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τα οποία εκπροσωποῦν μόνο τις ἀπόψεις τῶν συγγραφέων.

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# ARCHIVES OF ECONOMIC HISTORY

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# ECONOMIC IMPACT OF DIRECT DEMOCRACY: A LITERATURE REVIEW, SUGGESTIONS FOR GREECE

N. K. KYRIAZIS\* N. I. GKANAS\*\*

## Abstract

The purpose of this paper is to define the issues concerning the processes of citizen participation in political decisions in Greece and the impact that participation has in the economic performance. After analyzing the dimensions of democracy –especially the direct one–, the ancient Athenian democracy and elements of direct democracy in the modern world focusing in Switzerland, Germany and the U.S.A. we discuss the possibility of adopting stronger direct-democratic processes affecting the economic performance in Greece. We also suggest some indicative questions for possible referenda. The conclusions make it necessary to adopt bottom up processes of direct democracy to put fiscal reform issues and creating an attractive business environment in order to reduce fraud, increase government revenue, stimulate the labor market and increase growth.

*JEL Classification: N4, K1, P59*

*Keywords: direct democracy, economic impact, athenian democracy, initiative.*

## 1. Introduction

The governance of a state, a country or a city is a permanent field of debate and exchange of views between experts and non-experts. The participation of the people or not in common issues, the degree of people representation to a greater or lesser rate, the way to exercise political governance are important issues to the daily lives of people and the existence, emergence and progress of a country or a nation, a city, both economically and socially.

Until today it has been implemented a number of regimes, other successful and others not. The crucial element is always the welfare of the people and, therefore, it has become almost entirely accepted that a democratic regime is more positive among the existing regimes and if this does not happen, then democracy is the least negative concerning its impacts.

Democracy can take many forms; among them the direct and indirect or

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representative democracy. Direct democracy is much less used than indirect democracy worldwide.

The recent political and economic situation of Greece that is undergoing a deep crisis, coupled with the announcement of a referendum by the Greek Government (November 2011)<sup>1</sup> for obtaining a new loan from the European Union (EU) and the International Monetary Fund (IMF), raises many issues for the direct involvement of the people in political decisions. The last option has an impact in both economic and political fields.

The purpose of this paper is, after making a brief reference to the regime of direct democracy in the recent and the long past and contemporary forms of direct democracy in countries such as Switzerland and in states like California, to define the issues of procedures citizen participation raises in political decisions in Greece and the impact that participation has in the economic process. Moreover are outlined questions that could be set for future referenda in Greece and possible implications.

## **2. Definitions for Democracy**

Democracy is the political system that provides citizens with opportunities for change of government rulers and election of persons of their choice (Lipset, M.S., 1960). Democracy means rule of the people or sovereignty of the many (from the Greek words *Demos* (citizens) and *Kratos* (Power)). The main characteristics of democracy are the following: It comes from the people, exercised by the elected representatives that serve the interests of them (Schmidt, 2000). Each member should have equal and meaningful opportunity to vote and all votes should be counted as equivalent (Dahl, 1998). There should be free, fair and frequent elections, freedom of expression and access to alternative, independent sources of information (Crick, 2006). Democracy ensures a high degree of equality, encourages human growth and increases welfare (Dahl, 1998). The disadvantages of democracy are that mediocre leaders are chosen (skilled staff is not attracted, since they prefer the more lucrative career in the private sector), it is expensive, incubates corruption and bribery, and finally there is the risk of degeneration into despotism (Tocqueville, 1840).

The two basic categories of Democracy are indirect democracy and direct democracy. In indirect democracy, the executive and legislative power is exercised by legally elected representatives of the people, elected periodically (Cronin, 1999). In the second citizens decide on an important issue directly

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<sup>1</sup> And finally the decision to withdraw the proposal.

themselves (Kaufmann et al., 2010). The latter is also known as “Theory of participatory democracy» (Pateman, 1970; Bachrach, 1970; Bachrach & Botwieniek 1992;), “Expansive democracy” (Warren, 1992), “Strong democracy” (Barber, 1984), “Assosiative democracy” (Hirst, 1994), “ Interactive democracy” (Giddens, 1997) and as “Conference democracy” (Habermas, 1992, 1999).

The issues that direct democracy faces are (Kyriazis, 2012): the problem of principal-agent representation and the actual preferences of voters. According to the principle of representation citizens choose their representative, the party and the government to take concrete policy initiatives, most of which are promised during the election period. Very often, after a party forms a government it follows a different policy in relation to its commitments, to reap the benefits for itself sometimes. In a fully representative democracy, citizens do not have the ability to control their representatives during their term. The effect of this lack of control is increased waste of resources, corruption and fraud. Second issue is the actual preferences of voters-citizens. In representative democracies the only option for the voters is the pre-election programs of parties. They cannot make choices about specific issues and cannot add topics that are absent from their electoral programs. Political parties therefore have a monopoly on the issues on which decisions are taken.

The means that direct democracy uses in order to achieve its objectives are (Kaufmann et al, 2010):

- **Popular or citizen initiative.** Initiative procedures are characterised by the right of a minority, normally a specified number of citizens, to propose to the public the introduction of a new or renewed law. The decision on the proposal is made through a popular vote. The initiative procedure may include a withdrawal clause, which gives the sponsors the possibility to withdraw their initiative, e.g. in the event that the legislature has taken action to fulfill the demands of the initiative or part of them. In some cases a representative authority (normally parliament) has the right to formulate a counter-proposal to the initiative proposal. Both proposals are then decided on at the same time by a popular vote. In another case (Initiative Agenda) a specified number of eligible voters suggests a public authority to adopt a law or measure. The authority decides what will happen with the proposal / initiative. Additionally there is another form of initiative (Authorities’ minority initiative) which allows a specified minority of an authority (e.g. the one third of Parliament) to make its own proposal on the political agenda and let people decide on it by a popular vote.

- **Referendum bottom up.** The referendum is a process of direct

democracy, which includes the popular vote on a substantive issue, such as a constitutional amendment or a bill. Voters have the right to accept or reject the proposal. The process begins either by law<sup>2</sup> (→ mandatory referendum), by a certain number of citizens (→ popular referendum - that is caused by people - bottom up), or by a minority in an authority (authorities' referendum minority - top down). There are five types of referendum bottom up (Kaufmann et al. 2010, pp.201-202): *Popular or citizen-initiated referendum*. It allows a certain number of citizens to initiate a referendum and let the entire electorate to decide whether, e.g. a particular law should be enacted or repealed. This process acts as a corrective action in parliamentary decision-making in representative democracies and as a check on parliament and government. *Popular referendum and counter-proposal*. This direct democracy process combines a popular referendum against the decision by an authority with a referendum on a counter-proposal. *Referendum Proposal*. This process is characterized by the right of a predetermined number of registered voters to propose to the competent authority to hold a popular vote on a particular issue. The demand is addressed to competent authorities (usually parliament - local or national), which will decide on further action. *Mandatory referendum*. This process of direct democracy is activated automatically by law (usually the Constitution), which provides that certain issues should be put before the voters for approval or rejection. *Authorities' minority referendum*. It is characterized by a minority right authority to put the majority decision of the same principle, in the popular vote for approval or rejection. This procedure allows a minority of one authority to give the last word to voters.

• **Referendum top down.** A top down referendum is decided and controlled “from above”. Various authorities (the President, the Prime Minister, the European Parliament) decide when and for what the people will be invited to vote or give their opinion. Rather than being involved in the control of the process, citizens are the means for a decision determined by a public authority. Referenda top down (or plebiscites) give additional power to politicians than citizens. They are used to avoid political responsibility for the controversial issues that have become an obstacle: to take legitimacy to decisions that have already been taken by those in power; and they are used by an authority to circumvent another authority. The goal of the top down referendum is not to implement democracy, but to reinforce or rescue those in power with the help of “the people”. There are two types of referendum top down (Kaufmann et

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2 A popular vote procedure, which is triggered and controlled exclusively by the authorities, is not a referendum but a plebiscite.

al. 2010, p.203): *Plebiscite (popular vote controlled by the authorities)*. Its use is exclusively under the control of authority. In this form the author of the proposal to a vote and the initiator of the process is the same (for example, Parliament or the President). *Veto-Plebiscite (popular vote controlled by the authorities)*. And in this case its use is exclusively in control of the authorities. In this form the author of the proposal to a vote and the initiator of the process are not the same. For example, a government or a president can oppose (veto) a decision of Parliament and shall refer the matter to a referendum. Hence the name veto-plebiscite.

• **Recall.** The recall of political officials is a mechanism that exists in few countries worldwide and is used infrequently. The last years experienced a rise, especially in the U.S.A. Recall exists in the U.S.A. from the early 20th century (except at the federal level), in Switzerland, in Canada (since 1995), in Venezuela<sup>3</sup> and Cuba. It grows increasingly internationally as governments in India, Britain and Australia directed to adopt the institution of recall in a custom format (L.A.T- Spivak., 2011). The roots of this mechanism are found in ancient times, the period of Athenian democracy and the similar mechanism that prevailed then, ostracism<sup>4</sup> (Kyriazis, 2012).

The distinction between top-down (i.e. from leaders to citizens) and bottom-up (bottom up, i.e. from citizens to leaders) procedures of direct democracy is crucial. The plebiscites are popular voting procedures that cannot be triggered from citizens, and whose use is solely in control of the authorities. This distinction between referenda top down (plebiscites) and referenda bottom up is fundamental to an understanding of direct democracy. The distinction is not often done, and often leads to much confusion in the debate on direct democracy.

The benefits of direct democracy are that (Cronin, 1999; Przeworski and Limonghi, 1993; Barro, 1996; Tavarez and Wacziarg, 2001): it promotes government accountability, transparency is safeguarded, public interest in politics increases, public spending is lower, and prosperity increases, uses non-violent political means and also is an alternative for dealing with difficult issues. The weaknesses of direct democracy are the small number of people who can

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3 Article 72 of the Venezuelan Constitution determines the recall for any elected representative, including the President. This option is used when the 2004 recall referendum was held for President Hugo Chavez, unsuccessfully.

