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# The Greece Debt Crisis: Where the World Economies are Heading Up to

**Mr. Shivam Shukla** M.Com (Finance), UGC NET (Commerce) Banaras Hindu University (BHU)

**ABSTRACT**

*"A glorious past can't protect Greece's future" is a statement which has gained prominence and popularity for quite some time now. The country of Alexander the Great is in a state of complete turmoil and turbulence, there is utter pandemonium in the whole of Greece right now and more precisely the situation started worsening way back from 2009 but it is now that economic tremors and aftershocks have reached an unimaginable and unprecedented level. Needless to say, it is not going well and Greece is heading back in recession and crisis, and the government is facing default and of being kicked out of the euro zone. Three years earlier Greece had been accepted into the euro zone. But it was not economically sensible, and they now realise it was a terrible mistake. In this context the present study aims at discovering why such a situation actually occur in Greece, how the crisis like situation fairing for the Economies of the world and what could be the possible impact of the debt crisis on India.*

**KEYWORDS : Euro Zone, Debt Crisis, Unemployment Rate, GDP growth rate, Credit Ratings, Actual Individual Consumption, IMF, OECD**

## Introduction

The economy of Greece is the 43rd and 52nd largest in the world at $242 billion and $284 billion by nominal gross domestic product and purchasing power parity respectively, according to World Bank statistics for the year 2014. As of 2013, Greece is the thirteenth-largest economy in the 28-member European Union. In terms of per capita income, Greece is ranked 37th and 40th in the world at $22,083 and $25,331 for nominal GDP and purchasing power parity respectively.

The country is also a significant agricultural producer within the European Union. With an economy larger than all the other Balkan economies combined, Greece is the largest economy in the Balkans and an exigent territorial investor. Greece is sorted as an advanced, high-income economy, and was amongst the founding members of the Organization for Economic Co-operation and Development (OECD) and the Organization of the Black Sea Economic Cooperation (BSEC).

On 1 January 2001 Greece adopted the euro as its currency, replacing the Greek drachma at an exchange rate of 340.75 drachmae per euro. Greece is also a member of the International Monetary Fund and the World Trade Organization, and is ranked 23rd on the KOF Globalization Index for 2014 and 35th on the Ernst & Young's Globalization Index 2012.

The country's economy was desolated by the Second World War, and the high levels of economic growth that followed throughout the 1950s to 1970s were dubbed the Greek economic miracle. Greece enjoys a high standard of living and very high Human Development Index, ranking 29th in the world in 2013.However, the severe recession of recent years has seen GDP per capita fall from 94% of the EU average in 2009 to 72% in 2014. Actual Individual Consumption (AIC) per capita fell from 104% of the EU average to 83% during the same period.

Greece's main industries are tourism, shipping, industrial products, food and tobacco processing, textiles, chemicals, metal products, mining and petroleum. Greece's GDP growth has also, as an average, since the early 1990s been higher than the EU average. However, the Greek economy also faces significant problems, including rapidly rising unemployment levels, an inefficient public sector bureaucracy, tax evasion, corruption and low global competitiveness.

## Need of Study

Greece, the weak link in the euro zone, is inching closer to defaulting on its debt. The country has been in a long standoff with its European creditors on the terms of a multibillion-dollar bailout. If the country goes bankrupt or decides to leave the 19-nation euro zone, the situation could create instability in the region and reverberate around the globe. The country missed its 30th June 2015 deadline to repay roughly 1.6 billion Euros, or $1.8 billion, to the International Monetary Fund. Hours before the deadline for the payment, Prime Minister Alexis Tsipras asked the other nations that use the euro to provide another bailout, which would buy time for Athens to renegotiate its crippling debt load. Chancellor Angela Merkel of Germany said earlier in the day that no deal with Mr. Tsipras's government could be negotiated until after a Greek referendum scheduled for Sunday. Greek voters will be asked to accept or reject an offer made last week by the country's creditors.

## Objectives of the Study

1. To understand why Greece default on its debt and the factors leading to such crisis like situation.
2. To evaluate the ongoing status/position of the Greek economy through selected Economic Indicators.
3. To clarify how does the crisis affect the global financial system and major economies of euro zone in particular.
4. To study the potential impact of the Greek crisis on the Indian markets and the overall economy of India.

## Research Methodology

Research methodology is the blue print of the research which is being conducted. The Research design in this study is Descriptive research design. As per the nature of the study researcher had to go for the collection of some relevant data for further study. There were lots of raw information available in literature for the related topic. The Data is collected from secondary sources particularly from Web sites, newsletters and data from various reports. The Internet Facility has been substantially used during the process of research.

