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The Greek debt crisis - lessons for the ECOWAS single currency project

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**WEST AFRICAN
MONETARY INSTITUTE (WAMI)**

**INSTITUT MONETAIRE DE
L'AFRIQUE DE L'OUEST (IMAO)**



**WAMI OCCASIONAL PAPER SERIES
NO. 8**

THE GREEK DEBT CRISIS – LESSONS FOR THE ECOWAS SINGLE CURRENCY PROJECT

**ACCRA, GHANA
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THE GREEK DEBT CRISIS: LESSONS FOR THE ECOWAS SINGLE CURRENCY PROJECT

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EXECUTIVE SUMMARY

The study examined the Greece debt crisis by bringing into sharp focus the genesis, effects on the Greece economy, the European Union as well as the entire global economy. The motivation was primarily to glean lessons from the crisis with a view to enhancing the resilience of the existing monetary unions and more fundamentally to build sufficiently robust safeguards for emerging monetary unions such as envisaged under the ECOWAS Monetary Cooperation Programme (EMCP). The study employed qualitative approach by reviewing macroeconomic developments in Greece before and during the crisis based on data obtained from numerous sources including the IMF, World Bank, Bank of Greece, EUROSTAT, and EU Commission. The study noted that the crisis started in late 2009 due to a number of factors that could be broadly classified into exogenous and internal factors. The exogenous factors include the spillover of the 2007-08 global financial crisis, the subprime mortgage crisis of 2007–09, and the structural rigidities of the European Monetary Union (EMU). The internal factors were persistent fiscal deficits, loss of external competitiveness with the attendant current account deficit, misreporting of debt and fiscal data and the ensuing loss of Greek government credibility among lenders.

Macroeconomic performance of Greece prior to accession into the monetary union was characterized by financial instability and state interventions in many sectors that were supposed to be purely market driven. Macroeconomic imbalances and structural problems were exacerbated by oil price shocks, while monetary accommodation and the introduction of full wage indexation entrenched high inflationary environment. Consequently, productivity stagnated, investment declined, and unemployment rate doubled. To address the macroeconomic imbalances, the government embarked on a medium-term adjustment program in the late 1990s with the goals of reversing years of fiscal laxness and eliminating pervasive market distortions. Given the timing of the reform however, it could be reasonably adjudged that the whole essence was to ensure the admittance of Greece into the EMU.

Most of the reform measures ceased by mid 2000s with the persistence of large public deficits, leading to heavy indebtedness of the public sector. The country's government debt to GDP ratio was the second highest in the Euro zone by 2007. In addition to high public sector indebtedness, the private sector's debt burden increased substantially over the period. More specifically, the outstanding balance of Monetary and Financial Institutions (MFI) credit to Greek households increased to 45.6 percent of GDP in 2007, from 12.5 per cent in 2000, while credit to domestic businesses increased from 31.1 percent in 2000 to 48.8 in 2007. Gross external debt increased from

¹ The authors are staff of the Research and Statistics Department of the West African Monetary Institute (WAMI). The authors are grateful to the members of the Operations Committee of WAMI for their invaluable contributions to this paper. On behalf of WAMI, the authors wish to express their appreciation to the African Capacity Building Foundation (ACBF) for their financial support in publishing this paper. Finally, the views expressed in this occasional paper are those of the authors and do not necessarily represent the views of WAMI.

95.0 percent of GDP to 136.0 percent between 2003 and 2007. In comparison with the rest of the Euro zone, the various macroeconomic parameters appeared to be on the same trajectory beside public debt to GDP ratio.

The study observed that the Greek debt crisis has far-reaching implications not only on the Euro zone but on the global economy as well as monetary unions in the making. The crisis has the potential to snowball into major financial crisis in Europe given that most European financial institutions hold substantial investments in Greece. The crisis has also a strong implication for the stability of the exchange rate of the euro and its use as reserve money. Following the crisis, the euro has lost value, depreciating substantially against the US dollar. Thus, the long-term objective of making the euro second reserve currency after the US dollar will be in jeopardy. For the global economy, the crisis has the potential of sending signals to the market for bond holders to start paying attention to countries such as Japan, the UK and the USA with the likelihood of triggering another episode of global financial crisis. Thus, the modest and steady recovery that the global economy has enjoyed since 2009 will be short-lived.

With respect to upcoming monetary unions, the key question is that if the EMU with its level of sophistication, technology and advancement could fail, then it is not likely that other regions with comparatively less sophistication can succeed in their quest for monetary and economic integration.

The analysis of the issues revealed key lessons that must be brought on board in the quest to strengthen the existing monetary unions as well as ensuring the success of EMCP. These, among others are: the need for all member countries to meet and sustain the critical convergence criteria before joining the monetary union; the need to strengthen and expand the scope of the Stabilization and Cooperation Fund (SCF) and make it operational on or before the commencement of the ECOWAS monetary union; need for the development of a sovereign bond market and the general development of the financial sector to free the central and commercial banks from the burden of financing government; need to build up adequate revenue base through the diversification of the economy; need for an independent Central Bank that will guide monetary policy formulation and implementation and that can withstand the pressures from government for deficit financing; the need to continue monitoring the convergence process and multilateral surveillance even after the formation of a monetary union; the need to sacrifice reasonable degree of sovereignty for political convergence; and the need for accurate statistical reporting to be able to identify risks and take corrective measures promptly to avoid crisis that engender the survival of the monetary union.

Following this Executive Summary, the remaining parts of this paper are organized in eight sections. Section 1 gives a background to the Greece Debt Crisis to the ECOWAS Monetary Cooperation Programme; Section 2 presents a general overview of the Greek Debt Crisis; Section 3 outlines the evolution of the crisis, while Section 4 analyses the causes of the crisis. The implications of the crisis for the Euro Zone, the global economy and monetary unions in the making are discussed in Section 5; Section 6 contains the assessment of the efforts aimed at resolving the crisis. Section 7 presents lessons for ECOWAS single currency programme, while Section 8 concludes the paper.

Keywords: Debt Crisis, budget deficit, financial markets, Euro zone, ECOWAS Monetary Cooperation Programme, Monetary Union.

JEL Classification: F33, F36, G15, H62, H63

1.0 INTRODUCTION

Background to the Greek Debt Crisis

The Greek debt crisis started in late 2009, triggered by a number of factors including turmoil of the Great Recession (related to the financial crisis of 2007–08 and the subprime mortgage crisis of 2007–09). The financial crises exposed the structural weaknesses in the Greek economy and some structural fragility of the European monetary union and eventually leading to sudden crisis in confidence among lenders.

Persistent huge budget deficits in combination with declining external competitiveness played a decisive role in the Greek debt crisis. Increased public expenditure during the last decade following the launch of EMU led to dramatic increase in borrowing requirements and high levels of accumulated public debt. In addition, lack of the necessary fiscal consolidation and continuous false reporting of fiscal data undermined the Greece government credibility in the perception of international private creditors. The country's precarious fiscal position was further exacerbated by two longer-term trends: the anticipated reduction of the European Union structural funds from 2013 and increased financial pressures arising from speedy ageing of the working population.

The decline in competitiveness since the country's entry into the EMU, led to persistent deficits on the current account (Malliaropoulos, 2010). Increased "twin deficits" together with the lack of domestic structural reforms to address labour market rigidities, social security and market competitiveness weaknesses, forced Greece to issue new bonds at short maturity periods and at higher interest rates compared to Germany the "anchor" of the EMU. As a result, the ability of the Greek government to honour its debt service obligations questioned by the international capital markets with expectations of a high probability of sovereign default. As the financial crises evolved, the flow of funds from the European core countries to the periphery began to dry up.

On March 25, 2010, the EU leaders agreed to provide bilateral loans pooled by the European Commission (the so-called "Greek Loan Facility") for a total amount of €110 billion (consisting of €80 billion provided by the euro-area Member States and €30 billion from the IMF). This was a 3-year rescue package conditioned on implementation of austerity measures, structural reforms, and privatisation of some government assets. The First Economic Adjustment Programme for Greece was adopted by the Eurogroup on May 2, 2010. This was however followed by a decision of the Governing Council of the ECB to "suspend the application of the minimum credit rating threshold in the collateral eligibility requirements for the purposes of the Eurosystem's credit operations in the case of marketable debt instruments issued or guaranteed by the Greek government" (ECB, 2010) and that ECB should continue to accept Greek government bonds until further notice (ECB, 2012a and 2012b).

The continued successful auction and sale of bonds was however only possible at the cost of increased yields, which in turn caused further worsening of the Greek public deficit. As a result, the rating agencies downgraded the Greek debt to junk status in April 2010 (Eurostat 2011). This led to a freeze on access to the private capital markets, requiring the Greek financial needs to be covered by international bailout loans to avoid sovereign default. In April 2010, it was estimated that up to 70% of Greek government bonds were held by foreign investors, primarily banks. A year later, worsened recession along with delayed implementation by the Greek government of the agreed conditions in the bailout program revealed the need for Greece to receive a second bailout.

On March 14 2012, the Euro area finance ministers approved financing of a Second Economic Adjustment Programme for Greece; the Euro area Member States and the IMF

committed the undisbursed amounts of the “Greek Loan Facility” (that is the first economic adjustment programme) plus an additional €130 billion (including a bank recapitalisation of €48bn) for the years 2012-14. Private creditors holding Greek government bonds were required at the same time to sign a deal accepting extended maturities, lower interest rates, and a 53.5% face values loss. A total of €240bn was to be transferred at regular tranches through the period of May 2012 to December 2014. To address the worsened recession and continued delays in implementation of the conditions of the bailout program, in December 2012, the Troika² agreed on some debt relief measures, including an extra €8.2bn of loans from the IMF to be disbursed during the period of January 2015 to March 2016. Due to an improved outlook for the Greek economy, with achievement of a government structural surplus both in 2013 and 2014, along with a slight decline in unemployment rate and return to positive economic growth in 2014, the Greek government re-gained access to the private lending market through the sale of bonds to private creditors albeit at high interest rates to fully finance its 2014 gap.