4 The ostracism or excommunication was a voting procedure in ancient Athens, which decided freely, without trial, the forced exile (for ten years, then fell to five years) or not of a person that was judged dangerous for the city. It was applied after the reforms of Cleisthenes 508/507 BC and lasted for fifty years.

really express themselves, especially in countries with large populations and the overestimation of the capacity of citizens, since it is almost impossible to be aware of all the issues, which will have to be decided upon (Dahl 1998; Schmidt 2000).

### **3. Athenian Democracy**

The Democracy of Ancient Athens (510 BC - 323 BC) had the following creations causes (Kyriazis, 2012):

1. Creation of city-states.
2. Appearance of a new class of warriors/citizens acquiring values such as discipline, obedience, common goals, equality, independence through working in the phalanx and triremes.

These values were transferred to politics and contributed to the development of democracy. This transfer is essentially the application of bounded rationality (Simon and March, 1993). Values such as fairness (equality before the law), equality, 'isigoria' (freedom of expression) moved from cooperation in the phalanx and triremes in the political field.

Alongside it was important the contribution of Solon, Cleisthenes and Ephialtes. Solon (Sinclair, 1991) divided the citizen body into four classes (pentakossiomedimnoi, ippeis [horsemen], zeugites ['yokemen'], thetes [poorest]) depending on their income (592 BC). In fact he replaced the aristocracy of family that prevailed until then, to an aristocracy of money (Cohen, 1992). The origin of the family was by then the critical ingredient for participation in the running of the state, but Solon was a merchant and he believed that economic progress is evidenced and the ability of individuals. Additionally he abolished the debts of the rural population (known as seisachtheia), where before that farmers were losing their freedom and became slaves to the lenders, if they could not repay their debts (Dunn, 1992). The contribution of Cleisthenes was the division of the citizen body into ten tribes (508 BC), based on residency only (op.cit.). Moreover he established the House of five hundred attended by fifty people equally from each tribe. The contribution of Ephialtes was that reduced the executive and judicial powers of the Areopagos (Supreme) Court (Aristotle, Ath. Pol. 25.1-4).

Democratic institutions in ancient Athens was the Assembly (working with the internal administration, legislation, elections, religious and external affairs), the House of 500 (with particular attention to the pre-processing of bills imported into the Assembly) and the Iliiaia (Elijah) Court that listed 6000 people. Citizens (men) were selected in all offices by lot for an annual term.

The causes of the fall of the Athenian Democracy span in several dimensions. The majority of citizens were biased towards the rich ones, as they face them with envy and often vote for laws that reduce the income of the latter. The transformation of the middle class that caused from the fall in income led them to running less in the state. The House of 500 became biased, as accepted financial assistance with result the influence of the laws (Lysias, against Nikomachus, 22). The economic diversion from the many benefits, especially "theorika"<sup>5</sup> and the rhetoric of politicians as well, exacerbated the collapse of Athenian Democracy.

## **4. Modern Forms of Direct Democracy**

### **4.1 Existing Situation**

Apart from the assembly of citizens conducted even in some Swiss cantons and municipalities of Switzerland and the United States of America, direct democracy does not exist in its purest form. In Switzerland and the U.S.A. elements of direct democracy such as referenda and initiatives, work additionally to the institutions of parliament and government in a framework of representative democracy. The initiatives (constitutional and legislative) establish new laws, coming from the Citizen. Their standard format allows the voters to propose a new law and if they can collect a significant number of signatures from fellow citizens, the proposed law put to the vote. In this way, representatives are led to decide a law and/or to adopt measures that they do not want to adopt and would have not voluntarily decided. There are also audit referenda that allow citizens to approve or cancel laws from the Legislature. These can be mandatory or optional. Optional referenda are executed if a certain number of voters require a referendum. Compulsory referenda impose responsibility on representatives to hold a referendum on legislative projects and with pre-determined time limits. Such referenda exclude the possibility that the laws imposed will not be against the willingness of the majority of citizens.

Heads of several countries have often addressed the people to decide on various issues. The President Corazon Aquino put, in 1986 the Constitution of Philippines before people for the validation and this Constitution provides the right of initiative and referendum. The Spanish people voted to keep Spain in

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5 It is payment to poorer citizens out of state revenue to enable them to watch the 4 days theatre plays and to participate in the Assembly.



**Figure 1: Countrywise popular votes on substantive issues**

Legend: first number: all countrywise popular votes on substantive issues since 1793, number in brackets: votes since 1991  
 countries in white background: no popular vote provided  
 Source: Kaufmann et al (2010), p.207.

the North Atlantic Treaty Organization. Irish and Italians voted on the issue of divorce. Swiss often vote for major and secular subjects. Charles de Gaulle put to French voters the question whether France should withdraw from Algeria and he won their trust in this policy. British people voted in a national referendum on whether to keep the country in the European Common Market. And several other countries resolve border or border disputes, putting these issues to the people (Cronin, 1999).

Figure 1 shows the total number of national popular votes by continent. Europe ranks first with 934 votes, followed by America and Asia which are at the same level, followed by Oceania with fewer referenda (102 from 1793, 37 from 1991).

As shown in Table 1, the difference of direct democracy in Switzerland and other consolidated democracies is inferred by the number of national referenda. In Switzerland 311 referendums took place in the period 1945-1988. In second place, and far from the first, is Italy (47), followed by New Zealand

**Table 1: Number of national referenda in democracies of the world, before 1945 till 1988**

<b>Country</b>	<b>Before 1945</b>	<b>1945-1988</b>
Australia	21	24
Austria	1	2
Belgium	0	1
France	14	12
Denmark	3	15
Switzerland	137	311
Greece	3	4
USA	0	0
Japan	0	0
India	0	0
Ireland	1	21
Iceland	5	0
Spain	3	5
Israel	0	0
Italy	2	47
Canada	2	1
Costa Rica	0	0
Luxemburg	3	0
G. Britain	0	1
New Zealand	17	26
Norway	4	2
Germany	6	0
Holland	2	0
Portugal	1	2
Sweden	1	4
Finland	1	1

Source: Gallagher (1996, p.230), Butler and Ranney (1994, p.266)

(26), Australia (24), Ireland (21), Denmark (15) and France (12). Spain with five polls and Sweden and Greece with 4 polls each sit in the next positions to be followed by countries in which between 1945 and 1988 there were only one or two referenda (Belgium, Finland, Great Britain, Norway, Austria and Portugal). Finally there is a group of countries which are characterized by a maximum of representative and a minimum of direct democracy, which is the Federal Republic of Germany, Israel, Japan, Luxembourg, the Netherlands. These countries have not used a national referendum. Finland was also included a long time in this group, but in 1994 there was a crucial referendum, on the inclusion or not of Finland in the European Union (Butler and Ranney, 1994; Gallagher and Uleri, 1996; Linder, 1999).

#### **4.2 The case of Switzerland**

Switzerland is the leader in the use of direct democracy among modern countries. No other country offers its citizens so many opportunities to participate as the Swiss federation. Direct democracy is developed there at an unusually high degree, not only nationally but also in the cantons (the Swiss version of German federal states) and communities (Kobach, 1993; Linder, 1994, 1999). By collecting 100,000 signatures, citizens can trigger constitutional review and with 50,000 signatures can put a referendum (Federal Constitution of the Swiss Confederation, articles 138, 139, 141).

The legislative initiative provided in local level and concerns issues such as social welfare, environment, economy, finance, social integration policies and peace. Indicative decisions of referendums and initiatives in Switzerland are: the abolition of favorable tax arrangements for foreign millionaires (canton of Zurich -2009), the rise of price of diesel by 13 cents per liter for strengthening public revenues and the establishment of national VAT in order to increase the pensions (1993). The effect of direct democracy in Swiss economy (Feld and Kirchgässner (2004, 2005, 2006, 2010) is impressive: in cantons with stronger participation rights for financial affairs, economic performance is 15% higher (in terms of per capita GDP); in cantons where citizens can vote on the public budget, there is 30% less tax avoidance. This is because people are more ready to support public spending, when they are involved in decisions about how their money is spent. In towns where the budget must be approved by referendum, public spending is 10% lower per capita. Municipalities that use fiscal referendum face 25% lower public debt. Public services cost less in towns and cities with direct democracy: the disposal of waste is approximately 20% cheaper.

### 4.3 The case of Germany

The Bundesrepublik (Germany) is a federal country. Re-unified Germany consists of 16 states (Länder), 323 districts (Landkreis) and 13,854 local authorities (Kommune), of which 2,047 are towns and cities. The federal states have important powers that are primarily administrative, for example in the areas of transport, education, culture, policing, and the environment. The states participate in national legislation on matters which concern them via the Bundesrat (national parliament), which is composed of representatives from all the state governments. The local authorities have competence in certain areas of decision-making, such as local taxation, energy supply, refuse collection, roads and transport, infrastructure, and planning permission. Germany has developed a very strong trend towards more direct democracy since the reunification in 1990. The most developed of the federal states in this area is Bavaria, which had more than one quarter (33) of 145 popular initiatives in the 16 states in total and 5 of the 10 referenda that have been raised by citizens since 1990 (at state).

On average about 200 local referenda are conducted in Germany each year. In Bavaria alone, more than 1,360 initiatives have been launched and 640 referenda took place from 1995 to 2001 (at local / municipal level).

A major problem has been poor design of initiatives and referendums, which are not very citizen-friendly. This has weakened the potential of law-making by the citizen (Kauffman, 2004).

Germany is one of the few EU countries which so far have no experience in national referenda. The Constitution (Article 29) provides for national referenda only for changes to administrative boundaries (Schmidt, 2000, p 399). In the Weimar Republic, there were three popular initiatives and two national referenda (1926 and 1929). During the National Socialist period, three plebiscites were held, with biased questions and blatant manipulation of the results.

