The implications of the greek referendum's outcome

Introduction

This paper will examine the social welfare and economic implications of the recent 2015 referendum on Greek bailout conditions offered by the ECB and IMF, starting with and examination of the history behind the crisis, the resulting series of financial bailouts along with the conditions imposed and their economic and social welfare ramifications, and the potential irrelevancy of the recent 2015 referendum on the actual outcome of the negotiations.

The Background to the Greek Debt Crisis

The Greek debt crisis essentially started in late 2009, after economic reports about the Greek government's current deficit and debt levels made clear that the Greek government had deliberately under-reported their current deficit and financial situation in 2008 and 2009, with the deficit at the end of 2009 estimated independently at 12. 5% of Greek GDP, twice the amount reported by official Greek governmental figures during that time (Simitis, 2014). These issues were further exacerbated by the revelation that Greek sovereign debt exceeded the 91. 4% of Greek GDP previously reported, and actually stood at 126. 8% of total Greek GDP due to a number of debts and liabilities within the Greek public sector that had been over-looked during the previous reports issued by the Greek Ministry of Finance (Simitis, 2014). These discrepancies in reporting raised serious concerns over Greece's ability to accurately report its current financial situation, and the resulting sovereign debt ratio of 128% of GDP raised serious questions over the government's ability to meet its current financial obligations (Ardagna and Caselli, 2014). The results of the revelations, occurring during the aftermath of the recent global financial crisis, led to a downgrading of Standard and

Poor’s credit rating of Greece to BB+, a rating which indicates a significant possibility of default on borrowing (Standard and Poor, 2015). This caused the interest rates of 5 year bonds issued by the Greek government to rise to 5. 385% in November 2009, a figure 1. 42% higher than the average rate of all other similar Euro-zone government bonds during that time (Simitis, 2014). This also occurred at a time where the Greek government was running a significant structural deficit, with governmental spending at 53. 2% of GDP, and public revenue of only 37. 8% (Ardagna and Caselli, 2014). In other words, only further borrowing would be able to sustain the current level of Greek public services, borrowing which had just became exponentially more expensive to maintain.

Given the developing crisis in the Eurozone, the European Central Bank (ECB) chose to step in and offer assisted bailouts and loans using funds appropriated from other EU member states and the IMF (Baimbridge and Whyman, 2014). To this end, the Commission, the ECB and the IMF established the European Financial Stability Fund (EFSF, 2015). The EFSF issued a bailout loan of €110bn in 2010 to the Greek government, which came with the condition that tight austerity measures be put into place, including a number of cuts across a broad spectrum of public services and a series of tax increases to boost governmental revenue (Ardagna and Caselli, 2014). Similar conditions were given to other recipients of bailout loans from the EFSF, including Ireland and Portugal, who as of 2014 have successfully reduced their national debt levels and current account deficit to that specified by the bailout conditions (Baimbridge and Whyman, 2014). However, the Greek government was hit with a further recession in 2011, with GDP growth contracting by 9. 6% in the 4th quarter of 2010, and then a further 10. 4% fall in the 1st quarter of 2011 (World Bank, 2015). The continuing economic problems faced by Greece were due to a number of factors, including a severe fall in revenue from both tourism and shipping due to the global economic crisis, two of Greece's most important industries, and significant discrepancies between total taxes owed and total tax revenue, with total tax income in 2012 being €51. 99bn, against the expected €110. 79bn as reported by a State Audit Council report (Argitis and Nikolaidi, 2014).

These conditions meant that Greece was unable to continue to meet its financial obligations in 2012 and again faced the possibility of sovereign debt default, requiring another bailout loan to be made by the EFSF of another €130bn, with additional conditions attached that required Greece to cut public spending by a total of €3. 3bn by the end of the year, followed by further cuts of €10bn by the end of 2013, and again in 2014 (Ardagna and Caselli, 2014).

The Ramifications of the Imposed Bailout Conditions

The austerity measure conditions that were included as conditions on the two separate bailout loans to the Greek government were met with strong resistance from the Greek populace, and a number of anti-austerity demonstrations and riots occurred throughout the country in 2010, 2011 and 2012 (Simitis, 2014). The public reactions to the suggested austerity measures have been suggested to be responsible for the Greek government's delay in more fully and efficiently implementing the necessary austerity measures and tax collection reforms necessary to close the gap between public spending and revenue (IMF, 2014).

Despite the social and economic issues resulting from the Greek populace's resistance to the bailout conditions, in 2014 the Greek economy appeared to be on the road to recovery, with improved economic performance and growth across the Eurozone driving recovery in both the tourism and shipping industries, and the achievement of a structural surplus, mainly due to a series of stringent cuts to governmental spending and public services, including the closure of the state-owned broadcasting company ERT (IMF, 2014). These improved economic conditions allowed Greece to once again issue government bonds on the private equities market since the initial bailout had been implemented, allowing the Greek government a much-needed source of finance to cover any future spending gaps, with Greek government-issued 5 year bonds being traded at interest rates of 4. 95% in mid-April of 2014, at their lowest rates since the start of the 2009 debt crisis (IMF, 2014).

