The great Greek exceptionalism (on recessionary austerity and government effectiveness)

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The latest round of negotiations between the Greek government and the 'troika' must have convinced even the most romantic of those following the Greek crisis that the Greek state is not serious(ly committed to the policies and reforms emanating from the bailout agreements). The 'conclusion' of the negotiations left again Greece with a 'halfhouse fix' that includes a partial release of the next tranche of the bailout funds and an agreement for the continuation of the 'negotiations' in the autumn. The uncertainty in the country remains, the problems of inefficiency in the public administration remain, the economy continues to be squeezed and squashed, and society is still in turmoil.

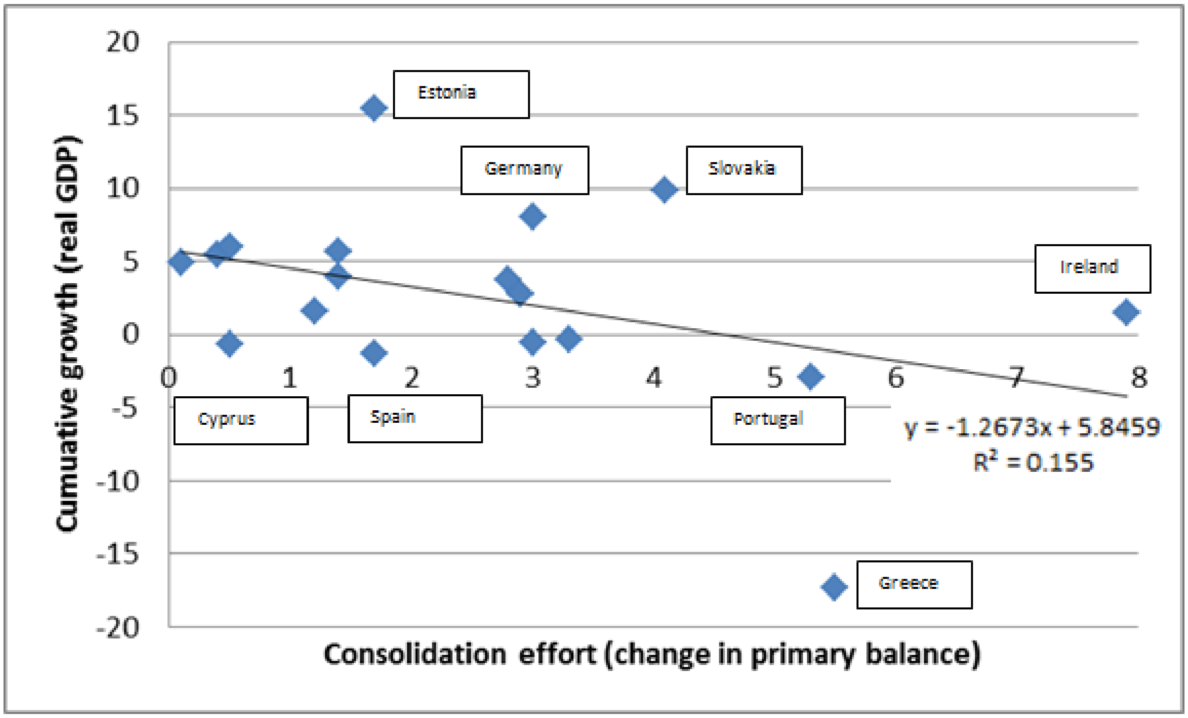
But Greece starts its summer season with two exceptional innovations, never seen before in the 'developed' world: the closure of its public broadcaster (the 'interim' EΔT is not a substitute – by the way, take a look here) and the abolition of its municipal police (effective 'from September'). In both cases the government justified its decision on the basis that these two institutions, the organisations running these two public services, were inefficient, ineffective, corrupt, or simply 'non-reformable'(!) And in both cases the real reason was that the government was unable to deliver even partially on the public sector downsizing that it promised, first time in March 2011, then in July 2011, again in October 2011, and again in February 2012, July 2012, December 2012, and April 2013: again and again and again and again.

According to the Minister for Administrative Reform, who was responsible for the decision concerning the municipal police, the institution of municipal police has failed – strangely enough, only in Greece among all countries that ever tried the institution and only when the government had a shortfall of 3,500 in its long-awaited public sector mobility programme (I have found this as a relevant background study – not sure about its quality or accuracy). So the municipal police officers are hastily integrated into the state police. From there, they will presumably (nobody actually knows, as no relevant plan has been published) continue to provide the same services as they did before – only this time more effectively, as they will now be free from the chains of their "failed" organisation. More conveniently – but also more incredibly – they may even take up additional tasks, of formal policing, despite the fact that they do not have the relevant training or qualifications. Importantly, this will somehow have no adverse impact on the quality or effectiveness of policing and crime prevention. (Not that anybody has claimed, or even considered, this; but it follows logically from the government's reasoning.)