## Factors leading to Greece Default

Since the turn of the millennium, Greece saw high levels of GDP growth above the Euro zone average, peaking at 5.9% in 2003 and 5.5% in 2006. The subsequent Great Recession and Greek government-debt crisis, a central focus of the wider European debt crisis, plunged the economy into a sharp downturn, with real GDP growth rates of −0.2% in 2008, −3.1% in 2009, −4.9% in 2010, −7.1% in 2011, −7.0% in 2012 and −3.9% in 2013. In 2011, the country's public debt reached €355.141 billion (170.3% of nominal GDP). After negotiating the biggest debt restructuring in history with the private sector, Greece reduced its sovereign debt burden to €280.4 billion (136.5% of GDP) in the first quarter of 2012. Greece returned to growth after six years of economic decline in 2014, but went into recession again in 2015.

Harris Dellas, director of the Institute of Political Economy at the University of Bern, and George S. Tavlas, a member of the Monetary Policy Council of the Bank of Greece draw two main suggestions as to why this happened to Greece.

First, the durability of a monetary union is crucially dependent on the existence of a well-functioning adjustment mechanism.

- In Greece, there was no mechanism to adjust money and credit growth, causing it to run large current account and fiscal deficits without taking remedial policy measures. This behavior resembled that of the Latin American countries and of European countries (such as Greece) that were not members of the gold standard.
- Under the gold standard, European peripheral countries ran current account deficits, but the size of those deficits was small relative to those experienced by Greece under the euro.
- They were small because fiscal shocks were smaller and, more importantly, because the adjustment mechanism while imperfect, worked to mitigate the buildup of external imbalances.

Second, adherence to a hard peg is no panacea and cannot be sustained without the support of credible fiscal institutions.

- In the euro zone, the market's perception that Greek sovereign debt represented a safe investment -- probably founded on the expectation of a bailout by core countries -- suppressed the effect of sovereign credit risk on Greek interest rates.
- At the same time, low interest rates greased the wheels of fiscal expansion by sending the message that there was no price to be paid for the buildup of sovereign debt.
- Hence, while external imbalances were essentially self-correcting under the gold standard, they were self-perpetuating in the euro zone due to the perception of an absence of credit risk.

**Current condition of Greek Economy**

Unemployment Rate in Greece remained unchanged at 25.60 percent in March of 2015 from 25.60 percent in February of 2015. Unemployment Rate in Greece averaged 14.94 percent from 1998 until 2015, hitting an all time high of 28 percent in September of 2013 and a record low of 7.30 percent in May of 2008. Unemployment Rate in Greece presented here is reported by the National Statistical Service of Greece.


**Chart 1**

The Gross Domestic Product (GDP) in Greece extended by 0.20 percent in the first quarter of 2015 over the same quarter of the previous year. GDP Annual Growth Rate in Greece averaged 1.04 percent from 1996 until 2015, reaching an all time high of 7.50 percent in the fourth quarter of 2003 and a record low of -10.40 percent in the first quarter of 2011. GDP Annual Growth Rate in Greece given here is reported by the National Statistical Service of Greece.

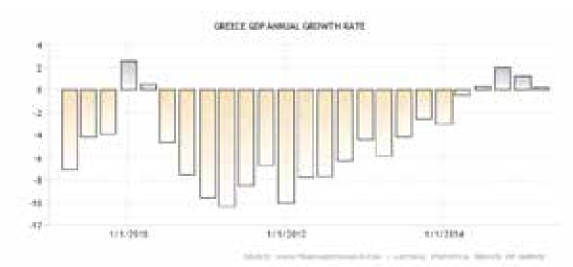



**Chart 2**

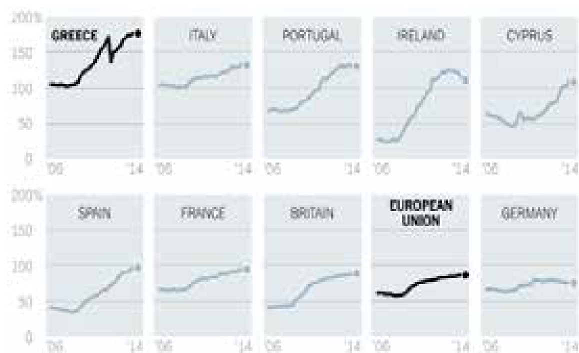
Credit Ratings are commonly understood as the opinion of a rating agency on the relative capability of a country to pay its debt service obligations as and when they arise. The ratings agencies cited the potential for dissolving liquidity in the Greek government, banks and economy. S&P wrote that outlook for full-year economic growth looked "highly uncertain." "Without deep economic reform or further relief, we expect Greece's debt and other financial commitments will be unsustainable," S&P wrote in a recent press release.

| Rating Agency | Rating | Interpretation |
|---|---|---|
| S&P | CCC- | Negative (vulnerable to nonpayment of obligations) |
| Moody's | Caa3 | Negative (poor quality and very high credit risk.) |
| Fitch | CCC | Negative (default is a real possibility) |

