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Everything's Fine With Greece, Just Ignore Some Facts

- By IRWIN STELZER



So it's all right, then. The agencies monitoring Greece's ability to meet the austerity targets set for it by the European Commission, the European Central Bank, and the International Monetary Fund are sufficiently satisfied with its progress to recommend release of the €9 billion (\$11.95 billion) that is the next tranche of the €110 billion bailout package agreed by the eurocracy and the IMF. Of course, to reach that conclusion, the only one available to those with a political stake in the durability of the euro, the authorities had to ignore a few nasty facts.

Most important, Greece has to rely on the bailout fund because the markets do not deem it sufficiently credit-worthy to be allowed to borrow at tolerable rates. The market has higher standards than the EC, IMF and ECB, and no political reason to show any tolerance. "We don't expect any return to the markets very soon," says Poul Thomsen, the IMF's Greece mission chief. The alternatives remain continued bailouts, or rescheduling or restructuring, to use oft-preferred euphemisms for default.

Little wonder, given some of the facts the monitors chose to downplay. Regional and local governments and entities continue to spend money they don't have. Tax evasion by high earners continues, the authorities so far being unable to get their collection procedures in order, or to cope with threats of tax flight. High-income ship owners, who flaunted their wealth at their champagne-sodden semi-annual "Posidonia" bash, are prepared to suffer exile in the

south of France if the government tries to force them to pay taxes bills. Or even endure the less agreeable climate of London.

Not that the rich have been untouched by their nation's problems: PropertyWire.com reports that the price of a 4,800-square foot house in the swanky Ekali suburb of Athens has been cut in half, to €2 million, a decline helped along by a proposed increase in property taxes.

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The Greek government could bow to an angry public.

Then there are the banks. Their capital is declining and their bad loans rising, both trends that will accelerate as the economy contracts by a predicted 4% this year. And if the summer tourist season is as poor as many expect—television pictures of riots in Athens and terrorist threats are redirecting those seeking a bit of relaxation in the sun to Spain and Turkey—the projection of a 4% decline might prove to be an understatement: tourism has traditionally accounted for 15% of Greek GDP. Finally, the overall euro zone economic recovery, powered by Germany's exports, well might bypass Greece, which has little to sell increasingly affluent Germans.

If the German taxpayer wearies of financing the Greek bailout, default will become inevitable. Such weariness might set in if what Federico Sturzenegger and Jeromin Zettelmeyer (professor at the Universidad Torcuato di Tella in Buenos Aires, and Director for Policy Studies at the European Bank for Reconstruction and Development, respectively) call "skeletons" are exhumed. In their comprehensive study, "Debt Defaults and Lessons From a Decade of Crises," the authors note that such skeletons—explicit debt that might not be on

the government books, such as pension obligations or guarantees to specific constituencies—"have a habit of showing up in crisis times."

Still, there is reason for some optimism. As Messrs. Sturzenegger and Zettelmeyer note, "crises operate as catalysts for reform." If that holds true for Greece, the government just might not let this crisis go to waste, and put its fiscal house in order.

But the magnitude of the task is daunting. Austerity will take about 10% out of GDP, with all that means for jobs. And still leave Greece with unmanageable debt levels and interest obligations.

Fortunately for Greece, in the bargaining between the bailed and the bailers, it has the upper hand. The cost to Greece of default is relatively trivial compared to the cost to its creditors, mostly European banks unready to take large write-downs. And the political cost of having been unable to forestall default by one of its tiniest members is unacceptable to the eurocracy. Not to mention the effect on the ability of other Club Med nations to continue recent progress in tapping international debt markets.

So the Greek government just might decide, if necessary, to bow to an angry public and renege on promises of austerity, passing the cost of its past profligacy on to German and other eurozone taxpayers, or to its creditors. Some 95% of Greek debt was issued in Greece, and is subject to sovereign immunity laws, which reduce the options available to unhappy creditors lining up for their haircuts.

Don't think that Greece's politicians are unaware of their powerful position vis-a-vis both their euro-zone colleagues and any creditors who feel unhappy with the deal they will be offered in lieu of full repayment. It would be understandable if they decide that unhappy euro-zone taxpayers or short-changed creditors are lesser evils than angry Greek voters.

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