However, following the formation of an anti-austerity Syriza-led government and its subsequent refusal to respect the terms of the bailout agreement, improved economic outlook was replaced by a fourth recession in the last quarter of 2014. The rising political uncertainty caused the Troika to suspend all scheduled remaining aid to Greece under its current program until such a time when the Greek government either accepted the previously conditional payment terms or alternately could reach a mutually accepted agreement on some new updated terms with its creditors. This rift caused a renewed and increasingly growing liquidity crisis (both for the Greek government and the Greek financial system), resulting in plummeting stock prices at the Athens Stock

Exchange, while interest rate for the Greek government at the private lending market spiked, limiting access to the private creditors as an alternative funding source.

Faced by the threat of a sovereign default, some final attempts for reaching a renegotiated bailout agreement were made by the Greek government in the first and second half of June 2015. Despite these attempts, Greece subsequently defaulted on a \$1.7bn IMF payment on June 29, 2015. Default will inevitably entail enforcement of necessary capital controls to avoid collapse of the banking sector and potentially could lead to exit (GREXIT) from the Eurozone due to growing liquidity constraints making continued payments of public pension and salaries impossible in Euro.

The pertinent question is if the Euro zone with high degree of sophistication in financial markets and advanced technology could experience crisis, what is the prospects of enduring success for less sophisticated monetary unions such as the EMCP? In addition, what are the possible lessons that could be learnt by other monetary unions particularly the EMCP from the crisis?

Against this background, the main objective of this paper is to identify the causes of the Greek crisis and the various lessons that the Economic Community of West African States (ECOWAS) can learn from such a crisis. The paper intends to explore qualitative analysis based on data from Greece National Bank, IMF, World Bank, EUROSTAT, and European Commission.

Background to the ECOWAS Monetary Cooperation Programme

The Economic Community of West African States (ECOWAS) was established in 1975 to foster closer economic and monetary integration among member states in order to raise the level of welfare and the standard of living of the Community citizens. In this

² The term Troika means the ‘group of three’ describing the European Commission, International Monetary fund and European Central Bank who

form a group of international lenders that laid down stringent austerity measures when they provided bailout during the euro crisis.

respect, the ECOWAS Monetary Cooperation Programme (EMCP) was adopted in July 1987 by the ECOWAS Authority of Heads of State and Government. The programme was intended to usher the sub-region into a single monetary Zone to complement the customs union /free trade area arrangement. A specialized institution called West African Monetary Agency was set up to create a single monetary Zone in ECOWAS in 1992. The target date for the EMCP was shifted several times because of weak political commitment on the part of member countries to implement the needed economic reforms to achieve the macroeconomic convergence criteria and the existence of parallel and uncoordinated schemes in the sub-region.

The Authority of Heads of State and Government, in order to facilitate the process of convergence and the emergence of a single monetary Zone in ECOWAS, in December 1999, decided on a two-track approach to economic and monetary integration in the sub-region. Under the arrangement, a second monetary Zone was to be established to organize the countries outside the first monetary Zone, the West African Economic Monetary Union (WAEMU), into a monetary union. WAEMU is an organization established in 1945, well before the establishment of ECOWAS, to provide a common means of payment for French-speaking West African countries. Thus, the idea for the formation of the second monetary Zone, the West African Monetary Zone (WAMZ), was to ensure that the countries outside the WAEMU were organized into a formidable and competitive union as the WAEMU. In the two-track approach, the WAMZ was scheduled to commence in January 2003, after a convergence process and after successful operations to be merged with the WAEMU into a single monetary Zone for ECOWAS. However, the fast-track approach could not materialize due to several reasons, including weak macroeconomic performance, non-ratification of legal instruments and weak institutional preparedness.

The Authority of Heads of State and Government following the transformation of

ECOWAS Executive Secretariat into ECOWAS Commission, in June 2007, directed the Commission to re-examine the monetary integration process with a view to creating a single currency for the Community. The implementation of this directive led to the development and adoption of the roadmap for the ECOWAS Single Currency Programme by the ECOWAS Convergence Council on 25 May 2009 with two major milestones, 2015 for the WAMZ common currency and 2020 for the ECOWAS single currency.

The Summit of Heads of State and Government during its 43rd Ordinary Session held on 17 and 18 July 2013 in Abuja directed the President of ECOWAS Commission to make every effort to expedite the harmonization of macroeconomic policies and take all necessary measures to ensure the realization of the second monetary Zone on time. In addition, the Extraordinary Summit of Heads of State and Government on 25 October 2013 in Dakar appointed President Mahamadou ISSOUFOU of Niger and President John Dramani Mahama of Ghana to oversee the creation of the common currency in a timely manner. The two Presidents constituted a Task Force to advise them periodically on the monetary integration programme. The Task Force consists of Ministers of Finance of Ghana and Niger, Special Representatives of the two Presidents, Governors of Central Banks in ECOWAS Member States, Directors-General of the West African Monetary Agency (WAMA) and the West African Monetary Institute (WAMI), and Presidents of ECOWAS and UEMOA Commissions.

The two Presidents made recommendations to the 44th Ordinary Session of Heads of State and Government of ECOWAS on 24 March 2014 in Yamoussoukro, Cote d'Ivoire relating to, among others, abolition of the two-track approach for a one-track approach, revision of the roadmap of activities for implementation. One key component of the roadmap is the establishment of an ECOWAS Monetary Institute (EMI) by January 2018. The ECOWAS Monetary Institute (EMI) is to create

the necessary conditions for a smooth transition to the new common currency. It also aims at facilitating the establishment of a common ECOWAS Central Bank (ECB) which would

issue the new common currency and conduct monetary policy for all countries in the ECOWAS region.

2.0 OVERVIEW OF THE GREEK DEBT CRISIS

The Greek debt crisis is the first of five sovereign debt crises in the euro zone. Other member countries of the European Union, which had debt crises, include Spain, Portugal, Ireland and Italy. The Greek financial crisis is different from the other crises that were to erupt in other parts of euro area (like Portugal, Ireland, Spain and Italy). While the Greek debt crisis was caused by a build-up of public sector imbalance as was reflected in large and growing fiscal and current account deficits, the crises in other parts of euro area countries were mainly as a result of banking crises. The Greek sovereign debt crisis also spilled over to the banking system, unlike other euro area where the crises originated from the banking sector and spilled over to the sovereign sector. The crisis which started in late 2009 was triggered by a number of factors including turmoil of the Great Recession. It is argued that as the global economy was hit by the financial crisis of 2007–08, Greece was hit especially hard because its main industries—shipping and tourism—were especially sensitive to changes in the business cycle. The government spent heavily to keep the economy functioning and the country's debt increased accordingly.

Fears developed about Greece's ability to meet its debt obligations from a revelation that previous data on government debt levels and deficits had been misreported by the Greek government. This resulted in crisis of confidence in the Greek economy, reflected by a widening of bond yield spreads and the costs of risk insurance on credit default swaps compared to other euro zone countries particularly Germany. By April 2010 it was apparent that Greece was becoming unable to borrow from the financial markets. Consequently, the Greek government, on April 23, 2010, requested an initial loan of €45 billion from the European Union (EU) and International Monetary Fund (IMF), to cover its financial needs for the remaining part of 2010. Credit Rating Agencies began downgrading Greek sovereign bonds.

The Standard & Poor's for instance, slashed Greece's sovereign debt rating to BB+ or "junk" status amid fears of default, in which case investors were liable to lose 30–50% of their money. The series of downgrades of Greek sovereign bonds generated increased uncertainty, leading to deposit withdrawals and deleveraging which reinforced each other, resulting in banking crises.

The continued successful auction and sale of bonds was however only possible at the cost of increased yields, which in turn caused further worsening of the Greek public deficit. As a result, the rating agencies downgraded the Greek economy to junk status in April 2010. This led to a freeze to the private capital market, requiring the Greek financial needs to be covered by international bailout loans to avoid sovereign default. In April 2010, it was estimated that up to 70% of Greek government bonds were held by foreign investors, primarily banks. A year later, worsened recession along with delayed implementation by the Greek government of the agreed conditions in the bailout program revealed the need for Greece to receive a second bailout.

The First Economic Adjustment Programme for Greece was adopted by the Eurogroup on 02 May 2010 under which the EU leaders agreed to provide bilateral loans pooled by the European Commission (the so-called "Greek Loan Facility") for a total amount of €110 billion (consisting of €80 billion provided by the euro-area Member States and €30 billion from the IMF). This was a 3-year rescue package for Greece conditioned on implementation of austerity measures, structural reforms, and privatisation of government assets. This was however followed by a decision of the Governing Council of the ECB to "suspend the application of the minimum credit rating threshold in the collateral eligibility requirements for the purposes of the Eurosystem's credit operations in the case of marketable debt instruments issued or guaranteed by the Greek government"

(ECB, 2010) and that ECB should continue to accept Greek government bonds until further notice.

Following deepening economic recession and delays in the implementation of the agreed austerity measures, the need for second rescue for Greece became apparent. On March 14, 2012, the Euro area finance ministers approved financing of a Second Economic Adjustment Programme for the country. This would include the Euro Area Member States and the IMF committing the undisbursed amounts of the first economic adjustment programme plus an additional €130 billion (including a bank recapitalisation of €48bn) for the years 2012-14. Under the arrangement, the country's private creditors were required to accept extended maturities on their bond holdings, lower interest rates, and a 53.5% face values loss (haircut). A total of €240bn was to be transferred at regular tranches through the period of May 2012 to December 2014. The implementation of the programme contributed to an improved outlook for the Greek economy, with the achievement of a government structural surplus both in 2013 and 2014, along with a noticeable decline in the unemployment rate and return of positive economic growth in 2014, the Greek government re-gained access to the private lending market through the sale of bonds to private creditors to fully finance its 2014 gap.