**Table 1**

**How does the crisis affect the Euro Zone?**

Since Greece's debt crisis began in 2010, most international banks and foreign investors have sold their Greek bonds and other holdings, so they are no longer vulnerable to what happens in Greece. (Some private investors, who subsequently plowed back into Greek bonds, betting on a comeback, regret that decision). In the meantime, the other crisis countries in the euro zone, 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. What's more, the European Central Bank has instituted powerful firewalls, by buying huge amounts of euro zone government bonds and by assuring to purchase more if needed, making governments less subject to market whims and fancies. The following Chart represents Gross government debt as a percentage of gross domestic product of top euro zone economies plotted through the fourth quarter of 2014. (On next page)




Source: Eurostat (Gross government debt as a percentage of gross domestic product)

**Chart 3**

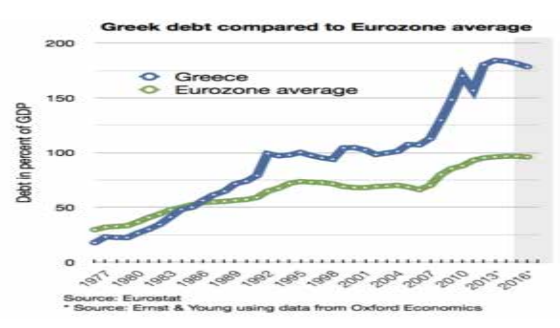
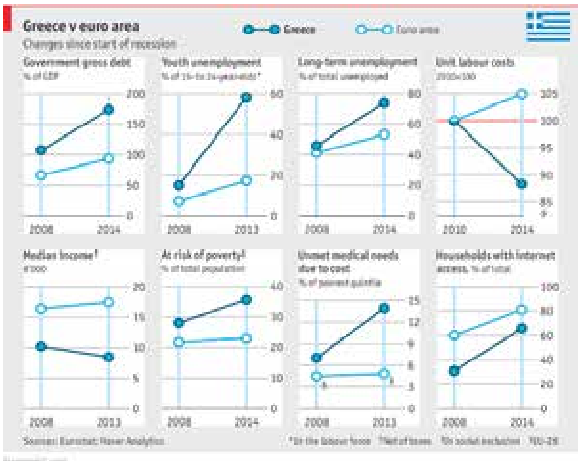



**Chart 4**




Source: Economist.com **Chart 5**

The financial crisis – particularly the austerity package put forth by the EU and the IMF – have been met with anger by the Greek public, leading to disputes and social unrest. Despite the long range of austerity measures, the government deficit has not been restrained accordingly, mainly, according to many economists, because of the subsequent recession. Public sector workers have come out on strike in order to resist job cuts and reductions to salaries as the government pledges that a large scale privatization programme will be given an impetus. Immigrants are sometimes treated as scapegoats for economic problems by far-right extremists. In 2013, Greece became the first developed market to be reclassified as an emerging market by financial services companies MSCI and S&P Dow Jones Indices. Greece exited its six-year recession in the second quarter of 2014, but the challenges of securing political stability and debt sustainability remain.

**Impact of Greece Crisis on India**

1) India does not have a large exposure to Greece as far as direct trade is concerned, said Commerce Secretary Rajeev Kher. But he said that exports from India could be adversely affected if the European Union lands into problem.
2) Former RBI governor Bimal Jalan too said he does not see the Greece crisis impacting the Indian economy to a great extent. India is not a very high trade dependent country and India's GDP growth rate could be impacted by "0.2 per cent or something" if the crisis intensifies, he said.
3) Dr Jalan hopes that the European Central Bank, which is in the midst of a sweeping $1.1 trillion stimulus programme, would be able to holdback the spread of the Greece crisis across the continent. Global brokerage Nomura too said that it does not see the Greece problems escalating into a systemic pan European crisis.
4) If the Greece turmoil persists, the US Federal Reserve may delay its interest rate hike, said Saugata Bhattacharya, senior VP for Business & Economic Research at Axis Bank. Analysts had earlier said the Fed was on track to hike rates from end of this year. A Fed rate hike may cause some trepidation in global financial markets as investors could commit their funds in US bonds to take advantage of higher rates.
5) Experts in fact remain bullish on Indian rupee, citing India's stronger economic fundamentals as compared to the other emerging markets. RBI Governor Raghuram Rajan recently said that he anticipates India's economy would be able to withstand any impact from the crisis in Greece, thanks in part to its foreign exchange reserves, which reached a record high of $355.46 billion as of 19th of June 2015.
6) Market view: Analysts say that Indian markets have shown a strong rebound to the Greek crisis as compared to a bigger selloff in other markets. The recent selloff in Chinese stock markets could trigger some safe-haven buying in Indian equities as India remains less exposed to Greece crisis as compared to some other Asian countries.

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