



### What Explains the Greek Economic Crisis?

In 2008, a number of developed democracies underwent a profound economic crisis that by many measures was the worst since the Great Depression. These countries saw a sharp decline in housing prices and stocks, high unemployment, and negative or minimal growth. While many developed democracies have since slowly emerged from this crisis, profound effects remain, such as increased inequality. Of all the countries affected by the recession, the worst hit was a seemingly unlikely one—Greece. After 15 years of steady growth, between 2008 and 2012 Greece's GDP fell by an astounding 27 percent, which is roughly the same amount as in the United States during the Great Depression. Why did Greece fall so far?

Greece was a latecomer to both industrialization and liberal democracy. After World War II, the country experienced a devastating civil war that pitted communists against the monarchist government. During that war, both sides received support from their respective Cold War allies. The defeat of the communists and the end of the civil war did not create stability, however. Battles between leftist and rightist parties eventually resulted in a military coup and a dictatorship that lasted from 1967 to 1974. Following the end of military rule, the political parties that came to dominate politics—particularly the Panhellenic Socialist Movement, which ruled for much of the next 30 years—used clientelism to institutionalize their support. This strategy was reinforced by the relatively underdeveloped economy. In the absence of private economic opportunities, political parties could offer state benefits, such as jobs, to their backers.<sup>9</sup>

The result was a system that benefited those connected to the political parties but raised significant barriers to others. The Greek civil service grew large and offered some of the highest levels of compensation. The state created many regulatory barriers, making economic development difficult. Regulations emerged that limited such things as the number of pharmacies, lawyers, and long-haul truckers that were allowed to operate. These regulations have contributed to discrepancies in unemployment; the unemployment rate stood at 17 percent in 2019 (over double the rate across the European Union as a whole), and for those under 25 it was over 30 percent.

Finally, the deep connections created by clientelism between the state, economy, and political parties have led to widespread corruption. According to Transparency International, on its scale of corruption Greece ranks 67th out of 180 countries. That is a big improvement due to recent reforms, but it remains one of the worst in Europe. Many businesses function in a “gray” or informal sector (see Chapter 10) where they are unlicensed and can therefore avoid state regulations and tax obligations. By some estimates, this group comprises over a quarter of the economy, functioning outside the law. Individuals and formal businesses similarly evade taxes, often by bribing tax officials or simply counting on the fact that an overburdened tax-collection system cannot catch them. This corruption points to a broader failure of state autonomy, capacity, and overall legitimacy; as we have noted earlier, tax compliance can be a function less of enforcement than of the

public's general sense that taxation is acceptable and that most people are participating. In Greece, the *fakelaki*—a small envelope of cash, necessary to secure public services ranging from health care to building permits—has essentially replaced the tax system.

The combination of these institutional factors explains the Greek crisis. In Greece, the weakness of the private economy combined with the state's corruption and outlays through clientelism has meant that the government has consistently faced a large budget deficit. Greece adopted the euro in 2001 on the condition that it would reduce its budget deficit. Instead, it fudged its books and continued to run high deficits, which as an EU member, it easily covered by borrowing money. As deficits continued to grow, so did debt.

What finally triggered the Greek crisis was the recession in the United States. Once the U.S. housing bubble popped, investors grew nervous about investments elsewhere in the world—including Greece, whose debt and deficits were becoming clearer. Investors were no longer confident that Greece could sustain its economic situation or that the EU could or would bail the country out. Short of funds, the Greek government was forced into dramatic austerity measures: tax increases, a later retirement age, limits on pension benefits, and massive cuts to defense, health care, and education. Total household income dropped by a third. Not surprisingly, the economic crisis has led to political instability and polarization, which saw the rise of parties on the far left and far right. Greece's economic situation has improved, but it still is burdened by the highest unemployment rate in the EU—six times higher than that of Germany. Not surprisingly, Greece also confronts a brain drain as young people leave the country in search of jobs. This hampers economic recovery, as



A woman walks past the Bank of Greece headquarters with a wall covered with graffiti: "Rob to Get Money," as well as "Bank of Berlin." This reflects the widespread view that the European Union, dominated by Germany, has forced unbearable economic cuts on the Greek state.

those leaving tend to be university graduates and other highly skilled individuals—precisely those needed to sustain economic recovery.

1. In what ways did the Greek government's use of clientelism hinder economic development?
2. What role did Greece's membership in the EU play in advancing its economic crisis? What concerns does this raise about the EU in general?
3. How has Greece's political and economic corruption affected the state's capacity and legitimacy?