In regional (state) level popular participation in formulating and passing laws is divided into three stages, but as the specific procedures developed by individual states, differ significantly in detail. The following describes generally the most important provisions:

a. Request to initiate a process that can eventually lead to a referendum. The first stage is when people submit a formal request/application to initiate the process and the legality of the application is checked. Initiatives for legislative and constitutional matters are allowable in principle to most parts of Germany, although in Berlin, Hesse and Saarland, constitutional issues are excluded. In practice, only the legislative proposals (bills) are permitted,

although “other political issues” can be raised in Brandenburg, Hamburg and Schleswig-Holstein. Initiatives that are directly or indirectly to the economy (the so-called “finance taboo”), including taxation and salaries of politicians and officials, are excluded.

b. Initiative (“People demand», *Volksbegehren*). The second stage involves the collection of signatures supporting the initiative. The minimum signatures quorums typically range between 8% and 20% of the electorate of the state. Only Brandenburg, Hamburg and Schleswig-Holstein have low, “citizen friendly” limits of 4% and 5%. Registration procedures vary. Nine states allow free collection of signatures within a time frame of between 3 and 12 months. In seven other states, the signatures must be recorded in designated official venues and time limits vary between two weeks to two months. A «*Volksbegehren*» (popular demand), which achieves the required number of signatures should be discussed in the state parliament (*Landtag*). If the latter accepts the proposal as it stands there is no need for a referendum to be held. If the proposal is not accepted and the issue is taken to referendum, the Parliament has the right to make a competing alternative legislative proposal.

c. Citizens’ Decision („*Referendum*», *Volksentscheid*). The result of a referendum is legally binding. However, in most states – in contrast to the rule of elections – a simple majority of votes cast does not automatically lead to positive results. In referenda on simple legislation, most states require a minimum authorization of 20%, 25% or 33% of the electorate. Only Bavaria, Hesse and Saxony did not require such a limit. In a constitutional referendum, all states have a minimum approval rate of 50%, with the exception of Bavaria, where the approval rate is 25%. Moreover, this rate is further linked to a two-thirds majority in favor of reform, making changes nearly impossible. In fact, about one quarter of citizens’ initiatives have been declared invalid for legal reasons. By 2003, 145 popular initiatives (“*Volksinitiativen*”) had begun, 41 of them reached the second stage, the popular demand («*Volksbegehren*”), and ten finally went to a referendum. The majority of popular initiatives (31 of 131) and referenda (5 of 10) were in Bavaria, the only state scoring regular and active use of instruments of direct democracy in Germany.

The overall picture is somewhat disappointing: in four of the 16 federal states there was only one referendum that has been initiated by citizens. On average, a referendum takes place in each federal state only once every 43 years. The direct success rate of all initiatives (in all stages) is around 20%. In addition to legislative referenda, there are other types of referenda. 14 states constitutions were accepted by popular referendum. In Bavaria and Hesse, there is a statutory referendum on the Constitution, which has been used on

five occasions in each of these states. Seven referenda have been conducted on changes in administrative boundaries/borders. Overall, there have been 34 referenda since 1946 in all federal states.

At the local level (municipalities), the right of popular participation in decision making by local referendum (Bürgerentscheid) before 1989 was known only in Baden-Württemberg, but today direct democracy has been introduced at the local level, in 15 of the 16 states. Only in Berlin there is still no direct democracy at city level. Bavaria and Hamburg are special cases. Here the right to local referendum was introduced by the people themselves in statewide referenda, even though in both cases the state government was opposed to it. Not surprisingly, therefore, these two states have by far the most liberal procedures. In all states, popular decision-making process is in two stages:

a. Popular Initiative (Bürgerbegehren). In most states, some important local issues are excluded from the process (these are listed in a so-called “negative list”). In half of the states there is a sliding scale of quota of signatures depending on the size of the community: in Hamburg it is 2% to 3%, in Saxony-Anhalt, from 6% to 15%. In the rest of the states there is a uniform threshold, which ranges from 10% to 20% among states. The time limit to collect signatures applies only when the initiative is directed against any decision taken by a local authority. The time period specified varies from four weeks to three months. Normally, the local authority decides on the admissibility of an initiative. The initiative group may appeal a rejection. The local council may accept the initiative and in this case the issue does not go to referendum.

b. Citizens’ Decision (Bürgerentscheid). In almost all federal states the minimum participation threshold is between 20% and 30%. Initially, Bavaria had no minimum participation threshold, but the state government introduced a sliding scale of between 10% and 20% depending on the size of the community. Only in Hamburg a simple majority of votes without further restrictions is accepted. When a local referendum is successful, the majority of states set a transitional period from one to three years, during which the outcome of the referendum can be repealed or changed only after a new referendum.

On average, about 200 local referenda are conducted in Germany each year, the majority in Bavaria, where there were more than 1260 initiatives and 578 referenda within 6 years (1995-2001). This means that every community in Bavaria conducts a referendum only, on average, once every 24 years. In other states, where the barriers are higher, local referenda are used less frequently. For example, in Lower Saxony there have been only 54 initiatives and 18 referenda, giving an average of only one referendum per community every 344 years.



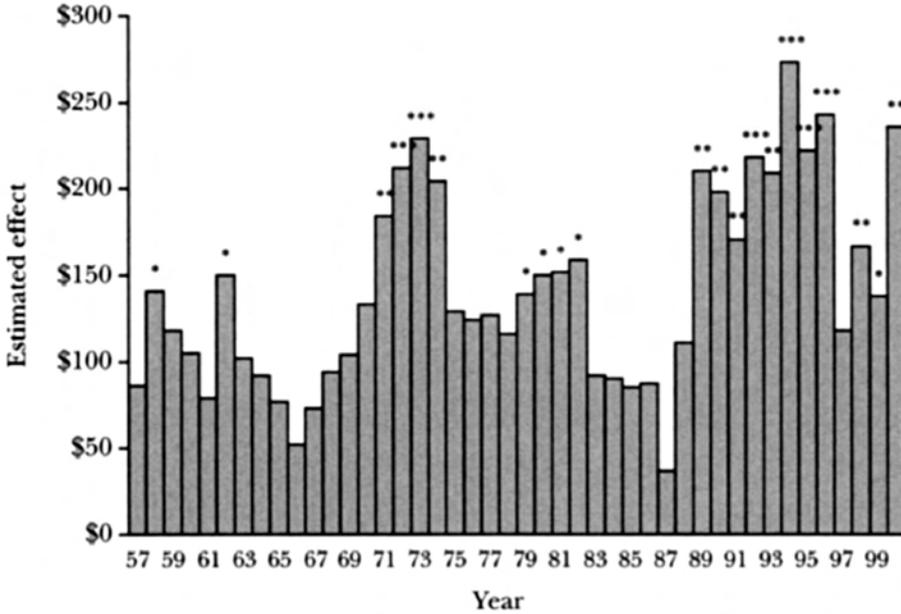
largest cities. At the state level, local initiative is more popular in the West, and is available in 77% of the cities. In the Northeast it is available in 47% of cities, in the South in 35% and 49% in Central cities (Matsusaka, 2005b). However only 35 initiatives were adopted in 1999 and 2000 compared to the 10,000 new laws adopted by the legislature (Matsusaka, 2005a). The usual issues of referenda and initiatives are tax reduction, legalization of gambling, control of alcohol sales, smoking in public places, environment, labor conditions and the denuclearization process. The economic impact of direct democracy in the U.S. is remarkable: there is higher GDP per capita in states with the initiative process (Blomberg et al, 2004), there is greater decentralization of public spending and support of the revenue mainly from dues, user fees and charges of services rather than taxes (Matsusaka, 2005b) and reductions of the state expenditure (Matsusaka, 2005a).

Graph 1 shows the difference in per capita state expenditure for each year between states using initiatives and states that do not use. For example, the first bar shows that states using initiatives spend \$ 86 less than the states that do not use initiatives for the year 1957. These numbers were calculated by a regression, which used as dependent variable the total state and local government spending per citizen. The explanatory variables included 41 year dummies equal to 1 for initiative states, dummies for 41 years, variables on income, population, population growth, population density, federal aid, urbanization and dummies for the southern and western states. The rate of initial dummy variable indicates the average amount of the reduction of costs per year due to the initiatives. The states using initiatives spend less than those not using initiatives, but this difference fluctuates over time. The first major difference opened in the 1970's when the reduction of expenses reached \$ 229 per capita, 7% of the mean. The gap was reduced during the period when initiatives began to reduce taxes (see Initiative 13), especially in the 1980's, where the differences disappeared and were not statistically significant.

Another huge gap is observed since the early 1990's, which reached \$ 273 per capita, 6% of the mean. Experience shows that reductions in costs due to initiatives appear during periods in which political and legislative power run slowly or cannot adapt to demands of voters (Matsusaka 2005a).

The State of California frequently conducts polls on economic issues, was the first U.S. state to introduce the recall (1903) and one of the two states that have recalled a governor in history (2003). In 1978 Initiative 13 was approved by the citizens. It was the first time in U.S. history that financial matter has been held in popular vote. More specifically the question was: reducing the property tax while reducing public benefits. It was decided to reduce the

**Graph 1: Estimated reduction of state expenditure year-by-year, triggered by popular initiatives in the U.S. for the period 1957-2000**



Notes: This graph shows the difference in per capita spending between initiative and noninitiative states for each year. For example, the first bar shows that initiative states spent \$86 per capita less than non-initiative states in 1957. All states are included except Alaska and Wyoming. Estimates are expressed in year-2000 dollars. Significance levels are indicated with asterisks above the bars: \* significant to the 10 percent level; \*\* significant to the 5 percent level; \*\*\* significant to the 1 percent level.

