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EU Measures in Response to Greece's Economic Situation

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In response to Greece's deep budgetary crisis the EU adopted an action package whose purpose is to make Greece take some radical consolidation steps in the public finance sector, as well as to implement structural reforms. The form of granting financial assistance (which would be an important signal for both financial market participants and Greek society) has yet to be officially presented. It would seem right for the IMF to take part in that action.

The Greek case poses a challenge for the EU in terms of economic policy coordination in the fiscal dimension (whose most crucial instruments are surveillance of the EU states' budgetary discipline and monitoring the compatibility of their economic policies with the general guidelines adopted by the Council). Following the entry into force of the Lisbon Treaty, both these competences were strengthened in respect of the Euro zone states (Art. 136 of the Treaty on the functioning of the European Union), a point which gains in importance in terms of the Greek case.

Surveillance of the Budgetary Discipline. Greece has been subjected to strict surveillance under the Excessive Deficit Procedure (EDP, under Art. 126 of the Treaty on the functioning of the European Union), implemented through the Stability and Growth Pact, formally launched (in respect of Greece) in April 2009 by setting a short space of time for the correction in the deficit (2010). In December 2009 the ECOFIN Council decided that Greece failed to take effective actions in order to reduce the deficit (Art. 126 (8)). That decision was influenced by the startling revelations of the data concerning the actual state of the Greek public finance (let alone the lack of progress in the implementation of consolidation measures).

In mid-February 2010 the ECOFIN Council launched another stage of EDP (Art. 126 (9) of the Treaty on the functioning of the European Union) requiring Greece to submit a precise schedule of the necessary deficit reduction steps by 16 March. These steps are meant to cause the deficit to drop by 4 percentage points in 2010 down to 8,7% (some of these measures should be employed by 15 May 2010). The expected actions include raising some of the indirect taxes (e.g. excise duties on cigarettes, alcohol and fuel), implementing progressive tax rates for all income sources and abolishing tax relief, freezing nominal wages, reducing other public sector spending, and overhauling the pension system. Most of the measures were laid down in the January 2010 Greek Stability Programme (which received the opinion by the ECOFIN Council in February 2010), and the remaining ones will be presented in early February. The Council appealed for additional austerity measures aimed at deficit reduction in 2010 (so did the EU Commissioner for Economic and Monetary Affairs Olli Rehn on his 1 March visit to Athens) and at identifying measures aimed at reducing the public sector deficit down to under 3% by 2012. Greece is also required to improve its budget reporting system as well as reform its statistical system, whose numerous shortcomings were exposed in the Commission's special report in early January 2010 (the European Commission opened an infringement procedure against Greece for violating the EU law on statistics standards).

The Greek government is supposed to submit a report containing a register of necessary measures for Greece to fulfill the obligations imposed by the Council, and then to report quarterly on the progress in their implementation. Should Greece fail to implement necessary actions a range of sanctions under the EDP might be imposed, such as the imposition of a non-interest-bearing deposit or the imposition of fines which are to press for the necessary efforts at reducing deficit.

Economic Policy Monitoring. Additionally to the above decisions, the ECOFIN Council adopted recommendations for Greece (Art. 121 (4) of the Treaty on the functioning of the European Union) whose purpose is to restore the compliance of Greece's economic policy with the general guidelines in that respect—since 2005 the integrated guidelines for growth and jobs, which are the basis of the renewed Lisbon Strategy. Such recommendations further improve the negative assessment of the Strategy implementation by successive Greek governments. The recommendations contain a wide range of reforms for Greece to carry out in order to improve its competitiveness. They include: administration, labour market reform and education reforms as well as improving the regulatory environment for companies. However, the recommendations are rather "soft," which makes the EU have less influence over Greece than under the EDP actions.

Financial Assistance. Ever since the European Council adopted its general approach towards financial assistance for Greece (during its 11 February 2010 informal session), no specific proposals were presented as to the form of the assistance. Thus, financial market participants' prolonged uncertainty regarding the developments in Greece rose as warning signs of further downgrade in the state's credit ratings appeared (revealed at the end of February 2010 by the two international rating agencies Standard&Poor's and Moody's). With no external assistance, the Greek government would experience more problems with financing its borrowing needs that are to exceed €53 billion.

One can believe that the solution taken into account (e.g. by Germany) is creating an assistance programme to the value of €20–25 billion (an amount corresponding to Greece's short-term needs in terms of debt-refinancing). In framework of this programme we would see the direct purchase of the Greek bonds or offering guarantees to commercial banks buying these bonds by the German state bank KfW and its French counterpart Caisse des Dépôts. The lack of relevant details renders it difficult to make a clear judgement whether such a solution would be in compliance with Art. 125 of the Treaty on the functioning of the European Union which makes it impossible for both the EU and any of its Member States to be liable for another EU Member State's public sector commitments (the so-called no-bailout clause).

The involvement of the International Monetary Fund in the assistance operation for Greece is still rather unlikely. Putting the Euro zone image aside, the IMF involvement seems a rational solution considering the EU formal limitations, as well as the IMF functions. The International Monetary Fund, which expresses its readiness to grant assistance to Greece, has at its disposal a set of credit options for countries struggling with financial stability problems. The agreement of the 2009 London G20 summit gives IMF even more a lending capabilities (lending resources were to ultimately increase by $500 billion, €125 billion of which is to be lent by the EU states). The IMF made in 2009 some far-reaching changes in the application of the conditionality of support principles (primarily in respect of the way of assessing the progress in structural reforms required from the beneficiary-countries) and thus became more flexible in dealing with specific cases. A slight difficulty may emerge in the event of the IMF involvement, namely the need to link the IMF assistance programme with the EU budgetary surveillance activities. That difficulty could, however, be solved by means of a formal agreement between the two institutions. For now IMF cooperates with the European Commission and the European Central Bank by monitoring the steps taken by the Greek government—the first joint mission of the representatives of these institutions took place in February 2010.

Conclusions. The current contrast between the EU active approach to launching a wide range of actions (concerning the surveillance and monitoring), and the difficulties in adopting financial assistance programme for Greece largely result from the EU terms of reference. The lack of a formal financial support mechanism for countries of the Euro zone makes the burden of responsibility for granting potential assistance rest primarily with them. As a consequence, the Euro zone states (with Germany at the forefront) are clearly trying to delay taking the decision, stressing at the same time the need for Greece taking further reduction steps. The financial assistance could ensure a more stable framework for these efforts and mitigate the anti-EU social mood which rose in Greece over the past weeks. The best possible solution would be to create an assistance programme encompassing both the IMF resources and the support offered jointly by the Euro zone states in accordance to Art. 125 of the Treaty on the functioning of the European Union.