Increasing dissatisfaction of Greeks with the terms of the bailout dictated by the Trioka saw the election of an anti-austerity party following a snap election. Following the formation of the new government, the terms of the bailout agreement were not adhered to, resulting in the suspension of all outstanding disbursements to Greece under the program subject to the Greek government either accepting the previously conditional payment terms or alternately renegotiating new terms. This rift caused a renewed and increasingly growing liquidity crisis (both for the Greek government and the Greek financial system), resulting in plummeting stock prices at the Athens Stock Exchange, while interest rate for the Greek government at the private lending market spiked, limiting access to the private creditors as an alternative funding source.

Faced by the threat of a sovereign default, some final attempts for reaching a renegotiated bailout agreement were made by the Greek government in June 2015. Despite these attempts, Greece subsequently defaulted on a \$1.7bn IMF payment which was due on June 29, 2015, becoming the first developed country to default on its obligations to the IMF. The default resulted in the introduction of necessary capital controls to avoid collapse of the banking sector. At this point fears of an imminent exit (GREXIT) from the Eurozone heightened due to growing liquidity constraints on the ability to continue payments of public pension and salaries.

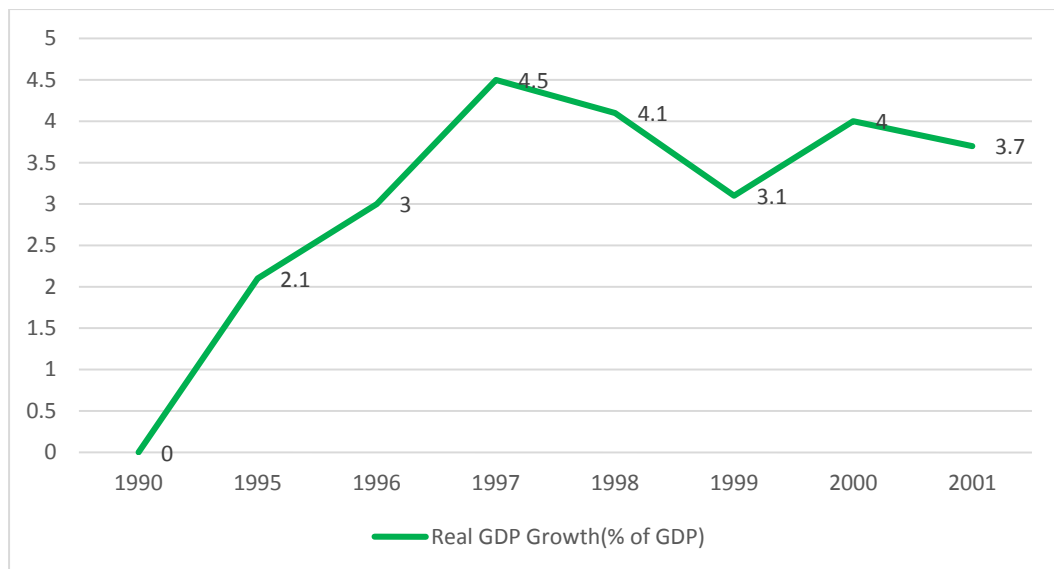
3.0 THE EVOLUTION OF THE CRISIS

3.1 The Greek economy prior to ascension the European Union (1990-2000)

Several views exist concerning the origin of the Greek debt crisis. Many believe that the structural challenges that made Greece vulnerable to the financial crises originated from performance and developments in the Greek economy a decade before the crisis. Indeed, the Greek economy in the 1990s was

characterized by macroeconomic imbalances and structural problems. The economy was characterized by low real growth (with 3.06% average growth rate), double digit-inflation, large fiscal and external imbalances, as depicted in Figure 1 and Table 1 below.

Figure 1: Real GDP Growth Rate- Greece (1999-2001)



To address the problems of macroeconomic imbalances, the government embarked on a medium term adjustment program in the late 1990s. The goals of the programme were to: reverse years of fiscal laxness, roll back the public sector, eliminate pervasive market distortions and fully integrate Greece into the European Community. From a deficit of 14.2 percent of GDP, at the turn of the 1990s, Greece managed to reduce its net borrowing to below 10.0 percent. The budget deficit declined from 9.1 percent in 1995 to 3.1 percent in 1999 allowing Greece to enter the EMU in 2001. However, both public and external debt increased during the period.

Table 1: Selected economic Indicators of Greek economy- Period prior to Greece's Ascension to the Euro (1990-2001)

	1990	1995	1996	1997	1998	1999	2000	2001
Public revenue (% of GDP)	31	37	37.8	39.3	40.9	41.8	43.4	41.3
Public expenditure (% of GDP)	45.2	46.2	44.5	45.3	44.7	44.8	47.1	45.8
Budget balanced (% of GDP)	-14.2	-9.1	-6.7	-5.9	-3.9	-3.1	-3.7	-4.5
Structural balance	-14.9	-9.4	-6.9	-6.3	-4.4	-3.6	-4.2	-4.9
Nominal GDP growth	20.7	12.1	10.8	10.9	9.5	6.8	5.6	7.2
GDP price deflator (%)	20.7	9.8	7.7	6.2	5.2	3.6	1.6	3.4
Real GDP growth (%)	0	2.1	3	4.5	4.1	3.1	4	3.7
Public debt (billion €)	31.2	87	98	105.4	112.1	118.8	141.2	152.1
Debt-to-GDP ratio (%)	68.3	93.1	94.7	91.8	89.2	88.5	99.6	100.1

Public debt increased from a low level of 31.2 percent of GDP in 1990 to a high level of 152.1 percent of GDP in 2001. The rise in general public debt during this period was attributable to large primary deficits and huge interest payments on government debt, as real interest rate increased due to financial liberalization. During the period, real GDP growth was increased from (2.1 percent in 1995 to 3.7 in 2001) but was very slow, averaging 3.6 percent

between 1995 and 2001 as a result of the depreciation of the domestic currency, economic uncertainty, speculation and negative real interest rates, among others. High inflation kept interest rates very high, putting additional burden on government finances through the high cost of debt repayments. Since the late 1990s, inflation rate had been on the declining trend, decelerating from 8.9 percent in 1995 to 2.6 percent in 1999 (see Table 1 above).

3.2 Greece in the European Monetary Union before the Crisis (2001-2008)

The entry of Greece into the euro area in 2001, led to a shift in the country's economic performance. The economy returned to financial stability and growth and major efforts were made to institute structural reforms. Initially, policies were driven by the requirements of the European Monetary Union (EMU) participation and deeper integration with the EU. A bold stabilization program, building on earlier progress, resulted in the cumulative reduction of inflation by 10 percentage points during 2000-2009 and of the fiscal deficit by 14 percentage points of GDP. Linking the adjustment programme with EMU participation, added credibility to the disinflation effort and helped prevent output losses. However, some adjustment fatigue could not be avoided as the unemployment rate ratcheted up. Growth accelerated to 4 percent

benefiting from the restoration of price stability, privatization, and liberalization of several sectors of the economy.

Unfortunately, the Greek governments of the period 2001-2009 did not take advantage of the low inflation environment and they ran fiscal deficits of 6 percent of GDP on the average, while they also increased the share of the government spending in the economy (Antzoulatos, 2011).

On the road to the euro, the government implemented a revenue-led fiscal consolidation programme that cut the deficit by nearly 2.5 percentage points of GDP. However, fiscal consolidation came to a halt in 2000 and during the period 2000-2004, fiscal policy became expansionary. This was reflected in the downward trend of the cyclically-adjusted

general government primary surplus, which turned into a deficit in 2003, reaching a peak of 7.5 percent of GDP in 2004. With the current account deficit remaining high, the fiscal stance became restrictive again in 2005. The government implemented a significant fiscal adjustment programme that cut the budget deficit to 2.8 percent in 2006. In 2007 the fiscal stance eased mainly on account of current primary expenditure slippages. The structural balance deteriorated by 0.3 percentage point of GDP. The fiscal deterioration continued also in 2008, with the deficit reaching 5.0 percent of GDP. Over the period 2000-2007, Greece's real GDP expanded at an average annual rate of 4.2 percent, compared to 1.9 percent in the Euro

zone, while the unemployment rate declined by 2.9 percentage points to 8.3 percent in 2007. Greece's economic expansion over the period was driven by a rapid increase in domestic demand supported by expansionary fiscal policy, and expansion of credit to households and private businesses at average annual rates of 29.6 percent and 14.8 percent, respectively. The country's current account deficit remained high over the period 2000-2004 and deteriorated further from 2005 onwards, reaching 14.2 percent of the country's GDP in 2007. The evolution of Greece's external deficit reflects strong imbalances in the trade accounts, as well as a rapid deterioration of the incomes' balance.