Source: Matsusaka (2005a, p.197)

property tax, set a maximum annual increase of 2% and 1% tax on the sale, while reducing public benefits. The benefits of this decision was the growing sense of security to home-owners and home-buyers due to tax stability, consolidating high reliability in the operation of income tax in the state of California and initiate similar measures to reduce taxes in several states (Lowenstein, 2010). By 2009 329 initiatives were proposed in California, of which 34% were approved, and half of them had an effect either in government spending or taxes (Matsusaka, 2010). Analysts believe that initiatives are the cause of

the state budget impasse, charging up to 70% of the budget (Economist 2009, 2011). In fact 33% of the budget addressed purposes decided upon by initiatives (32% of a single education initiative - Proposal 98) [Matsusaka, 2010]. These initiatives do not create obstacles to increases in personal income tax (except from the requirement that rates must be reformed) in California and increases in sales tax (only a small obstacle, i.e. the fact that they cannot be applied to food), which are by far the two most important sources of revenue for state governments.

In fact, the five main sources of revenue are not effectively constrained by voter initiatives. Two of the restrictions, on the contrary, increased revenues: the tax on alcohol and tobacco, the sixth most important source of revenue, were set at least at 75 cents per pack, and initiative-Proposition 37 (1984), which commissioned a state lottery in the state creating a revenue source. The initiatives that have imposed two significant obstacles in increasing taxes was Proposition 13 in 1978, where the maximum property tax rate is 1% of assessed value and limited increases, and Proposition 6 of 1982 concerning inheritance and gift taxes. Property and inheritance taxes, however, are relatively small sources of revenue for state governments. (Matsusaka 2005c).

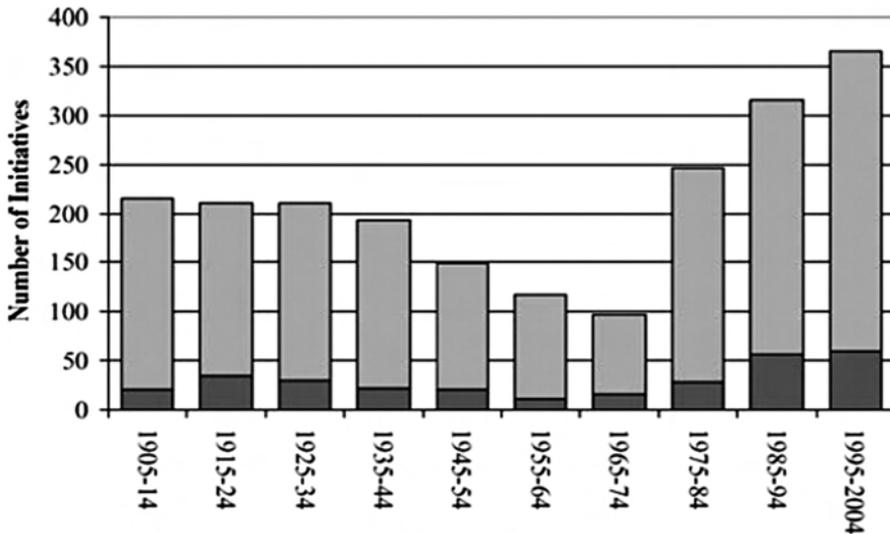
Examples of initiatives and referenda questions in California, show that the proposals for increasing taxes are routinely discarded (for alcohol, sales, fuel, road tax, income tax) while issues such as social care, employment and ensuring fiscal discipline were usually adopted (i.e. increase of 1% income tax for incomes over \$ 1 million to fund mental health services, increasing the minimum wage in all industries at \$ 5/hour to \$ 5.75 after one year, ban on accepting gifts and participation fees from political officials to the Board, submit a balanced budget every civic year, no increase of the salaries of state officials for the year of expected budget deficit, public sale of surplus property to reduce the deficit, issuing bonds to cover the state deficit)<sup>6</sup>.

Graph 2 shows the number of initiatives at the state level of the U.S. per decade starting in 1905. The use of the initiative increased in late 1970s and continued to expand over the next 30 years. During the period of 1995-2004 the number of state initiatives exceeded 360.

Table 2 shows that the restrictions are not the result of gradual accumulation of the initiatives, but rather is almost entirely the result of a single initiative, of Proposition (or initiative or proposal) 98. Without the latter, only 4% of the budget will be reserved for matters decided by initiatives. Concern about

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6 California Secretary of State - Website (2012): <http://www.sos.ca.gov/elections/ballot-measures/history-initiatives-info.htm>

**Graph 2: Number of state initiatives per decade**

Note: The number of initiatives in California is shown with dark shading.

Source: Matsusaka (2005b, p.3)

the correlation of initiatives and budget stalemate in California should be considered as concern for the proposal 98, rather than with the other initiatives.

Table 3 lists the main sources of revenue for state governments at the national level and the restrictions placed on them by the initiatives in California. These taxes, where enumerated in order of their importance to state governments at the national level, are about 75% of state revenues in general, with the remainder coming primarily from charges for services and fees.

Perhaps the most significant obstacle to revenue increase from an initiative is that Initiative 13 requires two thirds majority of the legislature to increase any tax in the state. While not technically a constraint on the legislature's ability to raise taxes—the legislature is permitted to raise any tax in any amount that it was permitted to raise before voters approved the initiative—this requirement certainly increases the degree of consensus required to raise taxes, and complicates the underlying politics.

**Table 2: State expenditure of California, triggered by initiative decisions, for the period 2009-2010**

<i>Year</i>	<i>Proposition</i>	<i>Description</i>	<i>\$ Billions</i>
1988	98	Education	34.66
2004	63	Millionaire surtax for mental health services	1.752
2002	49	After school programs	0.55
1998	10	Early childhood development	0.528
2000	21	Juvenile crime [for prisons]	0.449
1994	184	Three strikes and you're out [for prisons]	0.434
1988	99	Tobacco tax [funds for anti-smoking, wildlife, research]	0.286
2002	50	Water projects bonds [authorized \$3.44 billion]	0.228
2006	84	Water bonds [authorized \$5.388 billion]	0.132
1990	116	Rail bonds [authorized \$1.99 billion]	0.101
2004	71	Stem cell research bonds [authorized \$3 billion]	0.092
2004	61	Childrens' hospitals bonds [authorized \$750 million]	0.07
1990	117	Wildlife protection	0.03
2008	3	Childrens' hospitals bonds [authorized \$980 million]	0.029
1988	103	Auto insurance [administrative spending]	0.027
1988	70	Natural resource preservation bonds [authorized \$776 million]	0.021
1988	97	Cal/OSHA	0.01
1974	9	Political reform [California FPPC administration]	0.004
1990	132	Gill net ban [enforcement spending]	0.002
1986	65	Toxic discharge [enforcement spending]	0.002
<b>Total appropriation by initiatives</b>			<b>39.407</b>
<b>Total state expenditures (excluding federal funds)</b>			<b>119,244.90</b>

Source: Matsusaka (2010)

**Table 3: Restrictions on major state revenue sources, triggered by decisions of initiatives in the state of California for the period 2009-2010**

<i>Revenue source</i>	<i>Percent tax revenue nationwide</i>	<i>Constraints</i>	<i>Initiative</i>
<b>Taxes</b>			
Personal income.....	35	Minimum 1% surtax on millionaires	Proposition 63 (2004)
Sales (general).....	31	Prohibited on food	Proposition 163 (1992)
Corporate income.....	7	None	
Gasoline.....	5	None	
Alcohol & tobacco.....	3	At least 75¢/pack	Proposition 99 (1988), Proposition 10 (1998)
Property.....	2	No more than 1%	Proposition 13 (1978)
Death & gift.....	0.7	Prohibited	Proposition 6 (1982)
<b>Charges</b> .....	...	None	...
<b>Lottery</b> .....	...	Required	Proposition 37 (1984)

Source: Matsusaka (2010)

## 4.5 The case of Latin America

In Latin America the decade of 1980 was characterized by the return to democratic governance after a prolonged period of authoritarian and military regimes. However, the hopes of many people that representative democracy would better serve their interests, were false and dissatisfaction with political parties and representative government grew (Kaufmann et al., 2010). This disappointment in broad sectors of the population contributed to the emergence of more direct democracy in Latin America, as had happened in Switzerland in the second half of the 19th century and the U.S.A. around the late 19th / early 20th century. However, strong popular demands for direct democracy are not widespread, with the exception of Bolivia. In Latin America, most of the new constitutions adopted since the late 1980's included direct-democratic rights but also referenda top down (plebiscites) and sometimes the right of recall (e.g. Bolivia, Colombia, Peru and Venezuela).

Regarding direct democracy, Latin America can be divided (*op.cit.*) in three categories (see Figure 3). 1) In countries where direct democracy has been consolidated and regularly used. Uruguay can only be placed in this category. 2) In countries where direct democracy was newly established and has been used rarely or not at all. Apart from direct democracy, referenda top down were introduced (or already exist) and the last are used more often. Bolivia and Venezuela are examples that fall into this category. 3) In countries where direct democracy is not yet up and top down referenda have not been used since 1978.

Countries in this category are Cuba, Dominican Republic, El Salvador, Honduras, Mexico, Nicaragua and Paraguay. 108 popular votes took place in Latin America between 1978 and 2009, of which only 15 came from citizens' initiatives or referenda. Out of these 15 bottom up proposals, 12 were held in Uruguay (7 popular referenda and popular initiatives 5), 1 popular initiative took place in Bolivia and 2 consultative popular initiatives in Colombia. Apart from the previous procedures there were 2 recall elections (1 in Bolivia and 1 in Venezuela), 3 authorities' minority initiatives (all in Uruguay), 21 obligatory referenda and 69 referenda top down.

