This article is about the current state of the Greek Economy and what changes need to be made.

To be able to fully understand the current status of Greece’s economy, it will be necessary to comprehend the Greek sovereign debt crisis that occurred in 2008 and how it originated. Essentially, when Greece joined the European Union in 2001, it was mandatory for their budget deficit to be 3% so they could meet the Maastricht criteria, which was required for Greece to join the European Union and adopt the Euro as their currency. In reality, their budget deficit was 12.9%, immensely higher than what it was supposed to be, causing their debt to grow (Amaedoe). As a result of understating their deficit figures for years, they could no longer borrow money from banks ("explaining Greece’s") and rate agencies reduced Greece’s credit rating, which ultimately proved to be to the detriment of Greece since costs of future loans skyrocketed. Moreover, investors were scared off and it eventually became even more rigorous for Greece to repay their loans. This only increased their debt and put them on the path toward bankruptcy (Amadeo). In order to address this dire issue, organizations such as Troika, the International Monetary Fund (IMF), and others issued Greece with a bailout plan of 240 billion euros. However, it was mandatory for Greece to meet certain austerity measures, including vast decreases in budgets, high increases in taxes, and cuts in government expenditure. Nevertheless, Greece’s sovereign debt crisis has remained since the majority of the borrowed money does not go into the economy. Rather, it goes towards reducing its immense debt load ("explaining Greece’s") and paying off their debts interest, which merely ensures that banks are capitalised (Brunsdon). As such, Greece’s aggregate demand remains minimal, below its potential and they fail to pay off their debt.

The four macroeconomic objectives any nation wishes to accomplish is full employment, price stability, economic growth, and equity in the distribution of income. Currently, Greece, part of the European Union, lacks financial autonomy and its own monetary policy, meaning it cannot control its own money supply and interest rates. As such, any present government policies implemented to improve the state of the four macroeconomic objectives include the austerity measures imposed by Troika, which only work to a certain extent. Thus, austerity and retraction are Greece’s ongoing economic policies. The first macroeconomic objective is full employment and it allows a nation to be considered healthy. This is described as 3-5% unemployment. While the European Union has an average unemployment rate of 7.2% as of January 2018, Greece’s unemployment rate as of December 2017 is 20.8% (Unemployment Rate).

![Unemployment Rate in Europe (monthly), 2018. Google Public Data Explorer.](image)

![Figure 1: Unemployment Rate in Europe (monthly), 2018. Google Public Data Explorer.](image)

Looking at the graph, which depicts Greece’s unemployment rates, from the early 2000’s till 2008, when Greece’s economy was at its peak, it was close to the European Union average. Once the Greek economic crisis occurred in 2008, the nation’s economy began to retract and cyclical unemployment began. Consequently, from 2008 to 2013, Greece’s unemployment rates rapidly increased. This is due to the fact that the harsh economic terms imposed on Greece have increased the unemployment rates greatly since the increase in taxes has led to firms letting off more workers in response to the decrease in aggregate demand. This occurred as the banks stopped lending, market confidence declined, and the government stopped spending. This has led to a decrease in aggregate supply in order to remove the market surplus that was caused by a lowered aggregate demand, explaining the reduced workforce.

The middle class has been struggling with draconian conditions of constant rounds of salary cuts and tax rises, the only thing Greece was able to do to avoid bankruptcy. Not only this, but pensions were lowered and indirect taxes were slapped on things ranging from beer to fuel, while even the value-added tax (VAT) was raised, which only increases the levels of inequity in income distribution in the nation. Since the austerity measures, economic conditions in the nation have become so poor that the public has begun to fail to give receipts in order to avoid paying taxes just to make ends meet. Additionally, Greece’s aggregate supply has diminished by almost a third over the past six years due to the imposed cuts on government expenditure, further increasing the unemployment rate as with less consumption a smaller workforce is needed to provide a lesser output. Workers are also let off as the increase in business taxes has increased the costs of production, therefore cuts need to be made.
made. Almost half a million Greeks have migrated to other nations due to Greece’s absurdly high persistent unemployment, at above one-fifth of the total labour force (Smith).

However, in the long-term, since 2013, Greece’s unemployment rate has consistently been decreasing as the austerity measures eventually led to a certain degree of price stability. This is because of the decrease in the budget deficit and the fact that they showed signs of slow economic growth. Meanwhile, initially, Greece was only averting bankruptcy.