Table 2: Selected economic Indicators of Greek economy- (2001-2011)

Selected Indicators	2000	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
Public revenue (% of GDP)	43.4	40.6	39.4	38.4	39	38.7	40.2	40.6	38.7	41.1	43.8
Public expenditure (% of GDP)	47.1	45.5	45.1	46	44.4	44.9	46.9	50.6	54	52.2	54
Budget balanced (% of GDP)	-3.7	-4.9	-5.7	-7.6	-5.5	-6.1	-6.7	-9.9	-15.3	-11.1	-10.2
Structural balance	-4.2	-4.5	-5.7	-7.7	-5.2	-7.4	-7.8	-9.7	-14.7	-9.8	-6.3
Nominal GDP growth	5.6	6.8	10	8.1	3.2	9.4	6.9	4	-1.9	-4.7	-8.2
GDP price deflator (%)	1.6	3.5	3.2	3	2.3	3.4	3.2	4.4	2.6	0.8	0.8
Real GDP growth (%)	4	3.2	6.6	5	0.9	5.8	3.5	-0.4	-4.4	-5.4	-8.9
Public debt (billion €)	141.2	159.5	168.3	183.5	212.8	225.3	240	264.6	301	330.3	356
Nominal GDP (billion €)	141.7	162.3	178.6	193	199.2	217.8	232.8	242.1	237.4	226.2	207.8
Debt-to-GDP ratio (%)	99.6	98.3	94.2	95.1	106.9	103.4	103.1	109.3	126.8	146	171.4

Source: Eurostat and European Commission

In the years leading up to the eruption of the Greek sovereign-debt crisis in 2009, unsustainable fiscal and external imbalances were building. Greece's fiscal deficit increased from 4.5 per cent of GDP in 2001 to 15.3 per cent of GDP in 2009 mainly driven by expenditure. As the share of government spending in GDP rose about 9 percentage points, to 54 per cent. Within the period also the ratio of government debt to GDP rose from

103.7 per cent in 2001 to 129.7 per cent in 2009. The competitiveness of Greece as measured in terms of the country's unit labor costs against those of its main trading partners, deteriorated by about 30 per cent over the period 2001 to 2009. The current account deficit rose from 11.5 per cent of GDP in 2001 to a peak of 18.0 per cent of GDP in 2008, before declining to 14.4 per cent in 2009.

Figure 2: Budget Deficit (% of GDP) and Debt-to-GDP Ratio of Greek economy- (2001-2011)

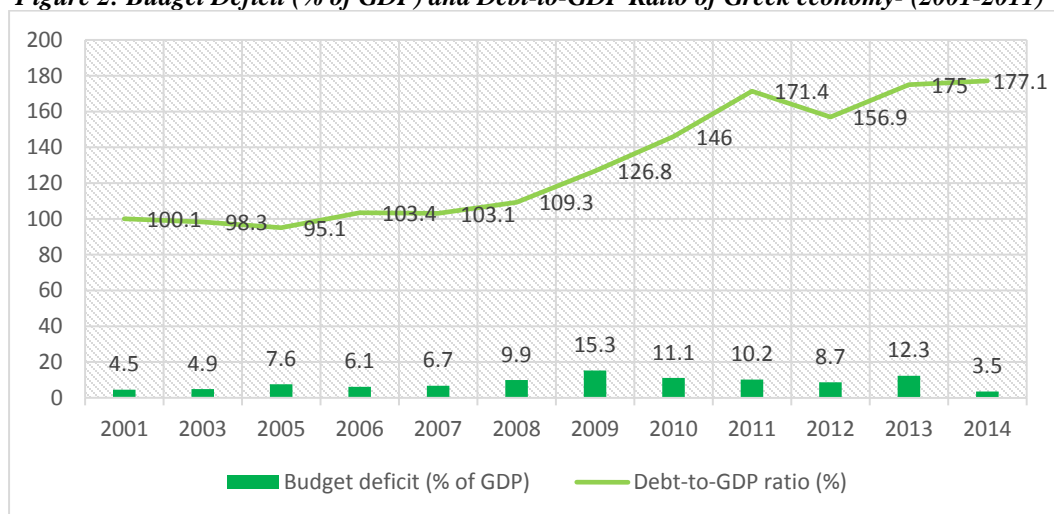
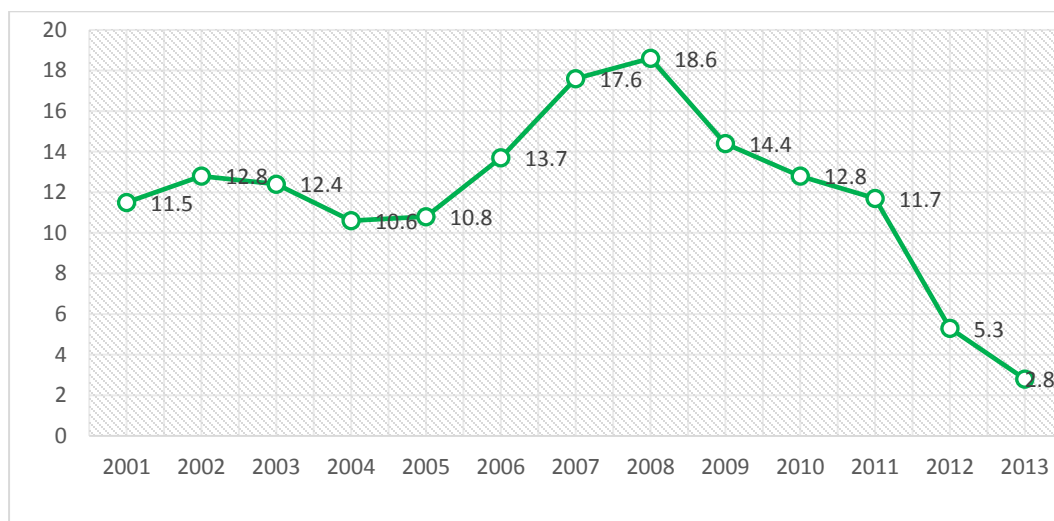


Figure 3: Current Account Deficit (% of GDP) - (2001-2013)



SOURCES: ELSTAT (Hellenic Statistical Authority) and Bank of Greece

4.0 ANALYSIS OF THE CAUSES OF THE CRISIS

From the above discussions, one could categorize the causes of the Greek debt crisis into: country-specific factors, European Monetary Union (EMU)-related factors and global economic factors.

4.1 Country-Specific Factors

Analysis of the evolution of the crisis reveals that the remote cause and the escalation of the crisis can be principally attributed to the steady deterioration in macroeconomic fundamentals over the period 2001-2009 to levels which were inconsistent with long-term EMU participation.

Macroeconomic Imbalances: The deterioration in the Greek macroeconomic fundamentals began over ten years prior to the crisis as a result of inconsistent domestic policies and programmes pursued by the authorities. The growth in the economy largely driven by the service sector were financed by persistent borrowing by the government. It can be observed from the tables and figures above that in the years leading up to the eruption of the Greek sovereign-debt crisis in 2009, unsustainable fiscal and external imbalances were building. For instance, Greece's fiscal deficit increased from 4.4 per cent of GDP in 2001 to 15.6 per cent of GDP in 2009.

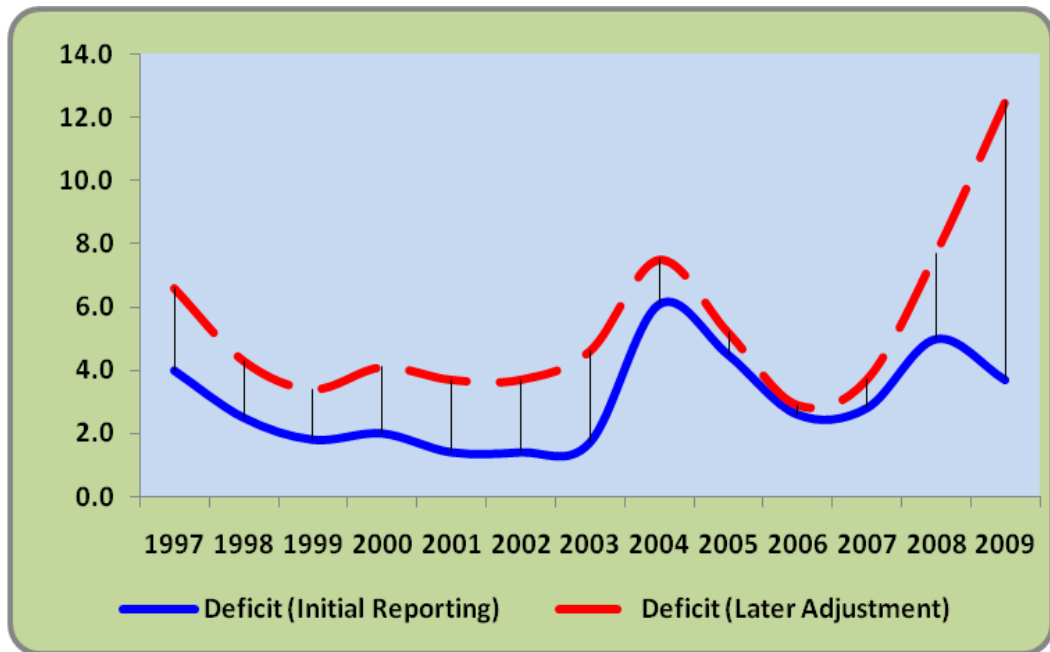
The widening of the fiscal deficit was mainly expenditure driven. The share of government spending in GDP rose about 9 percentage points, to 54 per cent. The ratio of government debt to GDP rose from 103.7 per cent in 2001 to 129.7 per cent in 2009. The current account deficit rose from 11.5 per cent of GDP in 2001 to a peak of 18.0 per cent of GDP in 2008, before declining to 14.4 per cent in 2009.

The macroeconomic imbalances resulted from several factors including generous pension schemes and increased ageing population culminated in substantial pension and social security payments. Unemployment and vulnerability allowances, free health care schemes and family allowances all continued to put pressure on the budget.

Statistical Misreporting: Another factor that has compounded the debt-crisis was the waning credibility brought about by its misreporting of debt and fiscal deficit data. For instance, on October 2, and 22, 2009, the Greek authorities transmitted two different sets of complete Excessive Deficit Procedure (EDP) notification tables to Eurostat covering the government deficit and debt data for 2005 – 2008 and a forecast for 2009. The latter notification adjusted the fiscal deficit figures for 2008 and 2009 upwards from 5.0 to 7.7 percent of GDP and 3.7 to 12.5 percent of GDP, respectively.

Earlier, in September 2004, Eurostat had to carry out upward revision of Greece's EDP notifications for the period 2000 – 2003. There was also a subsequent revision of fiscal deficit and debt data from 1997 – 1999 (Eurostat, 2004; European Commission, 2010). These Eurostat revisions and later Greece's own revisions of the deficit figures are presented in Figure 4 below.