Uruguay is the only Latin American country with a long tradition of effective use of direct democracy, and as such is a special case (*op.cit.*). It is one of the few countries which adopted the Swiss model of direct democracy. Therefore it applied the following types of process: mandatory referendum, popular initiative with counter-proposal, authorities' minority initiative and referendum on constitutional amendments. Issues that have been put before citizens and

finally have been approved are the privatization of telecommunication company, the protection for pensioners, the repeal of the law on privatization of the oil company ANCAP and the definition of water as a natural resource essential to life and access to it as a fundamental human right (Madronal, 2005). As in Switzerland, in the same way in Uruguay the authorities do not have the right of the top down referendum. Comparing Switzerland and Uruguay, we can observe some differences. In Uruguay, direct democracy was introduced from above (top down-decided by the leaders) in a highly centralized state (Altman, 2008). In Switzerland, the same happened in a strongly decentralized federal state and from below (bottom up).

Although both countries use referenda and popular initiatives in a normal manner, the legal design of these instruments varies significantly. In Switzerland, 2% (1%) of the electorate can start a popular initiative (referendum), while in Uruguay the consent of 10% (25% for referendum) of the electorate is necessary. In practice this means that the tools of direct democracy in Uruguay are made only for powerful actors, whereas in Switzerland weak groups can also use them. This is one reason why direct democracy is used much more in Switzerland than in Uruguay.

## **5. The Case of Greece**

### **5.1 Existing Situation**

Eight referenda of constitutional character have been conducted in Greece from 1862 to 1974. Greek Constitution provides only top down referenda. More specifically, Article 44 provides two types of referenda (top down):

- For critical national issue (activated after a proposal from the government and requiring acceptance by the absolute majority of Members of Parliament to undergo for vote).
- For voted bills regulating important social matters, except financial issues (activated after the proposal of 2/5 of Members and requiring acceptance by 3/5 of the Members to vote). The result is binding if: there is attendance of 40% of the electorate in the first case and 50% for the second case (L.4023/2011).

### **5.2 Critical areas of the Greek economic and political field**

In Greece, where public debt is high (142.8% in December 2011, 127% in

**Figure 3: Use of direct democracy in Latin America countries in national level**



Source: Kaufmann et al. (2010, p.223)

March 2010 before the country referred to the support mechanism of the EU and IMF, resulting in the automatically increase of the debt) an introduction of bottom up initiatives is necessary. The problem of the tax evasion is also acute in Greece. The labyrinthine tax regulations by the repeated vote of new financial laws, the complex institutional framework for setting up and operating businesses and corruption are extensive as well. The element that affects the situation is that sometimes the support of the reforms is weak.

The main weaknesses of the Greek economy were due to the distorted

development model that dominated the last decades. It was a model that relied on domestic demand, public and private, and fueled by government and households borrowing. The business sector has failed to adequately benefit from the opportunities provided by membership in the euro zone, while the enhanced expectations of households because of the integration and the soaring of public sector encouraged consumerism. The results were: negative net national saving from 2002 to date and continuous transfer of resources from the private sector to the hypertrophic and low productivity public sector. This model favored present consumption against the future one and was based on the illusion that sustained growth could come from the public sector. The rise in consumption, characterized by strong propensity to consume imported goods, encouraged and supported a “shallow” domestic entrepreneurship, which was oriented to the distribution sector and the consumer. But as the factors that supplied the consumption have been confounded, it was inevitable for this form of business to suffer. At the same time the conditions to encourage entrepreneurship in new sectors instead of old, oriented in a new development model have not yet been created (BoG 2011, p.22). The new development model that will pull the economy from the crisis, implies an increase in the share of investment and exports to GDP and reducing the share of private and public consumption, a substantial increase in savings (so that the net national saving from negative becomes positive), turning the entrepreneurship to the competitive field of production-oriented to international markets-, and public administration that will not deter investment or tolerate or encourage tax evasion (op.cit, p.38).

The evolution of public debt, which ranges over the last fifteen years at levels higher than 99% of GDP, combined with existing structural rigidities are the strongest sources of macroeconomic imbalances that led to a profound crisis of the Greek economy (see Table 4). Although the rapid growth from 2000 until the start of the crisis combined with low interest rates until 2005, primary surpluses by 2002 and revenues from privatization mainly from 1996 onwards, it was not possible to halt the upward trend of debt. Instead, the significant shortfall in tax revenues and increased spending in recent years through 2009 created heavy demand for new borrowing, boosting the country’s dependence of the developments in capital markets, while at the same time highlighting the structural problems in both the tax collection mechanism and the mechanism of control and containment of costs.

Unemployment rate in October 2011 amounted to 18.2% versus 13.5% in October 2010 and 17.5% in September 2011, according to the Labour Force Survey of the Hellenic Statistical Authority. The number of employed in October 2011 was estimated at 4,065,775 people. The unemployed amounted

**Table 4: Debt of general government to GDP ratio**

2002	2003	2004	2005	2006	2007	2008	2009	2010
101,7	97,4	98,9	109,0	106,1	105,1	110,3	126,8	142,5

Source: BoG (Bank of Greece) 2011, p. 132

**Table 5: Corruption Perceptions Index in selected countries for year 2009**

Position	Country	Index	Position	Country	Index
1	New Zealand	9,4	19	USA	7,5
2	Denmark	9,3	27	Cyprus	5,2
3	Singapore	9,2	61	Turkey	4,4
4	Sweden	9,2	71	Greece	3,8
5	Switzerland	9,0	79	China	3,6
6	Finland	8,9	84	India	3,4
6	Holland	8,9	95	Albania	3,2
8	Australia	8,7	106	Argentina	2,9
8	Canada	8,7	146	Russia	2,2
8	Iceland	8,7	179	Afghanistan	1,3
11	Norway	8,6	180	Somalia	1,1

Source: Transparency International, Global Corruption Barometer 2009.

to 903,525 persons, while the economically inactive population reached 4,382,356 people. The number of employed decreased by 303,768 persons compared with the respective number in October 2010 (7.0% reduction) and

increased by 14,666 persons compared with September 2011 (0.4% increase). The unemployed increased by 219,478 persons compared with October 2010 (32.1% increase) and 45,869 persons compared with September 2011 (5.3% increase).

Table 5 presents some of the 180 countries ranked according to the perceived degree of corruption in them, for the year 2009, by the international non-governmental organization Transparency International. The grading scale is from 0 to 10 where 0 indicates the degree of the greatest corruption, and as the ratio increases there is the sense that there is no corruption in the country. Although this indicator is not the result of objective quantitative measurement of corruption it is very important because it reveals that how the phenomenon is perceived. Greece is ranked for year 2009 in the 71<sup>st</sup> position of purity of the public sector (public administration, politicians and the general public field) in the world. There were 70 countries that were deemed to have a less corrupt public sector.

Of particular importance to investigate and address the phenomenon of corruption in a country is the general perception that has been formed regarding which institutions are considered the most corrupt in the country. Transparency International in opinion polls, whose results are published in the Global Corruption Barometer, analyzes the views of the public towards corruption and bribery experiences. The Global Corruption Barometer report for 2009 covers 69 countries, while the range of indices takes values from 1 (not at all corrupt institutions) to 5 (extremely corrupt institutions). Table 6 shows the perception of corruption of individual institutions in 2009 in selected countries.

An overview of the table shows that in Greece the political parties are regarded as the institution with the highest corruption in the country, which is estimated to be among the highest worldwide. Of the 69 sample countries, only Bolivia and Panama is estimated to be associated with a higher degree of corruption of political parties than Greece, while Ukraine is considered to be associated with higher average level of corruption in the institutions (higher average scores) on all 69 countries. A concrete example is the substantial elimination of the equality (isonomy) with the unequal treatment between citizens and politicians, which occurs under the guise of Article 86 and Article 62 of the Constitution that state that ministers are liable to persecution only by Parliament and Members of Parliament have the non-persecution right and crimes barred after the parliamentary session, respectively. The revision of the Constitution by adding a section that increases the degree of political control and making them accountable essentially, is essential to ensure a fundamental aspect of democracy: equality before the law.

**Table 6: Perceptions for institutions affected by corruption in selected countries, year 2009**

<b>Country</b>	<b>Political Parties</b>	<b>Parliament / Legislature</b>	<b>Businesses / Private Sector</b>	<b>Media</b>	<b>Public Servants</b>	<b>Judiciary</b>	<b>Average</b>
Denmark	2,6	2,1	2,9	2,8	2,3	1,7	2,4
Singapore	2,1	1,8	2,7	2,5	2,2	1,8	2,2
Switzerland	2,9	2,6	3,2	3,1	2,5	2,2	2,8
Finland	2,9	2,5	2,8	2,6	2,1	1,9	2,5
Holland	2,6	2,3	3,1	2,8	2,7	2,3	2,6
Canada	3,5	3,2	3,4	3,1	3,1	2,7	3,2
Iceland	3,9	3,1	4,3	3,5	3,4	2,7	3,5
Norway	3,1	2,7	3,8	3,5	3,2	2,5	3,1
USA	4,0	3,9	3,7	3,7	3,7	3,2	3,7
Turkey	3,4	3,4	3,6	3,4	3,6	3,3	3,5
Greece	4,4	3,7	3,4	3,8	3,7	3,4	3,7
India	4,2	3,6	3,4	2,9	3,7	3,2	3,5
Argentina	4,4	4,2	3,7	3,3	4,3	4,2	4,0
Russia	3,9	3,9	3,7	3,5	4,5	3,9	3,9
Bolivia	4,5	4,2	3,4	3,3	4,1	4,4	4,0
Panamas	4,6	4,6	3,3	2,8	4,3	4,4	4,0
Ukraine	4,4	4,5	4,3	3,8	4,5	4,5	4,3
Total of 69 countries	3,9	3,7	3,5	3,2	3,8	3,5	3,6

Source: Transparency International, Global Corruption Barometer 2009.

The principal agency problem (see also section 2) appears strongly in the current economic and political situation in Greece, as of the last elections in October 2009 to January 2012, have passed critical economic reforms, without the approval of the people.

