Tax breaks and VAT-free trade areas can help to kick start the regional growth that Greece badly needs

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While Greece's recent elections have reassured the international markets for now, this confidence is likely to disappear once again if Greece does not undertake more reforms aimed at restarting growth. **Dimitrios Thomakos** *argues that one of Greece's major problems is the concentration of population around Athens. A targeted initiative of tax breaks for individuals and businesses in combination with the introduction of VAT-free trade areas may be able to encourage new businesses to start and encourage growth.*

The recent Greek elections provided immediate buoyancy to the international markets, against the continued pressure of the European debt crisis. But this relief may be short lived if stronger measures are not soon taken to revitalize the growth potential, in Greece and the rest of Europe. In a recent article we looked at the main causes of the Greek crisis, focusing on the current account deficit. In that study we provided empirical results showing that Greece can be "saved", if the structural reforms and fiscal discipline program are actually implemented. But these arguments refer to economic measures that are primarily designed as short-to-medium term adjustments that will improve Greece's fiscal and debt positions and may not immediately relate to growth. It is now accepted by all, economists and politicians, that restoring growth goes hand-in-hand with fiscal measures to provide a sustainable economic recovery. Greece's growth potential can be boosted by actions that go beyond the tyrannical "regulatory microstructure reform" and are related to a longer-term vision of renewed prosperity and economic development.

Let us consider first the distribution of population in Greece. According to 2010 Eurostat data we have that over 4 million inhabitants, or about 36% of the total population of 11 million, live in the prefecture of Attiki which covers less than 3% of the total land area of Greece. The population density in the Athens metro area is higher than that of Berlin (which has about the same population), higher than that of Paris (which has twice the population) and on par with London. If you next think about the distribution of the available resources in Greece you will find that they are to be found outside of the larger metro area of the capital and if any longer-term development is to take place it cannot really happen within the geographical limitations of Athens and its suburbs. The resources and job potentials are just not there anymore and the old ways depending on heavy construction, retail trade and services are now gone. Growth incentives cannot be separated by population mobility incentives, and where people go skills and capital soon follow. Creating new or reviving urban centers outside Athens may well play a role in the future development of Greece – and in doing so the metro area of Athens will be revitalized as well. So how do we provide incentives for such regional development?

Time-limited tax breaks for both business and individuals is a good place to start. Don't be alarmed, the government coffers can still be filled by the growth aftereffect of such breaks. And note that I insist that tax breaks go to individuals as well. This is contrary to the standard approach of giving tax breaks only to businesses – for investing and relocating. These businesses still need customers to buy their products and boosting local demand is an important factor. Contrary to the popular "export-based" model, which is fraught with difficulties as to the degree that can generate enough local employment, the proposed approach gives incentives to both businesses and families to work together at the local level on renewing the money flow required for spurring growth.

The easiest way to implement tax breaks is to have lower (personal and corporate) income tax rates for a number of years, or for a fixed initial period of say 2 to 5 years after relocation. For businesses relocating to take advantage of such tax breaks, a sensible way to compensate for the loss of public income is to require an entry fee and to allow competition among prefectures on the level of such fees. A newly started business can then choose a new location based on a trade-off structure that will depend on a variety of factors: what does the area have to offer vis-à-vis the fee required and the cost of moving?

Another approach to generate an increased flow of goods, services and people would be to create VAT-free trade areas in different locations where public land could be provided for development. Businesses compete with one another for space, make the investment and get the benefit of the tax breaks and potentially increased demand for their products, now sold at lower prices. Families can either choose to relocate to a VAT-free trade area to benefit from lower cost of living but are required to stay there a minimum number of years – in this case they get the benefit of no VAT so they probably get no tax breaks; or they can travel there for recreation and shopping making such VAT-free areas attractive for tourism as well.

Regional development and population mobility cannot happen overnight and require bold actions to be implemented – going beyond the legalistic approach of taking care a billion of details of "how" and "when" and letting families and businesses decide if they will make the move or not. If sensible motives are provided and prefectures are allowed to compete for fresh faces then, in time, it can be done successfully. Others have done it, so why not the Greeks?

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