Although, from 2015-2016, the unemployment rate increased slightly due to the impending referendum and the Greek referendum in July of 2015 since Greece could not meet the demands of the bailout plan. As a result, Greek parties realised they could not turn their economic promises to fruition, and employment levels decreased. After this period, the downward trend in the unemployment levels graph continued, now getting closer and closer to the European Union (EU) average, but at an extremely slow rate. Yet, Greece’s unemployment levels remain to be too high, meaning that Greece still is not using all available labour resources in the most efficient way possible, hurting their economy. Other consequences of high unemployment rates include social costs such as an increase in crime rates, depression, homelessness, and in divorce rates.

The second macroeconomic objective is price stability, which, in general, is low and stable inflation rates, ranging from 3-5%. However, the monetary policy of the European Central Bank wishes for inflation rates below, but near 2% (“Monetary Policy”). In 2018, Greece’s inflation rate was below the Central Bank’s target, at 1.3% compared to the previous annum (“Greece: Inflation”).

![Greece Inflation Rate](image)


The above graph depicts the fact that after the 2008 economic crisis, in 2009, Greece’s high inflation rapidly increased, being an example of cost-push inflation, a result of a negative supply shock. This is because Greece surprisingly announced its false deficit figures and Troika’s austerity measures led to an increase in the costs of production for the nation’s producers through increased regulation by the EU and increased business taxes. However, soon after the reductions made in government expenditure led to a shrinkage of Greece’s aggregate demand and supply from the full-employment level of output, severely decreasing the nation’s average price levels, or inflation. This was also aided by decreases in wages, part of Greece’s budget cuts, serving to counteract cost-push inflation (“Explaining Greece’s”).

As previously mentioned, Greece regained price stability a couple of years after the crisis, hence the disinflation that can be witnessed from 2010 to 2013. There were numerous causes in this disinflation, such as a decrease in government spending, a decrease in wages, decrease in rent costs, et cetera. This was necessary and beneficial for Greece’s economy as if its inflation rate was too high, there would be a variety of negative consequences for Greece. For one, with high inflation rates, workers will desire higher wages in order to adapt to the higher average price levels. This is not something Greece could do as the austerity measures demand a decrease in government spending, which cannot occur with increased wages. Furthermore, low inflation rates are most desired for nations since there is consumer confidence over future price stability and businesses can invest, spend, and save without concerning about future decreases in the value of their investments and savings. This is why it is vital for Greece to have low inflation rates and meet the European Central Bank’s target of 2% inflation.

Greece reached low levels of inflation, and eventually levels of deflation, which is not preferred as it causes higher unemployment and delayed consumption, directly leading to further deflation and a deflationary spiral. This only lasted for a short period of time, albeit, and Greece has been on a generally upward trend of low inflation ever since, showing to be a success. However, there have of course been some alterations in this trend due to external reasons such as a change in the seasons, since consumer spending varies throughout the year, or due to other reasons such as the Greek referendum or changes in oil prices by OPEC. Greece cannot control these external factors, and neither can the European Bank, yet they still slightly affect inflation rates. With low inflation, compared to high inflation, household’s real income will increase, making consumers feel richer compared to the average price as they can now purchase more with the same levels of income. They will feel wealthier with the lower rates of inflation as the real value of their income increases when inflation drops. Similarly, real interest rates for savers will increase and there will be lower nominal interest rates for borrowers, thus decreasing the cost of borrowing money that can be invested in capital or to buy goods and services. Consequently, household and business spending will increase, leading to a vast increase in aggregate demand, in turn spurring the economic growth Greece so crucially needs.

The third macroeconomic objective is known as economic growth. Greece’s GDP per capita growth (per annum) is 0.22% as of 2016. It has been on the rise since 2011 when it was as low as -4% (“Greece - GDP per Capita”), when the economy was in retraction. An appropriate level of GDP per capita growth is defined as around 2-3%.
As shown in the graph, Greece’s Gross Domestic Product (GDP) growth was for the most part at an elevated rate leading up to 2008 (above or close to 5%). This is a rate that was unsustainable, and clearly not preferable, explaining Greece’s high budget deficit figures of 12.9% when its business cycle was at its peak (GDP Growth). Since then, Greece’s lenders have mandated that they significantly lower their government expenditure in order to decrease their debt. Following the financial crisis, the economy of the nation has been in the doldrums as it has experienced numerous quarters of negative growth and four recessions in a period of nine years (Martin). This is exhibited on the graph through the massive decrease in the GDP growth rate up until 2011 when it actually reached a level of around -9.3%, a trough in Greece’s business cycle. Essentially, Greece’s budget and fiscal deficit figures were so extremely high that it was necessary for the economy to shrink in order for them to be addressed, meaning Greece’s economy was in the contractionary phase.