The democratic deficit increased after 2009, when the new government which was elected under its promise for the provision of increased social benefits etc., totally reversed its policy and adopted the harshest austerity measures program after 1974, often being forced to apply for aid from the EU and the IMF. The Greek government practically agreed on measures introduced by the Troika (EU, ECB<sup>7</sup>, IMF), which obviously had no citizens approval, even though they might have been necessary. This could be interpreted as a major case of the agent-principal problem.

Undeniably the lack of bottom up direct-democratic processes are evident in Greece, as it is not provided: the initiative of citizens to propose new law, the referendum bottom up for adoption or not of a policy or a law, as well as the ability for authorities' minority referendum (such as the Municipality, the Parliament, the councils of organizations and institutions) to cause a referendum on the final adoption of a law. The institution of recall could also be adopted in order to enhance transparency and avoid corruption.

### **5.3 Suggested economic policy issues for initiatives or referenda bottom up in Greece**

Economic and coherent policy issues that could be put on initiatives or referenda bottom up in Greece are:

- Simplify tax procedures
- Stable tax system
- Fairer tax rates
- Establish strong mechanisms to confront tax evasion
- Fighting corruption and introducing stricter measures on the perpetrators
- Amend the Law of ministerial responsibility
- Strengthening of public free education and elimination of shadow education system
- Strengthening the public health and elimination of extra medical fees (sachets)
- Complete liberalization of closed off professions
- Eliminate permanence for civil servants

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7 European Central Bank.

- Reduction public sector with parallel reduction of tax rates

Due to the facts that Greece has requested aid from the EU and IMF support mechanism, and also implementing the medium-term program agreed in summer 2011 and in early 2012 signed the new loan (EUR 130 billion) initially agreed on 26/27 October 2011 and completed the exchange of bonds of private investors (PSI-Private Sector Involvement- “haircut”), it is considered crucial to the future for the Greek economy that these procedures are “legitimized” by being accepted through some democratic procedure, like a referendum, by the citizens. The crisis of confidence in the Greek economy began to increase due to elusive deficit rate of 15.5% for 2009 and this led the markets to eject the spreads to 500 and 1000 basis points and gradually overcome the 3000 basis points in January 2012 (Naftemporiki, 2012). Questions concerning this matter that could be put to popular vote are:

- Signature of new loans while increasing collection of revenue measures
- Remaining in the euroarea or not

#### **5.4 Impact of stronger direct democracy in Greece**

The effects of the introduction of stronger direct-democratic mechanisms in the Greek economic and political field could be the following:

- Increase state tax revenues by reducing tax evasion
- Increase the accountability of public rulers
- Create a stable and attractive business environment
- Creating new jobs
- Increase of growth in terms of GDP and per capita GDP
- Increase of the sense of social justice and equality, which affects productivity
- Valorization of proposals of citizens that could not be conveyed otherwise
- Create an image of the country that gains the trust and confidence of partners and markets

## **6. Conclusions**

Democracy was born in ancient Athens. The form that characterized this was direct democracy, i.e. the direct participation of citizens in public affairs. Over the centuries, democracy returned in the form of indirect (representative) democracy. In recent decades, the addition of elements of direct democracy in the governance of countries worldwide has increased. The benefits of direct democracy act as an incentive to adopt direct-democratic mechanisms such as the referendum, initiative and recall, in the governance of the country. Direct

democracy is increasing interest for citizenship, faces difficult issues that lawmakers often avoid, promotes accountability of officials, safeguards transparency, reduces corruption, uses non-violent means of popular participation and creates a positive influence on economic growth. The increasing participation of citizenship increases the chance for consensual arrangements and pushes participants to favorable activities for the common welfare (Schmidt, 2000).

Switzerland is the world leader in the use of direct democracy mechanisms, presents lower government costs, increasing prosperity and reduction in the extreme inequalities of wealth, increase in per capita GDP of 15%, decrease in avoidance rate of 30%, reduction of the public debt at the local level. Significant use of direct democracy mechanisms is practiced in Germany and the U.S.A., only at regional and local level. Germany at the Länder (state) and municipalities level and U.S.A. at state level and municipal level. Despite the frequent use of referenda in the Länder of Germany, economic and financial topics are not permitted. In the U.S.A. to conduct popular votes for taxation and finance social policies is very common. Initiative 13, which was approved in 1978 in California and involved the stabilization of property tax, is a milestone for citizen participation in economic activities.

During the last 30 years voting on financial matters has highly increased. Some analysts argued that the frequent use of such voting is the cause of the financial crisis in California. But a closer investigation of the data showed the costs incurred by the establishment of citizen initiatives, reflect the 33% of the budget of the State of California and especially the 32% comes from the needs created by a single initiative (for education).

In a period of about 40 years (1957-1999), it is estimated that the costs arising from decisions triggered by popular initiative, for each U.S.A. state using direct-democratic mechanisms declined substantially, reaching 6% and 7% for some years, compared with states that have not active similar mechanisms. The states that allow initiatives rely less on taxes and more on user fees and service charges and distribute the government spending in much more decentralized levels. The effect of direct democracy on economic growth is provided by the increase in per capita income (Blomberg et al., 2004).

In Greece the use of direct democracy is very negligible. Only 8 referenda were held over a period of 110 years (1862-1974) and during periods of non-constitutional normality. The Greek Constitution (Article 44) provides only the use of the top down referendum on national issues or voted bills regulating important social matters (other than financial). Recently, Law n. 4023/2011 set the details for a referendum. The percentage of citizen participation in the process, over which the referendum decision is binding are 40% for national

issue, 50% voted for a voted bill. It is obvious that the existing legislation in Greece is not conducive to extensive use of direct democracy, and thus to obtain its benefits. The absence of a provision for submitting a referendum for issues of financial interest, the lack of means of initiative and recall, and the differences in thresholds for citizen participation in setting the outcome of the referendum binding or not, are issues hindering the development of positive effects of direct democracy and perpetuate many of the distortions in the public and private life and the economic process. These distortions relate to the increased presence of corruption, in high public debt, in a large and unproductive public sector, the unattractive business environment, the democratic deficit that concerns the equal treatment of citizens and officials and the widespread tax evasion. The adoption of initiatives and referenda that will come from the people can be put before citizens and address the issues of these distortions. The mechanism of recall could help to reduce corruption, increase accountability and safeguard transparency. The revision of the Constitution by adding a section that will increase the degree of political control and making politicians essentially accountable is imperative to ensure a fundamental aspect of democracy: equality before the law (isonomy).

It is now generally accepted that the problems of governance, economic policy, corruption and economic performance of a country are linked closely. Often, solving one of them depends on addressing another and the deterioration of some of these often occurs as a result of the deterioration of others.

Greece is a country according to existing estimates that is considered democratic, but has the biggest corruption perception indicators in the euroarea, while it is among the countries with the lowest per capita income, even when that is expressed in units of constant purchasing power. From the above analysis we deduce that the effective mitigation on corruption in Greece will have a major impact on economic growth. Thus the appropriate developmental policies of governments must contain as one of its main axes, a substantial reduction in corruption. The fact that political parties are regarded as the institution with the highest corruption in the country and also is one of the largest worldwide, suggests that effective control of the phenomenon cannot be achieved without the appropriate structural changes in the existing system.

To sum up, direct democracy increases economic growth, reduces corruption, debt, income inequalities and enhances the accountability of officials. Taking under consideration the benefits of direct democracy, we conclude that the introduction of bottom up mechanisms of direct classic democracy in Greece will improve economic performance.

Suggestions for further research could be a field survey on the need for

popular initiatives in Greece, recording desired future referenda questions and the possibility of the increase of citizen participation in public affairs. The influence of direct democracy in the legislature is another future research field. Finally, the opposite issue of this paper may be researched, i.e. if economic growth increases the level of democracy and reduces the degree of corruption.

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# THE DEVELOPMENTAL PATH TO RECOVERY: A RADICAL APPROACH AT THE GREEK PROBLEM

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## Abstract

This paper presents and critically discusses the origins and causes of the Greek fiscal crisis and its implications for the euro currency. In the aftermath of the 2007-2009 financial crisis the enormous increase in sovereign debt has emerged as an important negative outcome, since public debt was dramatically increased. Although Greece is the country member of the Eurozone that has been in the middle of this ongoing debt crisis, since November 2009, this negative situation of the increasing debt leads the Greek government to happily accept a rescue plan of 110 billion euros designed and financed by the European Union and the International Monetary Fund (IMF). A lengthy austerity programme and a fiscal consolidation plan have been put forward and are to be implemented for the next three years (for the period 2010-2013). Then, we present an analytical reference of the three major problems of the Greek economy: the problematic productive structure, the increasing shadow economy and the existence of corruption in public administration. The lack of quality institutions led to distortion of incentives in the country and poor distribution of existing talent. Basically, all these factors highlight the need for developing successful negotiations at the forefront of the Greek and European scene in order to ensure the rights of Greece's workforce to the extent possible. The present paper attempts to analyze the catalytic role of the four forces which lead to social and economic development during a period of continuous changes in the political, social and economic life of Greece but also the entire European scene.

*JEL Classification:* H30, H63, H83

*Keywords:* Crisis, Greek debt crisis, the Tripartite Mechanism of Support, Troika, Corruption, Shadow Economy, Recession, Negotiations, Win-Win, S.W.O.T Analysis, PESTEL Analysis, Development Policies, Recovery.

