The Crisis in Greece: A (Kind of) Brief Guide

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I’ve heard a lot about some sort of crisis in Greece. What’s going on there?

Put simply - many bad things. But before we can discuss the specifics of the recent happenings in Greece, we need some context about the country. It’s a country in southern Europe that you probably know best as the creator of the Olympics, the setting for the movie 300, and the home of Plato. Shockingly, there’s a bit more going on in Greece than just that. Between the years of 1932 and 2001, its currency was called the **drachma**. However, in 2001, Greece joined the Eurozone, and began using the Euro as its main currency. And thus, one of the largest economic conflicts in history came to rise. I know this doesn’t really answer your question, but we’ll need some more background before we can do that.

What’s the Eurozone?

The **Eurozone** is essentially an assortment of European countries that have agreed to use the Euro as their form of currency. The Eurozone consists of Austria, Belgium, Cyprus, Estonia, Finland, France, Germany, Greece, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, the Netherlands, Portugal, Slovakia, Slovenia, and Spain. Just to give you an idea, a Euro is equivalent to about 1.09 USD (though this will fluctuate). The Euro is generally regarded as one of the most liquid forms of currency. **Liquidity** is how much of a currency is available in the form of cash, which is important given how much of the “money” in the world exists solely in the form of credit. Countries in the Eurozone are supposed to follow a number of basic rules, like having no more than 3% in budget deficits, but many countries (including Greece) have violated these rules in the past only to face few to no consequences. The crisis in Greece has also given rise to the idea that the Eurozone, while united financially, **needs to create a political union** so they’re all on the same page in that sense as well.

So what actually happened in Greece?

So it turns out the problem we’re dealing with started in the 1990’s - the thing is that nobody actually knew. Since the 1990’s the **Greek government has been reporting numbers regarding their deficits and debts that are significantly lower** than what was actually true. Every time a new government was elected, they’d be shocked to find out what had been done, but they only proceeded to do the same thing. **Companies including Goldman Sachs have been revealed to help Greece cover this up**. In 2009, **everything was spilled** and the true budget deficit of was revealed. At 13.6% of the country's total economic output, or Gross Domestic Product (GDP), this deficit was the second highest rate in the world, relative to the GDP, of any country, second only to Iceland (which has made an impressive recovery since then through the use of capital controls).

So how did Greece get into such a bad situation? Well there's a number of causes. For example, after joining the Eurozone, **Greece faced an increase in labor costs**, leading to a trade deficit as their products became less competitive due to increased prices. A **trade deficit** exists when a country consumes more than it produces. Greece also has a **huge problem with tax evasion**, costing them a potential 20 billion Euros annually, as many people work in the **gray market** (unofficially) and the government does a poor job of enforcing the income tax code. This is obviously an issue because the main source of income for any government is taxes. Additionally, Greece has around a 25.6% **unemployment rate**, so many citizens are not able to make sufficient income to pay for their lifestyles. There are a few other factors, such as **extremely high government spending** (coupled with the fact that their income had decreased due to the growing tax evasion problem), which worsened the situation. Greece already had a relatively bad deficit problem before they joined the Eurozone, but it only ended up getting worse once they joined. To clarify, **deficits aren't always bad**. Governments **can use the money to invest in ways to grow the economy and increase revenue**, like what we've seen in the United States. The United States has a pretty strong economy and it has been running a deficit for more or less the past 50 years.

Anyway, joining the Eurozone **wasn't all bad** for Greece. After joining the Eurozone, Greece **faced lower bond yields on their government bonds**, which basically means bond prices increased as more money was invested into the country. The correlation is thought to indicate that **investors believed Greece was less of a risky investment as a part of the Eurozone as compared to how it was alone**. Remember though, they still had a deficit problem. Earlier, they were able to borrow money at relatively low interest rates to pay back their debts because people figured Greece, and actually the entirety of the Euro, was a safe bet. However, in 2009, when the insanely high deficit levels were revealed, **investors weren't so sure about Greece anymore**. They started asking for higher and higher interest rates on the loans they'd give Greece. Greece, needing the money, had to accept these higher interest rates to pay back the loans they had already taken. As a result, their deficit just got worse and worse as this continued in the form of what's known as a **vicious cycle**. This was the beginning of what's come to be known as the **Greek Depression**.

Yikes. What'd they do to get out of this situation?

Well normally, a country facing such a stop in investment, couple with such a high deficit, **usually tries to make its currency depreciate, or lose value, through high levels of inflation**. This will encourage investment while allowing the country to pay back the debt in a cheaper currency. Sounds great, right? The problem is that **Greece didn't have this option since they used the Euro**. **Only the European Central Bank can print money,** or have any control whatsoever on the Eurozone's monetary policy. **That might be the biggest problem with the Eurozone**. Countries like Germany were and still are strongly against printing any money because it'd hurt the German economy. They also don't want to send any more money to Greece, because they don't see why they should be suffering for Greece's inability to pay its debts.