This is only one – the latest – example of the way in which Greece (and successive governments since 2010) engages with the issue of reforms and public sector restructuring: its ad hocery and lack of design, purpose and seriousness in policy-making. Some (myself included) have argued repeatedly that it is in these 'qualities' of Greek policy-making that one can find the explanation for the country's seemingly unstoppable slide into pauperisation: the negative growth; the rising unemployment and the cultural and financial impoverishment of society. But for many others, this is the wrong conclusion: one that looks at the tree and misses the forest, that fails to see the big picture – the big picture being either/both the systemic character of the crisis (the 'Greece is not to blame' argument) and/or the fallacy of austerity (the 'wrong recipe' argument). I am very reluctant to subscribe to either of these arguments, so I decided to devise a simple test to see if I can find anything Greek-specific, any evidence of 'Greek exceptionalism', to explain the continuing immiserisation of Greece.

So I collected data from Eurostat and plotted the size of fiscal consolidation in the Eurozone countries over the last three years against the growth rates that each of these economies registered during the same period. The outcome is the picture shown below. As can be seen, practically all countries have implemented some degree of fiscal consolidation since 2009, with primary deficits being reduced by between less than 1 percentage point of GDP (in the Eurozone 'offshore' economies: Luxembourg, Cyprus and Malta) and 7.9 percentage points of GDP (in Ireland). Many countries (but by no means all) have also experienced negative growth during the period: in fact, cumulative growth since 2010 ranges from +15% (in Estonia) to -17% (in Greece). Overall, one can definitely see a negative correlation, meaning that more austerity coincides with less growth (technically, the elasticity of growth to fiscal consolidation is -1.3, with the R-squared at 0.155 and a corresponding correlation coefficient of -0.39), a correlation that can rather safely be interpreted in causal terms as 'austerity causing recession'. This is the visual depiction of the "austerity doesn't work / self-defeating austerity" argument.

Fiscal consolidation and growth performance in the Eurozone (2009-12)



Source: Author's manipulation of Eurostat data (tables gov_dd_edpt1 and tec_00115).

But there are a few more things one can note from the scatterplot. First, the recession in Greece is exceptional. Portugal, for example, has implemented a similar consolidation (horizontal axis) in its public budget but its economy shrank by only a fraction of the contraction seen in Greece (3% versus 17%). Estonia's fiscal consolidation (by 1.7 percentage points) has in fact been accompanied by economic expansion (positive growth) – apparently, and rather 'exceptionally', for some curious reason austerity in Estonia seems to work! Ireland seems to be another 'exceptional' case. Here, a fiscal contraction greater than in Greece has produced growth rates comparable to those of the Netherlands – in fact, comparable also to those of the UK, which is free of the 'systemic failures' of the Eurozone. Even Spain, on which much of the 'systemic failures' argument is built, has seen a rather moderate decline in its GDP, with a contraction of only 0.8 percentage points for every unit (in terms of percentage of GDP) of fiscal consolidation – compare this to a value of 3.1 for Greece!

Given so many 'exceptionalisms', I decided to remove Greece from my sample and look again at the austerity-recession relationship. As if by magic, when Greece is taken out of the picture the austerity-recession spiral all but disappears! (correlation drops from -0.39 to -0.21 and the corresponding regression coefficient loses completely its statistical significance, with a p-value of 0.43). All in all, the statistical link between austerity and recession appears rather precarious: some countries grow indeed faster than others and some countries implement deeper budget cuts than others, but there is very little to suggest a systematic relationship between the two. Rather, what we see is that the 'rate of transformation' between austerity and growth varies greatly across countries: some countries, including both ones that have had to resort to limited fiscal effort (Estonia) and ones that had to take extremely harsh fiscal measures (Ireland), seem to have been much more effective in weathering the effects of austerity; others, most notably Greece, have a much less heartening picture to show in relation to their consolidation-recession record. The countries lying above the regression line (especially Estonia, Slovakia, Germany and Ireland) have been rather effective; inversely, the countries lying below the regression line (basically, the Eurozone 'south', plus Slovenia and – interestingly – Holland) have suffered disproportionately from any given amount of austerity – with Greece being by far the single most 'abnormal' case.

One of course can raise various objections here. That my 'results' may be spurious as I do not control for other factors influencing growth, that I impose a causal interpretation on a simple correlation, that I don't look at the actual size and mix of spending cuts and tax-hikes, that I am missing the counter-factual (how much growth we would have in the absence of austerity), that I should be looking at changes in the output gap than in actual GDP, that I don't take into account the role of exogenous factors and external actors (such as Merkel and the markets), etc. All these criticism are valid – some more, some less. But I seriously doubt they would change the overall picture: a picture that depicts the greatness of Greek exceptionalism in all of its glory. A picture that shows Greece, uniquely within the tormented Eurozone, not only as the only country without a public broadcaster, the country with a failed municipal police, the country with the largest and longest recession in post-WW2 Western Europe, but also as the country with the highest austerity-recession transformation rate: the country that produces more recession for any given level of austerity than anybody else in Europe. If this is not a proof of ineffective government, I don't know what is.