## 1. Economic crisis

After the outbreak of market prices of houses in the U.S. (August 2007) and the crisis' contagion worldwide from October 2008, is a global event that

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brought changes in everyday life of millions of people, in the function of banks, businesses and governments. One of the key features of the capitalist economic system is the crisis that occurs at regular intervals, as a feature of the economic cycles. In the past, an economic crisis was usually defined as the frustration of human endeavor, due to the adverse weather conditions, diseases and epidemics, and wars among other causes. But after the development of industrial production, the ripening and the spread of capitalism in the world economy through the process globalization and the rapid development of technology, economic crisis is defined as the overproduction or oversupply of goods and services (overheated economy), or the lack of the corresponding demand. This means that consumers cannot buy either because of insufficient income, either due to unemployment or anything else. The result of the reduction in demand leads to a vicious circle, since the industrial production is reduced, while reducing staff and cutting or "freezing" the wage level, and companies at the same time require less labor, fewer raw materials and less transport. The demand of less personnel leads to an increase of unemployment and thus further reduces the purchasing power of the public. As a result, this vicious cycle is inflated and spreads internationally with a consequent reduction of imports and exports and a reduction of international trade<sup>1</sup>. Generally, there are four stages of an economic crisis<sup>2</sup>:

1. The configuration of the current condition
2. The crisis' peak
3. The effects of crisis
4. The resolution and normalization of the economic system from the crisis

Simultaneously, the term of the economic crisis can be characterized by the descent phase and the continuing contraction of the economic activity. Economic crisis is a phenomenon in which an economy is in a lasting and significant decline of the economic activity. When we discuss about the economic activity we refer to all the economic aggregates such as employment, national output, prices, investments, etc. The key indicator of economic activity is the "investments"<sup>3</sup>. The phases of the economic fluctuations are two: the descent phase and the phase of the cathode. The economic crisis is one part of these two phases, the, the contraction of the economic activity. The market and the economy are unexpectedly changing as social and economic globalization and technology have made their appearance. In the conditions of an unfavorable

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1 Kaminsky, G.L. (2003), Varieties of Currency crisis, NBER working paper, No. 10193

2 Sfakianakis, MK (1998), Crisis Management, Ed. "Ellin", Athens

3 Theodorou, Th. (2010), "the economic crisis", [http://www.alfavita.gr/artra/art13\\_7\\_9\\_0703.php](http://www.alfavita.gr/artra/art13_7_9_0703.php)

economic environment, emerge some important changes in market conditions. A sharp drop in demand leads to changes at the projected sales and generally at the whole plan. The economic crisis brings to the forefront all the wrong mechanisms and becomes the foundation of a new theory to correct the past one<sup>4</sup>. History teaches us that since it is a recurring phenomenon, there is a common sense and a common workaround. The crisis terminates the cycle and then the whole system until is in a new type of development.

### **1.1 The Greek Fiscal Crisis: Brief history and analysis**

The Greek government-debt crisis is one of a number of current European sovereign debt crises. "In late 2009, fears of a sovereign debt crisis developed among investors concerning Greece's ability to meet its debt obligations due to strong increase in government debt levels<sup>5</sup>. This led to a crisis of confidence, indicated by a widening of bond yield spreads and the cost of risk insurance on credit default swaps compared to the other countries in the Eurozone, most importantly Germany"<sup>6</sup>. The Greek government's reliance on borrowing from international capital markets to pay for budget deficits and trade deficits left it vulnerable to shifts in investor confidence. If investors lost confidence in the Greek government's ability or willingness to repay its debt, they would stop lending to the government or charge interest rates that were higher than what the Greek government could afford. Lack of access to new funds would make it difficult for the government to borrow to repay existing debt as it became due (called rolling over its debt), meaning that the government would have to implement austerity measures quickly or risk defaulting on its debt. Starting in 2009, investor confidence in Greece's ability to service its debt dropped significantly. The global financial crisis of 2008-2009 and the related economic downturn strained the public finances of many advanced economies, including Greece, as government spending on programs, such unemployment benefits, increased and tax revenues weakened. Greece's reported public debt rose from 106% of GDP in 2006 to 126% of GDP in 2009<sup>7</sup>. Additionally, in

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4 Theodorou, Th. (2010), "the economic crisis", [http://www.alfavita.gr/artra/art13\\_7\\_9\\_0703.php](http://www.alfavita.gr/artra/art13_7_9_0703.php)

5 Higgins, M., Klitgaard, Th. (2011), "Saving Imbalances and the Euro Area Sovereign Debt Crisis", *Current Issues in Economics and Finance* (Federal Reserve Bank of New York), Vol.17, no.5. Retrieved 5 April 2012.

6 "Gilt yields rise amid UK debt concerns", *Financial Times*, 18 February 2010. Retrieved 15 April 2011.

7 International Monetary Fund, *World Economic Outlook*, April 2011. Debt for all levels of government (local, state, and central governments), and is gross debt (total financial

late 2009, the new government, revealed that previous Greek governments had been under-reporting the budget deficit. The new government revised the estimate of 2009 budget deficit from 6.7% of GDP to 12.7% of GDP<sup>8</sup>. This was shortly followed by rating downgrades of Greek bonds by major credit rating agencies. Allegations that Greek governments had attempted to obscure debt levels through complex financial instruments contributed further to a drop in investor confidence<sup>9</sup>. Greece's 2009 budget deficit was subsequently revised upwards a number of times, finally to 15.4% of GDP. As investors became increasingly nervous that the Greek government's debt was too high, and that it would default on its debt, they started demanding higher interest rates for buying and holding Greek bonds.

In mid-2010, and after revelations that the budget deficit of Greece which ended in 2009 at levels above those that would make debt sustainable, Greece was unable to borrow at reasonable rates from the market in order to finance the current government deficit and debt refinancing. The result was an imminent threat of bankruptcy and the suspension of the Greek Public Sector's payments. The attempt to regain the country's credibility in the international markets and achieve lower interest rates, led to measures to reduce costs, which were inefficient to reverse the negative climate. After these, Greece resorted to the help of the International Monetary Fund, the European Union and the European Central Bank, which constituted the support mechanism of Greece. The funding from the support mechanism was subject to conditions that Greece will take fiscal adjustment measures, particularly under conditions that will take fiscal consolidation. By funding from the mechanism the immediate danger of Greece's bankruptcy was averted. The first measures were announced on May 2, 2010. The Greek economy remained in fiscal imbalance situation and one year later, in June 2011, the government resorted to the adoption of medium-term program, which included new austerity measures and cuts. Also it was raised an issue of exploiting the public property and restructuring or "haircut" the debt in order to achieve a long-term debt reduction to sustainable levels. On May 3, 2010, Greece requested €80 billion from the rest fifteen countries and €30 billion from the IMF. This request was accompanied by three attached memoranda: the "Memorandum of Economic

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liabilities), rather than net debt (total financial liabilities minus total financial assets).

8 "Is Greece Heading for Default?," Oxford Economics, January 29, 2010.

9 For example, see Kerin Hope, Quentin Peel, and Tony Barber, "Greece Turns on EU Critics," *Financial Times*, February 13, 2009; Louise Story et al., "Wall St. Helped to Mask Debt Fueling Europe's Crisis," *New York Times*, February 14, 2009

and Financial Policy”, the “Technical Memorandum of Understanding” and the “Memorandum of Understanding on Specific Economic Policy Conditions”. On May 8, 2010, the “Loan Facility” and the “Settlement of Funding Immediate Readiness” with the IMF were approved. Then, it was created a group of representatives of the European Commission and IMF, called Troika, which evaluated quarterly the progress of the implementation of the Memorandum’s terms and made decisions on the disbursement of the relevant loan installment.

## **1.2 Searching for the “emergency exit”: The Tripartite Mechanism of Support, the “Troika”.**

Three international institutions might help prevent a Greek fiscal collapse: The European Council, comprised of heads of EU member states; the European Central Bank (ECB), a politically independent arm of the EU; and the International Monetary Fund (IMF), the global financial rescue team. These three institutions came to be known as the “Troika”. This word, meaning triumvirate in Russian, referred to notorious panels of judges who had condemned dissidents in the Stalinist era.

The Greek crisis presented the EU in its worst dilemma since the creation of the euro. The problem was especially difficult since the Maastricht treaty explicitly forbade bailing out member states through others' assuming their debts<sup>10</sup>. Thus, any solution would have to be invented on the fly, and- since it would de facto alter the treaty-would have to be approved by the Council of Ministers, particularly by the 17 euro area nations that would shoulder most of the costs<sup>11</sup>. Greece's repeated statistical misstatements and failure to tackle its other problems did not help its case. Nations outside the euro area, notably Britain, ruled out participating in a rescue, and a group in the euro area

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10 See European Union, Consolidated versions of the treaty on European Union and of the Treaty Establishing the European Community, Part Three (Community Policies), Title VII (Economic and monetary policy), Chapter 1, (Economic Policy), Article 103, section 1: "The Community shall not be liable for or assume the commitments of central governments, regional, local or other public authorities, other bodies governed by public law, or public undertakings of any Member State, without prejudice to mutual financial guarantees for the joint execution of a specific project". Official Journal of the European Union, C 321 E/84, 29.12.2006. <http://www.eurointelligence.com/uploads/media/ConsolidatedTreaty.pdf>, accessed Jan.25, 2011.

11 On the point that loans to Greece did de facto alter the treaty, see Ben Hall, "French Minister says bail-out alters EU treaty", Financial Times. FT.com, May 27, 2010, accessed Jan. 25, 2011.

was reluctant. Germany feared it would bear the brunt of the cost of Greek aid. German tabloids conducted a virulent campaign against a bailout calling Greece 'lazy' or suggesting it leaves the euro. Fears of moral hazard were widespread: if the EU bailed out Greece, what would stop other governments from spending recklessly and expecting to be rescued? Germany's representative on the executive board of ECB, Jürgen Stark, feared that a possibly expensive rescue "would give the wrong incentives and would burden countries with more solid public finances"<sup>12</sup>. However, France and several other nations in the euro area supported assisting Greece. Moreover, the EU might have to support Greece to sustain the euro and the European ideal. Already the euro accounted for 37% of global foreign exchange truncations and Europe hoped it would prove an alternative to the U.S dollar as a reserve currency<sup>13</sup>. But as fears of default spread to Portugal, Ireland, Spain, and, to a lesser extent, Italy, they created a spike in bond yields. In varying degrees, these countries also suffered from high public debts and current- account deficits. If markets progressively denied them access to refinancing as well, the euro area could be plunged into a potentially irreversible crisis. From a value of \$1.50 in October 2009, the euro fell to \$1.20 by mid-June. Already some Baltic States that had been preparing to adopt the euro were growing less enthusiastic about the idea<sup>14</sup>. EU members also had self- interested reasons to support Greece. Euro area banks, mostly in France and Germany, were estimated to hold €60 to €120 billion of Greek government bonds; other banks, mainly in European nations such as the United Kingdom and Switzerland outside the euro area, were estimated to hold another \$40 to \$80 billion of the bonds<sup>15</sup>. A Greek default could spark wider financial panic, a catastrophic prospect for a banking system still reeling from the effects of the global financial crisis. State rescues of the banks might well cost more than a loan to Greece.

