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The ball is now in Greece's court

by Michael Heise

Greece has been offered the prospect of further financial aid from the EU in order to ease the country's social hardships. A gesture of solidarity. Now, however, the ball is back in the Greek government's court. To date, it has missed practically all of the targets that it had vowed to meet before the elections. The economic recovery that emerged in 2014 has come to a standstill and nascent hopes of economic improvement have been dashed. The public budget has slid back further into the red, tax revenue is falling and people are pulling their savings out of Greek banks. The repeated calls for debt cancellation have once again barred access to the capital market. What sort of investor could be interested in buying Greek bonds with debates like these raging in the background? The situation was a very different one only last year, with even ten-year Greek government bonds being placed at acceptable interest rates.

If the Greek government fails to take action to counter these developments, the social situation in Greece will deteriorate further and lead the country to the brink of economic collapse. But many of the new government's reform plans do actually tie in with the expectations of the country's creditors: more effective taxation of income from large fortunes, combating nepotism and corruption, reforming the legal system, which currently does little to penalize people committing these crimes, and setting up land registries. Although these reforms have been on the agenda for years, not much has actually happened. The new government would have the power and the opportunity to tackle the necessary changes. Imagine the positive signals that it would send out to the country's creditors and, most importantly, to Greeks themselves if real steps were finally taken in this direction. In the long term, this sort of systemic change would allow the country to flourish.

In terms of fiscal policy, Greece wants to boost social expenditure and public sector employment and do without any proceeds from privatization. It cannot, however, simply leave taxpayers abroad to finance these plans. The country cannot borrow any new funds on the capital market and even the renewed debt relief that the government is currently calling for would do little to help, because the loans granted by the European countries are already largely exempt from any interest or capital repayments for many years to come anyway. Greece can only raise additional funds if it lays the foundation for economic growth and collects its tax receivables. If it fails to do so and the point of a sound budgetary policy is fundamentally called into question, the country's creditors will not be prepared to pay out any further loan tranches, let alone launch new lending programs.

Greece has to decide which direction to take: does it want to end its membership of the eurozone and, in doing so, inflict even more drastic loss and hardship on its people, or does it want to address the systemic reforms that are urgently needed to modernize the country and without which the financial aid supplied by Greece's partners is pointless? Despite all of the rhetoric, the government is likely to go for the second option.