net foreign direct investments that are practically zero
4. The consistent ranking of Greece by all competitiveness, business environment, administrative cost and governance surveys at a rank that is disproportionally low when compared to its per capita GDP and the productivity that is measures as GDP per worker.

Corruption matches well with this.

Detailed analysis shows that:

• High growth rates were mainly due to 'irrespectable of competitiveness' demand injections (cheap credit, money from tourism and shipping boom, EU structural funds, the boost from the Olympic Games and Athens area infrastructure, extensive public borrowing) and some reforms (banking, telecoms, some Private-Public Partnerships but that is it more or less).

• High Productivity index during that period is a combination of an artificially ballooning GDP (nominator) and low labour force participation rate (denominator). (Closed markets + low competitiveness being the culprit for that).

• Very few unregulated and tax evading self employed (over)work and few salaried employees work in Greece as product, service and as a consequence, labour markets are extremely close and rigid. So, unemployment and non-employed rates are very high, especially among unconnected young.

- The, at the same time, "high productivity- 'high (and of bad quality) market regulation' " puzzle is explained very well in the above context. High productivity is rather a deception, extensive market regulation and low competitiveness (in a high demand growth environment financed by borrowing and 'subsidies' indeed)- is true.
- Persisting inflation differentials and double-digit current account deficits and budget deficits + zero FDIs are only phenomena / consequences of falling competitiveness.
- The consistent ranking of Greece by all competitiveness, business environment, administrative cost and governance surveys at a rank that is disproportionally low when compared to its per capita GDP (Even compared to the productivity that is measured as GDP per worker, that we said we believe is to some or to a large extent, a deception).
- Corruption and institutional weaknesses characterized mainly by rent-seeking match well with this.

Policy should, thus, be oriented towards:
Open markets, reduce unnecessary regulation, encourage reform in education and job creation (through any kind of tax credits), fix public finances by cutting public waste and taxing the untaxed privileged so as not to hit domestic demand. Create incentives for the black economy to incorporate to the official one. And build well working, independent institutions and an administration that is not corrupted by the rents created now by closed markets.

The current situation and need for the aforementioned policy reforms require for a group of reform-minded politicians that will not yield to the pressures of the interest groups and that will have sufficient knowledge to use the significant powers of government, in spite of the fact that the administration is a weak tool for policy implementation. They will have to significantly change the "rules of the game" by setting the legislative framework for free and competitive markets across the board. This effort must also be complemented with the establishment of sufficient checks and balances and the setting of the legal basis for the widespread establishment of transparency and accountability in all levels of government and administration, which are also topics for further research.

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* You may see a longer paper by Prof. Pelagidis entitled "Greece's sudden faltering economy: The paradox of falling competitiveness and weak institutions in a high GDP growth rate context (1995-2008)" at www.cceia.unic.ac.cy