Since 2011, however, when Greece’s economic policy of austerity reached a certain level of stability, Greece achieved a recovery phase in its business cycle, with its GDP continuously growing (Smith). Because of discussions of Grexit and a referendum in 2014, credit ratings lowered, so the GDP growth rate lowered in 2015. This was in contrast to predictions by the IMF and Greece’s central bank that the country was poised for a strong recovery and that the economy would be growing by a minimum of 2.5% by 2017. The cause of this contraction in the economy in the fourth quarter of 2015 was a direct result of Austerity’s failure to complete the most recent bailout plan within 2016, as Greek head of state Alexis Tsipras had promised. As such, the central bank reduced its growth projections for 2017 to 1.5% ("Grexit-Economic"). Yet, from 2015 - 2016 when confidence in the Greek economy started to grow, the GDP started to increase. This is a result of Tsipras realising it would be beneficial to stay within the Eurozone since Greece does not possess financial autonomy so they cannot drive their own economy (Smith). However, while Greece’s GDP is growing, it is growing at a very slow rate since most countries in the European Union fear an uncertain economic future, meaning there is low business and household confidence in this region. Therefore, instead of investing and spending, they are saving (Amadeo).

The fourth and final macroeconomic objective is described as equity in the distribution of a nation’s income, which can be caused by economic growth since its benefits may not be equally shared across the different financial classes of society. This is especially true if the wealthy see their incomes rising dramatically in contrast to a stagnating middle class.
The above graph depicts the World Bank’s GINI Index for Greece. It is evident that since 2008, Greece’s GINI coefficient has been increasing rapidly from 33.9 to a peak of 36.2 in 2012. This is far from Europe’s average GINI Index of 31 (“European Union”). The Greek Economic crisis once more is the direct cause of this steep increase in Greece’s inequality with regards to the distribution of income. The austerity measures included indirect taxes on numerous common goods, worsening their income inequality. These indirect taxes are a form of regressive tax due to the fact that households with low incomes normally consume staple goods with a larger proportion of their income compared to households that possess high incomes since they save more money than the lower classes. As a result, when taxing commonly consumed goods by lower-income households, the poor face heavier tax burdens than the rich as they consume more relative to their total income. Thus, the disposable incomes of the poor will decrease while the disposable incomes of the rich will increase as they are already saving, so they will not give more of their income away as taxes. Moreover, Greece’s value-added tax (VAT), another form of regressive tax, has been increased, further increasing the levels of inequality in income distribution in the nation. In fact, the great income inequality Greece is experiencing has undoubtedly resulted in great relative poverty, which is the high unemployment levels aid with. It is primarily the lower classes that suffer the effects of this crisis.

Nevertheless, from 2012, when Greece’s GINI index was 36.2, and financial stability was accomplished to a certain extent, the GINI index lowered to 35.8 by 2014. Greece’s form of income taxation, which is progressive, showed to slightly improve its income equity since the richer classes paid the most in taxes since they can afford to do so, while those who cannot end up paying less. The end result is higher disposable incomes in poorer households (Hausen). This enables a higher standard of living in Greece, the ultimate goal behind income equity. Although progressive taxes tend to be the most successful method to decrease inequality, economists believe that it discourages hard work since you end up paying more in taxes the greater your income is. This has been made clear in Greece’s economy as the high tax rates have led to a proliferation in the presence of tax evasion in the nation (Hopper).

It is evident that Greece’s economy contains a myriad of issues that prohibit it from accomplishing all four macroeconomic goals. One appropriate method to address the issues that currently plague its economy includes an expansionary fiscal policy. Greece’s economy desperately needs an expansion in its money supply to encourage economic growth. One of their main creditors, the IMF, has been pushing for substantial debt relief in order to make it possible for Greece to pay off their debt and ease the austerity demand (“Explaining Greece’s”). This would allow Greece to escape the vicious cycle that they are currently in where the loans they receive fail to go into the economy itself and stimulate growth. Greece essentially needs to increase government spending. However, they cannot do this through a monetary policy, such as esparing the economy by lowering interest rates, since Greece is a part of the Eurozone and therefore lacks financial autonomy. Thus, an expansionary fiscal policy is needed. This, however, can only occur when the government possesses funds, which can be obtained through raising taxes. This is why Greece currently does, as it undertakes in a contractionary fiscal policy. A method like this certainly possesses limitations, albeit, and has shown to be ineffective in helping Greece escape the economic abyss it is currently in.