Figure 4: Discrepancies in Greek Deficit Figures, 1997 - 2009



Source: Eurostat (2004) and European Commission (2010)

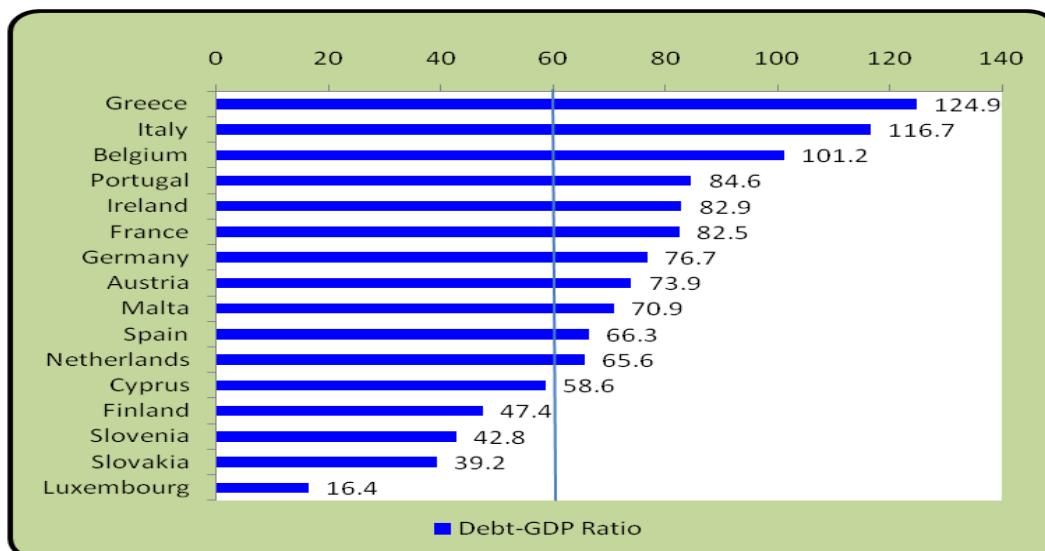
4.2 EMU-Related Factors

The low Interest Rate Policies Pursued by the European Central Bank

The heavy debt burden of Greece and, indeed of most Euro-zone countries, is partially attributable to the monetary policy of the European Central Bank (ECB). It is argued that, in the early part of the millennium, the ECB kept interest rates lower than what they should have been in order to accommodate the export-

driven industrial North of the Euro Zone. This sub-optimal interest rate created lax monetary conditions and induced countries south of the Euro Zone, especially Portugal, Ireland, Italy, Greece and Spain (PIIGS) to borrow excessively from the market to finance their budgets. See Figure 5 for the levels of national debts within the Euro Zone in 2010.

Figure 5: National Debts (as Percentages of GDP Forecasts) of the Euro Zone Members in 2010



Source: European Commission

Abuse of Credibility of the EMU by countries with previously weak economic fundamentals:

The adoption of the euro also gave benefits to countries like Greece with historical high levels of inflation and limited economic credibility. Thus, the introduction of the euro and the monetary policies pursued by the ECB led to reduction in inflation and inflation expectations in countries with high inflation experience, reducing uncertainty (Kouretas G.P, 2015). The adoption of the euro also led to reduction in exchange rate uncertainty to the benefits of countries which in the past has had episode of exchange rate volatility. The low inflation environment, reduction in exchange rate uncertainty and the related reduction in interest rates led to increased borrowing and lending at longer horizons.

ECB Policies led to mispricing of Risks of Greek Bonds by the Market:

Furthermore, the reduction in nominal interest rate impacted on risk premia and cost of servicing debts for most member countries.

During the period prior to the entry of Greece in the EMU, the interest rate spreads between the 10-year Greek bond and 10-year German bonds were reduced drastically from 1,100 basis points in early 1998 to about 100 basis points one year before the entry. Following the entry in the EMU, the spreads fell to 50 basis points and during the period 2002 until late 2007, the spreads fell even further ranging from 10 to 30 basis points.

Rigid exchange rate mechanism within the EMU inconsistent with individual member countries' competitiveness aspirations.

Non-competitiveness of Euro-zone countries has been attributed to the appreciation of the Euro from less than US\$1.00 to over US\$1.50 since 2003. Thus, Euro-zone countries, notably the PIIGS³, who lost control over the value of their currency as a result of their accession to EMU, found themselves in a straitjacket (Kenneth Matziorinis, 2010). Largely, the exchange rate mechanism within the EMU appeared too rigid and inconsistent with

³ Portugal, Ireland, Italy, Greece and Spain

individual member countries' competitiveness aspirations.

Lack of effective fiscal policy supervision mechanism in EMU

The debt problem of Greece was exacerbated by the EMU's inability to put in place effective fiscal policy supervision mechanism. It fails to monitor member countries on the tenets of the Maastricht Treaty *ex-post* the formation of the Union. While it was strict on adherence to the convergence criteria *ex-ante* the introduction of the Euro, the EMU appeared to have relaxed the conditions *ex-post*, giving rise to 11 out of the 16 Euro-zone countries exceeding, by substantial margins, the Maastricht Treaty's limit on the debt-GDP ratios. Indeed, the 2010 national-debt forecasts for the entire Euro Zone put the average debt-GDP ratio at 84.0 percent, as against the limit of not-more-than 60.0 percent.

Slow Response of Euro zone to the Crisis

The initial hesitant stand by the euro zone towards bailout for Greece escalated the crisis. This was born out of dilemma created by the crisis for the zone. There was confusion largely driven by domestic politics in Germany and other EU members regarding how the Euro Zone would handle the crisis. The bail out of

Greece was considered by some members of EMU to be creating a moral hazard situation where member states will engage in debt accumulation spree with the view that they will be bailed out. It was argued that it is unfair for profligate states to create heavy debt burden only for fiscally disciplined ones to be called upon to pay for their profligacy. Others held a contrary view that sticking to the no bail-out clause will spell doom for the entire zone and may put the EMU in jeopardy with the likelihood of a break-up. After a prolonged hesitancy, the Euro-zone members moved away from the no bail-out clause and taken decision to assist Greece.

These initial confusions about a bail-out plan for Greece accentuated the shift in market expectations about Greek EMU membership, from a regime of credible commitment to future EMU participation under an implicit EMU guarantee for Greek fiscal liabilities, to a regime of non-credible commitment to EMU participation without fiscal guarantees (Arghyrou and Tsoukalas, 2010). Thus, the market was expecting Greece to exit the EMU or be expelled from the Union. This created a crisis of confidence for the authorities' ability to service its public debt.

4.3 Global Factors

The credit crunch of 2008-2009

The credit crunch of 2008-2009 and its associated global economic downturn also worsened the deteriorating macroeconomic fundamentals in Greece. Though the stress tests conducted by the Bank of Greece (BoG) and IMF staff during the first-half of 2009 suggested that the Greek banking system had enough buffers to weather the financial crisis and its related economic downturn (IMF, 2009), the credit crunch did impact the Greek economy negatively. The shipping and tourism industries were adversely affected with revenues falling by 15.0 percent in 2009. Consequently, the authorities had to borrow

more money to finance their budget and shore-up the financial system.

The fiscal stimulus packages designed to contain the global financial crisis led to accumulation of debt by most developed economies. The fiscal deficits of the 30-member Organization for Economic Cooperation and Development (OECD) increased sevenfold since 2007 to about US\$3.4 trillion in 2009. Their total debt increased to about US\$43 trillion. The national deficits in the Euro Zone grew within the same period 12-fold with accumulated debt reaching US\$7.7 trillion (Der Spiegel, 2010). Thus, the US mortgage

subprime bubble degenerated into a debt bubble on the verge of busting in Greece.

The effects of Greek Bonds Downgrade

The Greek crises escalated further following the downgrading of the government debt by credit rating agencies including Fitch, S&P and Moody as credit default swaps (CDS) rose. On December 8, 2009, Fitch cut Greece's ratings from A- to BBB+ and placed

the government debt on a negative watch. S&P followed on December 16, 2009 by cutting Greece's rating from A- to BBB+. On December 22, 2009, Moody came out with its rating of Greek debt from A1 to A2. On April 27, 2010, S&P further downgraded the Greek bonds from investment rating to junk bond status. All these pieces of "bad news" sent negative signals to the market and thereby worsened the crisis.

5.0 IMPLICATIONS OF THE GREEK DEBT CRISIS

5.1 Implications for the Euro Zone

Though the Greek economy accounts for less than 4.0 percent of the Euro-zone economy and its debt, is far less than what was used to bail-out the multinational companies in the US (Kenneth Matziorinis, 2010), the crisis in Greece has implications first for the Euro Zone and secondly for the global financial system. To some observers, the Greek debt crisis is similar to that of the Lehman Brothers, given its potential to generate rippling effects throughout the Euro Zone that could bring the entire global financial superstructure to its knees. The bonds of the rest of the PIIGS were downgraded and there were fears that Greece's insolvency will be contagion throughout the Euro Zone.

The Greek debt crisis, if allowed to escalate and spread across the Euro Zone, will be transformed into a banking crisis given the high exposure of European financial institutions in Greece and the other PIIGS. Data from the

Bank for International Settlements (BIS) show that in 2009 French-based banks held US\$75 billion of exposure in Greek debt, while German banks held US\$45 billion (Evans-Pritchard, 2010). UK holdings of Greek debt stood at about US\$14.4 billion, while Greek investors held about a third of the Greek Government debt. Thus, a debt default on the part of Greece will have financial implications throughout Europe.

The debt crisis also has potential implications for the stability of the exchange rate of the euro and its use as reserve currency. Since the beginning of the crisis, the euro has depreciated substantially against the US dollar and other major currencies. The long-term objective of making the euro the world's second reserve currency after the US dollar will be increasingly untenable.