The problem got so bad, though, that the world couldn't just sit around and watch this happen. So in come the European Commision and the International Monetary Fund (IMF) to the rescue **with a 110 billion Euro bailout**. The European Central Bank also helped out by buying some of the Greek debt while increasing access to capital for the Greek banks. These three institutions (the European Commision, the International Monetary Fund, and the European Central Bank) eventually earned the nickname **The Troika**. All this help might seem very generous on the part of The Troika, but the Eurozone as a whole wasn't in the best condition at that time. As interest rates in Portugal, Ireland, and Spain were rising, there were **fears that the Euro would collapse in its entirety, which would cripple the global economy**. Also, remember, this was just a loan - not a gift. **Internal IMF papers were later revealed to acknowledge that the loan to Greece was known to be unmanageable for them to pay back as expected**, but the IMF refused to forgive any of the debt regardless. In exchange for this huge loan, Greece was forced into agreeing to **austerity measures**, meaning an increase in taxes alongside cuts in pensions and other benefits.

Did this fix the problem?

As I'm sure you can tell from the recent news reports, not really. The Greece budget deficit did, however, **decrease from 25 billion Euros in 2009 to 5.2 billion in 2011**, which is obviously a massive improvement. But the Greek economy **also faced major contraction**. Because of the austerity measures, **people had less money to spend as pensions decreased while taxes increased**. This led to the collapse of many businesses and **unemployment rates over 25%**. As the economy shrank and people had less money, tax revenues followed in suit, and the government faced a significant decrease in revenue. **So if anything, the situation just worsened.**

What'd they try after that?

In 2012, the Troika loaned Greece another 130 billion Euros, with more or less the same terms as the previous loan. But with 30% of Greeks living in poverty and nearly 20% without enough money to buy food to meet their daily nutritional needs, **the situation remained relatively poor**. Granted, from a **wider European economic perspective, the outlook has significantly improved over the past 5 years as a result of these bailouts**. Private European banks **now own much less Greek debt** than they did in 2010 **as a result of decreased investment in Greece**, while the economies of Ireland and Portugal are in **much better shape**. So while Greece wasn't in the best situation, **the fear about a major catastrophe from a collapse of the Greek economy or even Greece exiting the Eurozone (dubbed the Grexit) was significantly quelled.** Obviously the effects wouldn't be great if such an event were to occur, but at the very least, some potential damage has been mitigated.

So what is it that I've been hearing about in the news lately then?

At the end of last year, **a new leftist government was elected that was firmly against the austerity measures that came with the bailouts**. They argued that austerity was never going to accomplish anything because the **economy will continue to contract at least as fast as the deficit**. So they got rid of the austerity measures. In response, The Troika stopped sending them the loan payments, which forced a series of negotiations. Eventually, the Greek government said that their stance would be decided through a **referendum**. Basically, they put the matter to a vote with the national population, very similar to a national election. The two options were essentially, “Yes, we’ll keep the austerity measures to continue receiving the loan payments” and “No, we’re done with the austerity measures - we’re fine with not getting the loan payments”. Given the **short amount of time the population had to properly inform themselves on this matter**, lack of actually understanding the situation was a major problem. Further, the **government currently in office campaigned heavily for the “No” vote**, which, on July 5 of 2015, ended up **winning overwhelmingly**. This was unsurprising given how unpopular the austerity measures had been among Greek citizens. This vote was nothing more than **symbolic** though, as The Troika had pulled their offer from the table on June 30.

And so in present day Greece, there’s very much still a problem. As of June 29 of 2015, Greek banks were ordered to remain closed all week, ATM withdrawals were limited to 60 Euros a day, and only urgent international transfers were allowed. These measures that Greece implemented are called **capital controls.** Greece limited how much money people can withdraw at a time because Greek banks are thought to only have around 500 million Euros left, which equates to about 45 Euros per person in Greece. Many of the ATMs are **out of cash**, and others can only dispense 10 Euro notes because they’re out of 20’s. They also **closed the market** for quite a bit of time, knowing that everyone would immediately sell all their investments if possible, which would only make the market collapse more severe. **If this continues, Greece will eventually have to print some form of alternate currency**, because the government is also constantly spending their limited supply of money on retiree payments and government employee salaries. If this happened while Greece kept the Euro, the situation could worsen because the alternate currency would not have stable government backing. Regardless, the odds of this are extremely low, as Greece has neither the machines it used to make drachmas nor the money to buy new machines to make drachmas.

Negotiations occurred between Greece and international lenders in July, leading up to Greece receiving a potential new bailout of 86 billion euros over three years, and talks remained in session throughout August. A decision had to be agreed upon by August 20, because a payment of 3.2 billion Euros is owed to the European Central Bank from Greece on that date. Shortly after, on July 16, the Greek government ended up agreeing to austerity measures to go in pair with the bailout. On August 4, Greece reopened markets for the first full day of trading, and as expected, shares plummeted by around 30%. While the situation is definitely bad, the **proposed bailout has made the odds of a Grexit significantly lower**.

On August 20, Greece received the first 13 billion Euros of its the bailout package, having agreed to the terms, which allowed them to pay back the 3.2 billion Euros they owed to the European Central Bank. This was followed by Greece Prime Minister Alexis Tsipras resigning and calling for an early election.