One common method of promoting equity in a typical economy is to increase the minimum wage. However, this would not work for Greece as there is already a lack of jobs, shown through the immensely high unemployment rates. Furthermore, businesses in Greece are struggling to make ends meet (Amades). Therefore by increasing the minimum wage, firms will simply lay off more workers to deal with the increase in the costs of production. This would only increase the unemployment rates, decreasing their output levels and overall making matters worse. Government revenue must be spent in a way that increases employment levels and income equity. One example includes transfer payments, such as subsidised employment. This is especially true for the youth, which possess a higher unemployment rate (Hausen), and will make it more attractive to firms to hire workers, increasing employment rates. Such transfer payments will provide greater opportunities for poorer households, making Greece more equitable. Besides the unemployment benefits, other examples of effective equity-enhancing forms of transfer payments would include welfare benefits. By giving more money to low-income households to purchase basic necessities, a dire issue in a fragile economic wealth, would be redistributed in the nation to a certain extent, increasing equity. This can also be done by reducing taxes. By lowering tax rates, income would again be redistributed in the nation since it increases the disposable income of those that consume the greatest proportionality to their income: the poorer households. Although, by increasing equity in the nation through the provision of public goods and lower tax rates, Greece’s government budget balance would be harmed as they would be increasing government spending and decreasing tax cuts, so their revenue would decrease, placing them in greater debt. This explains why Greece has refrained from making such economic actions, as they need to lower their debt, not increase it. This problem could be solved through debt relief and an increased supply of money by Greece’s creditors.

As previously stated, in order for Greece to switch from a contractionary fiscal policy to an expansionary fiscal policy, and so that transfer payments can be made, Troika and the rest of Greece’s international creditors must provide debt relief and give Greece the funds to start expanding. This will increase Greece’s surplus which will lead to more money going into the economy so it can start to grow. Furthermore, as the IMF has been urging for, when austerity measures are eased and tax rates are lowered (“Explaining Greece’s”), Greek households and firms will increase their consumption. With current austerity measures, the Greek people and businesses are struggling to survive. Thus, by reducing the austerity measures and introducing more money into the economy, consumers disposable income will increase. In turn, they will feel wealthier and will consume and invest in more goods and services. Through a rapid and great increase in demand, businesses would have incentives to expand and hire more workers instead of merely saving. This would ultimately increase employment in the nation, a move Greece so desperately needs.

The increase in the aggregate demand that would result from the increase in consumption can be demonstrated in Figure 5. Aggregate demand would shift outwards from AD1 to AD2, leading to an increase in Real GDP from Y1 to Y2 and an increase in the price level (inflation), from P1 to P2. While also causing an upward movement on the Long-Run Aggregate Supply (LRAS) curve. Figure 5 is an appropriate diagram to show the effects of an expansionary fiscal policy since due to Greece’s high unemployment levels, they are not producing at full capacity. Thus, it would cause a great percentage increase in real GDP with a less noticeable increase in price levels. This would be desired by Greece since their inflation needs only to increase minimally, yet their GDP needs to be growing at a much faster rate in order to meet the goals of the European Union.

Thus, a plethora of Greece’s economic problems could be visibly addressed by switching from a contractionary to an expansionary fiscal policy. While certain creditors would refuse to provide Greece with debt relief as they see it strictly as providing them with grants, the pros outweigh the cons in this circumstance. This is because it would allow for decreased taxes (particularly reduced regressive taxes), rebates, transfer payments, and elevated government spending that would lead to increased aggregate demand, stimulating economic growth. The long-term effects of such a change in the economy would be Greece being able to eventually pay back their debt since a growing economy would permit them to do exactly this.

Albeit, it is important to consider that a major assumption in implementing an expansionary fiscal policy is “ostensibly paribus” (all other things equal). However, it is impossible to hold all other external factors in the real world equal. As such, this new fiscal policy might not have all of the intended effects to the same extent as in theory. Nevertheless, it would still undoubtedly aid in fixing the issue at hand. Therefore, after assessing the current state of Greece’s economy in-depth, it is clear that what it truly needs is an expansionary fiscal policy.