5.2 Implications for the Global Economy

Indeed, if the crisis is not contained, it has the potential of sending signals to the market for bond holders to start paying attention to other countries such as Japan, the UK and the USA, with high debt levels. If Greece exits the Eurozone, thereby creating a banking crisis in Europe, the global financial system will crash once again. Significant financial losses for the Eurozone countries and the IMF will be involved, which are owed the vast majority of Greece's debt. It will also impact on the IMF and the credibility of its austerity strategy, which has contributed to the Greek depression. Thus, the modest and steady recovery that the

global economy has enjoyed since 2009 could be interrupted.

In 2015, five years after the crisis began in 2010, most international banks and foreign investors have sold their Greek bonds and other holdings, were no longer vulnerable to what happens in Greece (some investors who subsequently ploughed back into Greek bonds, betting on a come-back, regret that decision). Also, the other debt crisis countries in the Eurozone like Portugal, Ireland and Spain, had taken steps to overhaul their economies and were now much less vulnerable to market contagion than they were a few years ago.

5.3 Implications for Monetary Unions in the Making

If the Greek crisis is not managed well, leading to the crashing of the EMU, it could send a wrong signal to other proposed monetary unions in the various regions that monetary union cannot work. The main argument will be that if the EMU with its level of sophistication,

technology and advancement could fail, then it is not likely that other regions with comparatively less sophistication can succeed in their quest for monetary and economic integration.

5.4 Implications for Greece Exiting the European Union

Some schools of thought believe that if Greece were to leave the currency union, in what is known as a “Grexit”, it wouldn’t be such a catastrophe. Europe has put up safeguards to limit the so-called financial contagion, in an effort to keep the problems from spreading to other countries. Others contend that Greece, just a tiny part of the Eurozone economy, could regain financial autonomy by leaving and reintroducing the drachma under a flexible exchange rate regime.

History shows that while leaving the Euro area and defaulting would have disastrous

implications for Greece and Euro area, it may become the best of bad options if Greece does not receive adequate support from the EU (U. Dadash and B. Stancil, 2010).

However, despite the frustration of endless negotiations, European political leaders see a united Europe as an imperative. At the same time, they still haven’t fixed some of the biggest shortcomings of the Eurozone’s structure, such as a federal-style fiscal arrangement (fiscal union).

6.0 EFFORTS TO CONTAIN THE CRISIS

The foregoing implications of the Greek debt crisis call for urgent measures to contain the crisis. Efforts made so far to contain the crisis are in five-folds. These are the Greek

Government austerity measures, Euro-zone initiatives and the IMF support, peripheral economies' austerity measures, and new financial market regulations.

6.1 Greek Government austerity measures

Faced with escalating cost of borrowing in the late 2009 and the beginning of 2010 the Greek government designed and adopted a fiscal consolidation programme named "The Greek Stability and Growth Programme", in order to reduce the public debt and provide the framework to improve stability and growth to the economy. This document was submitted to the European Commission on January 15, 2010. On the revenue side, the focus was on (i) measures to reduce tax evasion and improve tax collection (ii) reduction of social contribution evasion (iii) a special levy on profitable companies (iv) acceleration of EU receipts for the public investment programme and (v) increase on several types of indirect taxes. The following measures were also taken on government expenditures (i) a 10% cut in general government expenditure on salary allowances (ii) a recruitment freeze in the public sector for 2010 (iii) implementation of a 5:1 retirement/recruitment ratio for public sector employees from 2011 onwards. (iv)

reduction in the budget item linked to social security and pension funds by 10% and (v) other relevant measures to drastically reduce government expenditures in most public services (Kouretas G. P. and Vlamis P., 2010) Prior to the 2015 bail-out, the Greek government rolled out some austerity measures to bolster market confidence in the Greek monetary and financial regime to assure other EMU members that they were committed to the viability and sustainability of the Euro Zone. Greece needed to carry out reforms that would halt the deterioration of the country's macroeconomic fundamentals. A new austerity package emerged from the agreement of Greece with the Eurozone in 2015, for a new 86 billion euros bailout over three years:

1. Transfer of many services and products from the low to the high rate VAT (23%). Corporation tax rise from 26% to 29% for small companies
2. End to early retirement by 2022 and a retirement age increase to 67.

6.2 Euro-Zone/ IMF Bail-Out Scheme

The initial hesitant stand by the Euro Zone towards bail-out for Greece might have arisen largely from the dilemma created by the crisis for the zone. First, bailing out Greece is thought to be creating a moral hazard situation where member states will engage in debt accumulation spree with the view that they will be bailed out. It is argued that it would be unfair for profligate states to create heavy debt burden only for fiscally disciplined ones to be called upon to pay for their profligacy. However, sticking to the no bail-out clause would have been more damaging for the entire zone and may put the EMU at risk of a break-up. Hence, after

prolonged hesitancy, the Euro-zone members have moved away from the "no bail-out" clause and taken decision to assist Greece.

The Zone in conjunction with the IMF agreed on €110 billion bail-out package over three years. The EU member states provided €80 billion in loans with Germany contributing €22 billion over the three years (Der Spiegel Staff, 2010). This was essentially an extension of the European Commission (EC) Balance of Payments (BOP) lending facility by €60 billion, from its limit of €50 billion to €110 billion. €10 billion of this facility had already been used to

provide assistance to Hungary, Latvia and Romania. For this facility to be used to support euro area countries in the presence of the "no bail-out" clause, the European leaders evoked Article 122.2 of the Lisbon Treaty which requires qualified majority voting and states that a country can be granted assistance by other countries when it "is in difficulties or is seriously threatened with severe difficulties caused by natural disasters or exceptional occurrences beyond its control". Since this did not require national parliaments to vote, it could be activated quickly on request (Stocknews.ch, 19/05/10).

However, these measures did not convince the market players as the euro continued to depreciate. On May 10, 2010, the Euro-zone leaders agreed on a €750 billion stabilisation plan (including the BOP lending facility of €110 billion) to support the purchase of Euro-zone government bonds in order to shore-up confidence in the euro. The package comprised €440 billion contribution from Euro-zone

countries and €250 billion from the IMF (Barber, 2010).

The Euro-zone contributions of €440 billion were euro-area government-backed loan guarantees. As far as these will require parliamentary approval or new legislations, they were not immediately available for disbursement (Stocknews.ch, 19/05/10). However, the adequacy of the stabilisation package was in doubt. This was because the 2010 gross deficit-financing needs of the PIIGS stood at €450 billion. Further, medium-term financing needs of four of the PIIGS, Spain, Greece, Portugal and Ireland were estimated at €448 billion, €158 billion, €70 billion and €69 billion respectively (Barber, 2010). The total financing needs of the entire Euro Zone in 2010 was estimated at €1.6 trillion. Considering the entire financing needs of the Euro Zone in 2010, however, the market doubted the adequacy of the stabilisation package, prompting further depreciation of the euro.

6.3 The ECB's Monetary Management Efforts

To bolster investor confidence, the ECB purchased €16.5 billion worth of bonds as part of the international rescue plan (Oakley and Garnham, 2010). There were concerns, however, about sovereign bond purchases as this was considered monetisation of government debts which will spark inflationary spiral over the medium term. The ECB maintained that it was keeping to its core mandate of price stability as it hoped to sterilise its bond purchases with market interventions to restrict the money supply. It was, therefore, speculated that the ECB will start raising interest rates (Barber, 2010) at some point in the medium term.

The ECB also sought to address the severe tensions in certain market segments which were hampering the monetary policy transmission mechanism and, hence, the effective conduct of monetary policy. The Governing Council had

agreed on purchases of public and private sector securities under a Securities Markets Programme (SMP) in order to ensure depth and liquidity in those market segments which are dysfunctional. In order to sterilise the impact of the above interventions, the Governing Council recommended the following specific operations:

- ✓ To conduct long-term refinancing operations (LTROs) comprising 6 million LTROs with full allotment on May 12, 2010 and 3 million LTROs at fixed-rate tender with full allotment on May 26, 2010 and on June 30, 2010; and
- ✓ To reactivate the temporary liquidity swap lines with the Federal Reserve Bank of America and to resume US dollar liquidity providing operations at 7 and 84 day terms at fixed rate tenders with full allotment (Stocknews.ch, 19/05/10).

6.4 The Peripheral Economies' (PIIGS') Austerity Measures

To send a strong signal to the market that Eurozone is committed to tackling the problem, other debt-ridden countries of PIIGS character have made efforts to reduce their budget deficits by increasing taxes and downsizing expenditures. However, five years after the crisis began in 2010, most international banks and foreign investors have sold their Greek bonds and other holdings, so they no longer are

vulnerable to what happens in Greece (some investors who subsequently ploughed back into Greek bonds, betting on a come-back, regret that decision). Also, the crisis countries in the Eurozone like Portugal, Ireland and Spain, have taken steps to overhaul their economies and are much less vulnerable to market contagion than they were a few years ago.