An early parliamentary election was called in late 2014 after the current parliament was unable to vote in a new President for the 2015-2020 term with a parliamentary majority (Ardagna and Caselli, 2014). The Syriza party, which had been highly vocal in recent years about their lack of support for the austerity conditions imposed on Greece by the IMF and ECB, won a near majority and formed a coalition with a minority right-wing party in order to have the Syriza party leader Alexis Tsipras elected to the Presidential position. Upon gaining office, Mr Tsipras stated his refusal to respect the current bailout conditions imposed by the EFSF, with the intent of renegotiating more favourable terms (Ardagna and Caselli, 2014). The ECB and IMF responded by suspending any and all aid payments to Greece until either the existing deal was upheld or a new mutually-acceptable deal was agreed upon.

The resulting uncertainty caused significant economic and social upheaval within the country; the Athens stock exchange experienced its worst loss in total value in the following week since the 2011 recession, while interest rates of Greek bonds rose sharply in the private market, eventually reaching a peak of 24. 19% in early June, severely reducing the newly-established governmental ability to raise finance in the private equities market (Dellas and Tavlas, 2013). The resulting economic uncertainty caused a run on Greek banks, where customers were desperate to withdraw all their cash to protect against the risk of a banking industry collapse, which ironically severely increased the likelihood of such a collapse occurring (Mankiw and Taylor, 2014).

In response to this socio-economic panic, the government issued a series of capital control measures that restricted the current opening hours of Greek banks while only allowing daily withdrawals of €60 from personal accounts either through the bank or ATM (The Economist, 2015a). The government also placed restrictions on foreign transactions and foreign currency trading, to prevent Greek investors from transferring their funds to a currently more stable currency. However, these measures only served to deepen the social welfare issues within the country, as the number of foreign imports dropped dramatically due to the restrictions placed on foreign transactions, including in a number of key areas such as medical equipment, medication, food and farming materials, leading to severe social welfare issues during the negotiation period (The Economist, 2015b).

The 2015 Referendum

After a series of negotiations with the ECB and IMF that failed to reach agreement on the conditions of a new deal, Mr Tsipras, the Greek President, called for a public referendum on the proposed conditions put forward by the ECB and IMF in the latest meetings of June 25th. The announcement was made on June 26th, with the referendum to be held on the 6th of July (The Economist, 2015c). This is an incredibly short length of time to ruminate on a complicated issue, one which could have profound effects for the social, political and economic future of one’s country. The referendum paper itself also does not contain any details on the June 25th proposals, it merely asked whether the respondent is willing to accept them or not in a straightforward Yes or No ballot (The Economist, 2015c). Mr Tsipras, who campaigned for the No vote, listed those proposals during his campaign, including a controversial suggestion to raise taxes on tourism-related income that was later retracted by the ECB on June 26th, the day Mr Tsipras called the referendum (The Economist, 2015c).

Despite the public excitement surrounding the referendum itself, it is clear that the referendum was a tool that would have failed to provide a welfare maximising outcome regardless of the result. As Arrow (1950) notes, it is impossible for a ranked-order voting system with three or more options to provide a welfare-maximising solution that satisfies three criteria of fairness; first, that each individual holds a set of ordinally-ranked preferences that do not change with the introduction of alternative options; that the final outcome should satisfy the majority of voters; and that no one individual has dictatorship power over the vote. While the referendum at first appears to be a ranked order voting system with only two options, which would negate the relevance of Arrow's Impossibility Theorem, the options themselves are not clearly defined. The majority No vote of 61. 3% (BBC, 2015) merely rejected a specific set of conditions which were already irrelevant and out-dated at the time of the referendum. The results did not indicate whether those voters wish to accept different conditions, or to exit the Eurozone altogether, suggesting that there were more than two reasons for choosing one of the options that voters were inherently unable to express. Thus, those who voted No while expecting it to lead to a Greek exit from the Eurozone or a rejection of all further austerity measures would be ultimately disappointed.

The referendum was also biased in terms of Arrow's (1950) fairness criteria in one major way; there was indeed one individual with dictatorship power over the vote itself. The referendum results were merely used to gather public opinion on an out-dated bailout condition offer; the results were not legally-binding, and in the event of a Yes vote Mr Tsipras would still be free to return to the negotiating table and attempt to renegotiate further with the ECB and IMF (The Economist, 2015c). The referendum was clearly used as a means for Mr Tsipras to gain leverage during negotiations in the case of a No vote, potentially to imply that Greek voters would support withdrawing from the Eurozone altogether if necessary, though as noted those voters would end up disappointed along with the rest who voted against further austerity measures, as despite the referendum results Mr Tsipras agreed to a further €86bn bailout from the EFSF on the 14th of August, with 4 main conditions to the deal: a structural surplus of 3. 5% of GDP to be met by 2018; a series of pension system reforms intended to cut public sector pension spending (a condition with serious social welfare implications for the elderly and retired); reforms to labour and product markets to increase competitiveness; and a series of banking sector reforms intended to recapitalise the private banking sector (Wearden and Fletcher, 2015).

Conclusion

The 2015 Greek Referendum bailout conditions referendum was never capable of offering a welfare-maximising solution for voters; in fact, it barely offered any social, political or economic solution at all. Voters rejected a set of conditions that had already been altered at the time of the referendum, and were subsequently presented with a new bailout deal containing further harsh austerity measures such as cuts to public pension funding. It is doubtful whether the results of the referendum actually offered Mr Tsipras additional leverage in subsequent negotiations, but it is clear the Referendum results had little impact beyond this meagre measure

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