7.0 LESSONS FOR THE ECOWAS SINGLE CURRENCY PROJECT

- i. **Continuous Adherence to Convergence Criteria Post Accession:** A major pitfall that contributed to the crisis in Greece was a seemingly lax fiscal stance after admittance to the European Monetary Union in 2001. Public debt to GDP ratio assumed a phenomenal height from 2005 and the trend continued unabated up to 2014 contrary to the declining trend in the pre accession era. As a result, WAMZ countries should ensure that they adhere strictly to the various convergence criteria even after the Monetary Integration. Towards this, the multilateral surveillance on various countries must be improved upon and possibly relevant legislations to strengthen the process should be enacted in various countries.
- ii. **Zero Tolerance to Wrong Statistical Data:** The issue of revision of statistical data particularly when such data had been used for policy purpose should carry a heavy sanction. Under reporting of fiscal data was part of the key factors that caused excessive growth of public debt in Greece. Since Greece's entry to the euro area in 2001, Greek fiscal data have been subjected to a number of revisions, sometimes several years after the initial (real-time) release of the data. These revisions have often involved upward revisions of the fiscal imbalances, generating negative surprises. As a result, all WAMZ countries should strengthen the institutions responsible for producing official statistics in terms of both soft and hard infrastructures. Revisions of previously released statistics, where necessary, should not be unilaterally undertaken by a particular country but should be brought to the attention of the convergence council.
- iii. **Continuous Review of Convergence Criteria:** Most monetary unions are formed based on stipulated convergence criteria. Empirical evidence has not clearly shown that the requirements of the criteria were deficient in terms of forming and sustaining a monetary union but the experience of Greece and the entire Euro zone is, in the least, suggesting the need for some fine-tuning. A classical case in this regard is the debt to GDP ratio. Greece entered the euro area with a debt to GDP ratio of about 100 per cent. By 2006 that ratio had risen to about 110 per cent and remained there until 2009. The sustainability of the debt-to-GDP ratio was due to robust real GDP growth rates; between 2001 and 2007 real GDP grew at an average rate of almost 4 per cent. Real growth moved into negative territory from the later part of 2008, leading to a sharp upward jump in the debt to GDP ratio in 2009 and the debt dynamics became unsustainable. This clearly shows that the ratio of debt to GDP should always be treated with caution. The absolute amount of debt should equally be accorded some recognition while sectors that experience high degree of volatility could be discounted from GDP.
- iv. **Criteria for Public Borrowing should be defined based on each country's Fundamental:** It is not uncommon that different countries forming a monetary union are not on the same economic pedestal. Integration into the Euro Zone gave Greece a false sense of security, though it was not in the same league as Germany or France, economically. The euro zone membership however gave Greece easy access to cheap debts which fueled its excessive fiscal expenditures. To avert similar challenge in the proposed EMCP, the debt criteria for each country must be designed in consonance with its economic fundamentals to obviate the possibility of a country free-riding on the goodwill of other members of the union.

- v. **Strong Think Tank and Research Arm:** The proposed EMI should have a strong think tank and research arm staffed by competent researchers in various areas of financial markets. This recommendation is underpinned by the fact that most policies in respect of monetary integration in Africa derive strength from research conducted in western economies. The WAMZ/ECOWAS convergence criteria, for example, borrowed considerably from OCA and the Maastricht Treaty of the European Union. African Governments, policy makers, central bankers need to assess impact of global capital / liquidity standards (e.g. Basel 3) on their own economies and justify amendments modifications as required, whilst improving their influence in global policy making.
- vi. **Prudent Management of Resources Even During Periods of Economic Boom:** The debt crisis was a precipitation of nearly a decade of underlying fiscal deficits by Greece particularly when GDP was heading upward. This was funded by cheap borrowings and often masked by short lived surge in tax collections and asset bubbles. The problem has shown that there is no alternative to austerity during times of plenty in order to build fiscal buffers in anticipation of periods of dwindling revenue. Toward this, it may be advisable for all countries in WAMZ particularly natural resources based economies to take cue from countries like Norway by instituting fiscal buffer like Sovereign Wealth Fund.
- vii. **Cautious Approach to Rating Agencies:** The less than credible roles of rating agencies was once again revealed by the crisis. The risk rating agencies continued to classify Greek sovereign debt as investment grade not long before declaring it as risky and pushing up borrowing costs for Greece. Similar issue was observed prior to the global financial crisis of 2007/8. WAMZ countries in collaboration with the global community should therefore devise effective supervision of the work carried out by rating agencies. Policy measures to improve independence in terms of shareholdings and corporate governance aspects merits attention.
- viii. **Design of the ECOWAS Single Currency Project:** Analysis of the Greek crises reveal some fundamental lessons about the conceptual design of a monetary union. One issue that usually comes up in the design of a monetary union is whether all prospective members should satisfy and sustain the Convergence Criteria at a point or before the launch of a monetary union as well as whether the criteria should be ex-post. Indeed, the European Union were not OCA before the commencement of the monetary union. And this is often cited to support the meeting of OCA criteria ex-post relating to on-going monetary union projects like the ECOWAS single currency project. Various options for the actualization of monetary union and a single currency in the ECOWAS have been suggested. These include holding up until OCA, the Quick Fix/ Big Bang Approach, the Critical Mass Approach, other WAMZ countries joining the West African Economic and Monetary Union (UEMOA), and the Realistic Gradualism Approach. The Greek debt crisis provides very practical guidance concerning the appropriate single currency approach for ECOWAS. The crisis highlights the need for all member countries to meet the critical convergence criteria before joining the monetary union. Despite the fact that progress towards macroeconomic convergence has been challenging for both UEMOA and the WAMZ member countries (in both fast-track and double-track approaches in the past), ECOWAS should strive to meet the critical convergence criteria *ex ante* (before the commencement of the

monetary union) and to sustain the benchmarks for a number of years.

ix. The Need for Contingency Plan

/Stabilization Fund Two main policy gaps in the formation of the euro area that have resulted in its current state of instability is the absence of a contingency plan or safety measures to deal with sovereign debt crises. The Euro zone did not have protocol for member states should they find it difficult to access markets to refinance sovereign debts.

Indeed, for an effective functioning of a monetary union in ECOWAS, there is the need to ensure that the Stabilization and Cooperation Fund (SCF) has the scope and capacity to deal with short term imbalances swiftly before they result in crisis. The time it took Euro area to agree on the one trillion-dollar stabilization fund for the zone was a time lost to the speculators. It is therefore important to have a solid stabilization fund arrangement that will serve as a crisis mitigation framework. Furthermore, there is the need for the development of a bond market and the general development of the financial sector, to free the central and commercial banks from the burden of financing government. Also, there is the need to build up adequate revenue base through the diversification of the economy; expansion of the tax base, tax administration reforms as evident from the Greek experience.

x. Institutional Design of the Central Bank: It is important for ECOWAS to consider the institutional deficiencies of

the ECB in order to avoid falling into the same trap that the ECB is currently in. A crucial gap in the euro area is what to do when there is a run on government bonds since the ECB did not have a mandate to intervene. Also, crisis management facility, such as an enhanced European Monetary Fund was not available to address the problem. These highlight the importance of an independent central bank for the region that will guide monetary policy formulation and implementation. Furthermore, the central bank must enforce prudential financial regulations for the financial sector of member countries. The Greek fiscal crisis, spilled over to the banking sector, for which there is no central supervision or a central or federal deposit insurance mechanism.

xi. Reasonable Degree of Sovereignty to enhance Political Will:

The formation of the monetary union is a challenge given the great differing individual national economic strengths of the ECOWAS countries. The ideal integration situation is where the countries in the union share common monetary and fiscal policies, a common pool of foreign exchange reserves, and a common monetary authority or central bank. Otherwise, trying to operate a single currency without a degree of social, economic and political integration is likely to falter as evidenced by Euro zone crisis. Thus, the formation of a monetary union should be supported by strong political will for deeper integration from governments of member countries.

8.0 CONCLUSION

The study examined the Greece debt crisis by bringing into sharp focus the genesis, effects on the Greece economy, the Euro Union as well as the entire global economy. The motivation was primarily to glean lessons from the crisis with a view to enhancing the resilience of the existing monetary unions and more fundamentally to build sufficiently robust safeguards for emerging monetary unions such as the ECOWAS Monetary Cooperation Programme (EMCP).

The study employed qualitative approach by reviewing macroeconomic developments in Greece before and during the crisis based on data obtained from numerous sources including the IMF, World Bank, Bank of Greece, EUROSTAT, and EU Commission. The study observed that the crisis was due to a number of factors that could be broadly classified into exogenous and internal factors. The exogenous factors include the spillover of the 2007-08 global financial crisis, the subprime mortgage crisis of 2007–09, and the structural rigidities of the European Monetary Union (EMU). The internal factors were basically persistent fiscal deficits, loss of external competitiveness with the attendant current account deficit, false reporting of fiscal data and the ensuing loss of Greece government credibility. The macroeconomic performance of Greece prior to accession into the monetary union was generally poor; characterized by financial instability and state intervention in many sectors that were supposed to be purely market driven. Macroeconomic imbalances and structural problems were exacerbated by oil price shock while monetary accommodation and the introduction of full wage indexation entrenched high inflationary environment.

Consequently, productivity stagnated, investment dropped, and unemployment rate doubled. To address the challenge of macroeconomic imbalances, the government embarked on a medium term adjustment program in the late 1990s with the goals of reversing years of fiscal laxness and eliminating pervasive market distortions. Given the timing of the reform however, it could be reasonably adjudged that the whole essence was to ensure the admittance of Greece into the EMU and it was therefore not much of a surprise.

The analysis of the issues revealed key lessons that must be brought on board in the quest to strengthen the existing monetary unions as well as ensuring the success of EMCP. Among others: the need for all member countries to meet and sustain the critical convergence criteria especially fiscal discipline before joining the monetary union; the need to ratchet up the Stabilization and Cooperation Fund (SCF) and make it operational on or before the commencement of a monetary union; need for the development of a bond market and the general development of the financial sector to free the central and commercial banks from the burden of financing government; need to build up adequate revenue base through the diversification of the economy; need for independent central bank that will guide monetary policy formulation and implementation; the need to continue monitoring the convergence process and multilateral surveillance even after the formation of a monetary union; the need to sacrifice reasonable degree of sovereignty for political convergence; and the need for accurate statistical reporting.

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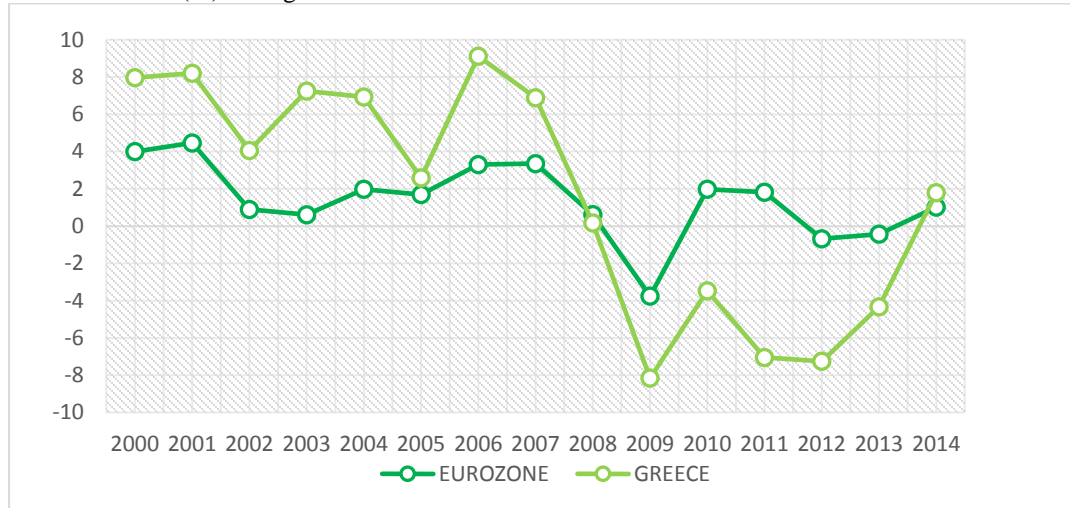
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APPENDIX

Figure A 1: Real GDP growth rate of Greece and Eurozone

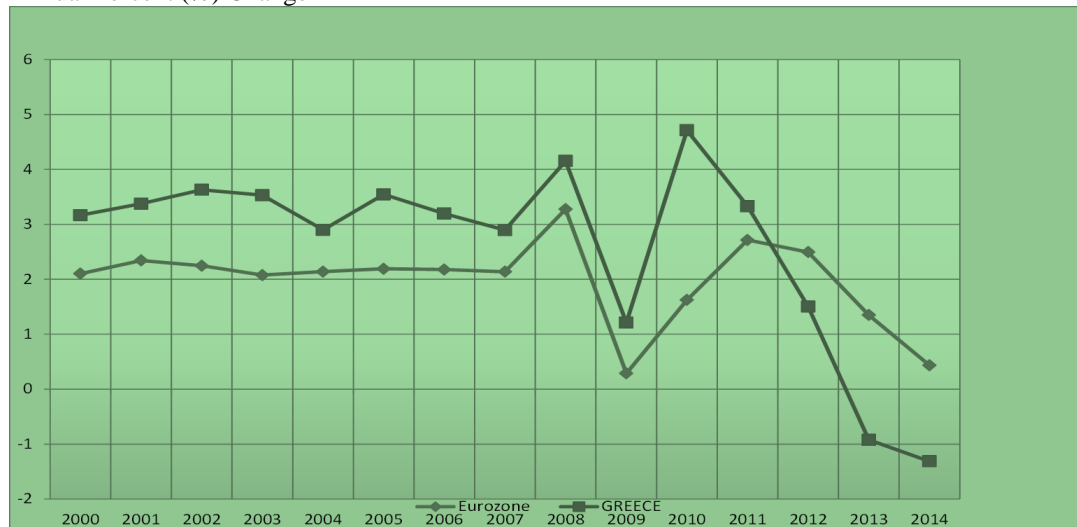
Annual Percent (%) Change



Source : www.elibrary-data.imf.org

Figure A 2: Inflation rates of Greece and Eurozone

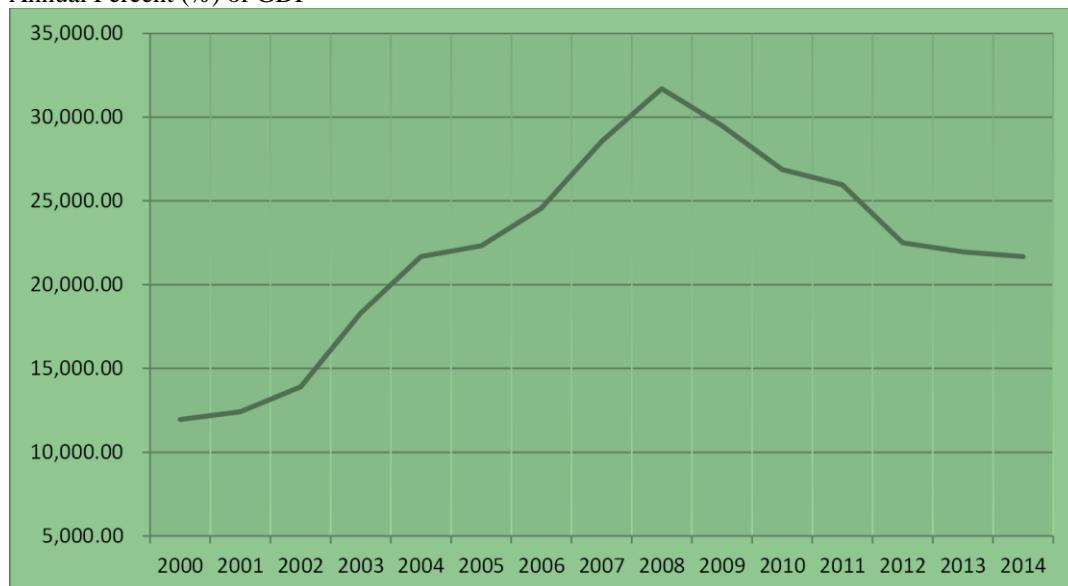
Annual Percent (%) Change



Source: www.elibrary-data.imf.org

Figure A 3: Greece Real GDP per capita

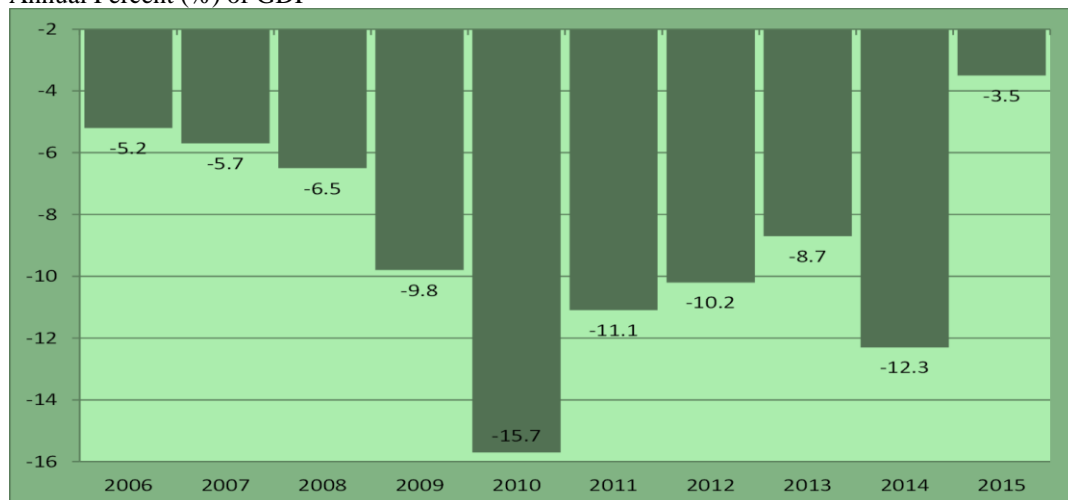
Annual Percent (%) of GDP



Source: www.elibrary-data.imf.org

Figure A 4: Greece Government Fiscal balances

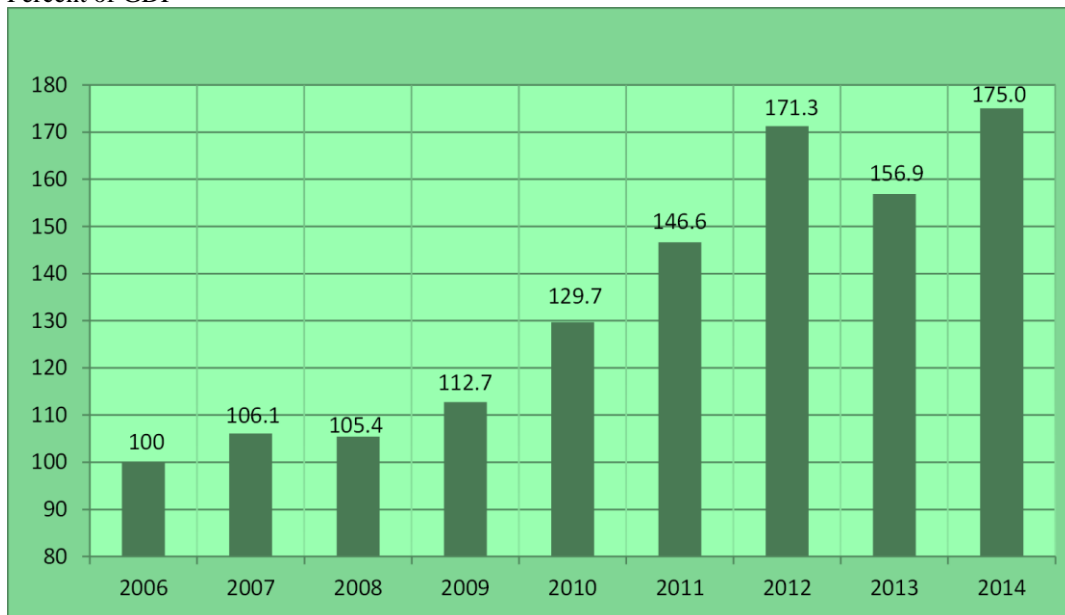
Annual Percent (%) of GDP



Source: www.elibrary-data.imf.org

Figure A 5: Greece Government Debt to GDP-Ratio

Percent of GDP



Source: www.elibrary-data.imf.org