The ECB's role was to maintain price stability and act as a lender for euro area banks. It found itself as the only independent EU authority that could act quickly in response to the crisis. The ECB had several standard financing tools. It used its weekly main refinancing operations (MRO's) to influence the rate at which banks lent to and borrowed from each other overnight. It set a minimum

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12 Jürgen Stark, Editorial, *Handelsblatt*, March 8 2010.

13 European Central Bank, "The international role of the Euro", July 2008, <http://www.ecb.int/pub/pdf/other/euo-international-role200807en.pdf>

14 Kramer, A. (2010), "Greece's Woes May Give Pause to Euro Zone Candidates", *New York Times*, accessed 11-02-2010

15 Still in a spin", *The Economist*, Apr. 17, 2010, particularly the chart "What's in the Vaults?" <http://www.economist.com/mode/15908288>, accessed 19-02-2011

interest rate, assessed the market's liquidity need, and determined the volume of funds to offer its loans with weekly maturities against qualified collateral. Banks bid for these loans, those that offered the highest rates receiving loans until the allotted funds ran out. The ECB also conducted long term refinancing operations (LTROs) that worked similarly but had a maturity of three months. Finally, the ECB had two overnight facilities to put a cap and floor on interest rates. Banks could deposit idle funds at an interest rate normally lower than the overnight rate in the interbank market. And banks in trouble that could not borrow from their peers could use a "marginal lending facility", posting collateral to obtain overnight liquidity at a rate normally higher than that of the interbank market. As the global financial crisis began to spread, the ECB first conducted an expansionary monetary policy by lowering its benchmark rate on MROs to 1%. After the collapse of Lehman Brothers, it introduced non-standard measures. Now it no longer fixed the volume of loans it would make in the MROs but set an interest rate and loaned all the funds banks requested at that level. It also introduced loans in its LTROs with longer six-month and one-year maturities to give banks more breathing space. Finally, after October 2008 the ECB broadened the range of assets it would accept as collateral against short term loans to national banks, extending it to paper rated BBB-. The ECB announced it would reverse these non-standard measures by the end of 2010.

The IMF provided loans to governments of nations in financial trouble, contingent on reforms- "conditionalities"- intended to address the underlying causes. It disbursed loans over time in "tranches", after verifying that promised reforms were being implemented on schedule. In dealing with debt crisis as in Asia in 1998-1999, the IMF carried a reputation for imposing excessive fiscal austerity and being politically insensitive. In the absence of major crisis it had been dormant since the early 2000s, but in 2009 was granted significantly greater resources to deal with effects of the global financial crisis. Under the leadership of Dominique Strauss Kahn, it became what Business Week called a "kinder and gentler" IMF, less obsessed with fiscal austerity and more concerned about social safety nets<sup>16</sup>. The IMF had never lent to euro area nation. It made emergency loans to Hungary, Latvia, Romania, and Iceland in the wake of the global financial crisis, but the last time it had intervened in a core western European country dated back to 1976, when it gave assistance to Great Britain.

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16 Levine, S. (2008), "The IMF is Back, Kinder and Gentler", Business Week, Nov.10, 2008.

## 2. The “heart” of the problem

Greece is a developed country with a high standard of living and "very high" Human Development Index, which ranks 22nd in the world in 2010 and 22nd in the index of The Economist's 2005 about the quality of life worldwide. Based on Eurostat's data the GDP of Greece was equal to 94% of the EU average in 2008. The main sectors of the Greek economy are tourism, shipping, industrial food production and tobacco processing, textiles, chemicals, metal products, the mining and oil refining plants. However, by the end of 2009 as a result of the combination of the global economic crisis and internal factors (uncontrolled waste just before the elections in October 2009), the Greek economy faced its most severe crisis since 1993, with the highest public deficit (although close to that of Ireland and the United Kingdom) and the second highest debt to GDP ratio in the EU. The three major problems of the Greek economy are the lack of institutional ownership, the failure of financial institutions and the existence of corruption in public administration<sup>17</sup>. The lack of quality institutions leads to distortion of incentives in the country and poor distribution of existing talent. The economic crisis could be an opportunity for institutional changes that would result in significant long-term benefits for the Greek economy. But due to the fact that the crisis is a relatively short-term cyclical phenomenon, while the results of an institutional upgrade are long term, the profits from an institutional improvement probably will not come in time to help address the current crisis.

### 2.1 Productive Structure

#### 2.1.1 Inadequate Primary and Secondary Production.

The current situation of the Greek economy is characterized by the unfavorable relationship of Exports-Imports and the huge trade deficit. The value of goods' exports traditionally covers the value of imports by a small percentage, by far the worst among the OECD countries. Indicatively is mentioned the deficit of staple foods (cereals, legumes, dairy products - livestock, feed, etc.). There is surplus only in products like fish, fruits-vegetables, tobacco, and vegetable textile fibers and oils- fats. Also known is the de-industrialization of the country, which occurred during the last decades. The final result is that

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17 Stefanadis Ch., “political economy amid crisis”, available at: <http://62.1.43.74/5Ekdosis/UplPDFs//syllogikostomos/17-d%20STEFANADHS%20321-330.pdf>

Greece imports 83% of its needs. The production is about 17%. This situation was not sustainable.

### **2.1.2 Inadequate Tertiary Production (Services)**

The tertiary production was surplus and covered a significant percentage of the trade deficit in the past. Recently, the source of immigrant exchange has extinct greatly and the maritime exchange has also significantly reduced. With regard to tourism, despite the undeniable growth, must take into account the increased outflow in recent years, since Greeks are traveling abroad more frequently and more lasting, even for leisure. Direct consequence of the above is the exponential growth of deficit of the current account balance in recent years, in unsustainable levels (from € 10 billion in 2001 to 34.8 billion €, or 15% of GDP in 2008 and about 10% recently in a climate crisis).

### **2.1.3 Low liquidity of produced products**

It is interesting that, according to recent studies, the 75% of products, which are produced in Greece, are internationally "Non Tradable". It is also important to mention that Greece ranks the 90th position in the global competitiveness ranking<sup>18</sup>.

## **2.2 Corruption**

The growing importance of corruption as an economic and political factor has led to systematic research into the phenomenon. According to the definition<sup>19</sup> that rightly includes the public and private sector: "corruption is intentional non-compliance, with arm's length relationship from this behavior for oneself or for related individuals' abuse of public power for private benefit". The linkage between the public sector's efficiency and the shadow economy has to do with the expected value of the penalty for underground agents<sup>20</sup>,

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- 18 Tsamis, A., Bakopoulos D. (2011), "Problems of the Greek economy- Suggestions", <http://www.mke.panteion.gr/attachments/article/34/%CE%A0%CE%A1%CE%9F%CE%92%CE%9B%CE%97%CE%9C%CE%91%CE%A4%CE%91%20%20%CE%95%CE%9B%CE%9B%CE%97%CE%9D%CE%99%CE%9A%CE%97%CE%A3%20%CE%9F%CE%99%CE%9A%CE%9F%CE%9D%CE%9F%CE%9C%CE%99%CE%91%CE%A3.%20%CE%92%CE%9F%CE%9B%CE%9F%CE%A3.30.05.12.pdf>
- 19 Tanzi, V. (1998), "Corruption Around the World: Causes, Consequences, Scope, and Cures", IMF Working Paper 63, p. 8.
- 20 Schneider, F. & Enste, D. (2000), "Shadow economies: size, causes and consequences", *Journal of Economic Literature*, Vol. 38, no.1.

lowering the level of the shadow economy. Hence, the relation of the efficiency of the public-sector, that is of bribery, with the shadow economy remains ambiguous, taking into account the fact that bribery which serves control avoidance is sometimes the substitute for going underground. Nevertheless high corruption levels are expected to act as an incentive for underground activities, and in general when regulations are costly -in terms of money and time- they stimulate the "exit option" (i.e. the decision to go underground)<sup>21</sup>. According to Transparency International<sup>22</sup> Greece is ranked in the 49th place out of 146 countries in the Corruption Perceptions Index, scoring 4.3<sup>23</sup>. The prime principal in every economic decision should be that personal or other relationships should play no role<sup>24</sup> in societies like Greece this would conflict with generally accepted norms that one has the obligation and even the right to favorably assist friends, relatives and personal "clients", even if this behavior might require bending, or even breaking administrative rules or the Law itself; the employer who refuses to "act accordingly" will be seen as breaking the prevailing moral code and will make himself "unpopular" or even "unwanted". From assisting friends and relatives it is a small step to beginning to expect and even demand payment from more distant persons (citizens) for performing tasks that it should be the duty of civil servants to perform, or for treating them in the same way as others. Without such compensation, those who required particular permits or legal documents or other services might have to wait a long time to get them. Thus "speed money"<sup>25</sup>, may be required to accelerate the process and bribes to get a positive response in cases where the bureaucrat has the opportunity of delay or the power of refusal. Evidently the corruption problem in Greece is related to a vast range of governmental activities distorting and weakening its allocative, redistributive and stabilising role in several ways and having serious economic consequences: (a) destroying the neutral scope of the tax system by favoring taxpayers who are able to reduce or avoid their tax liabilities, giving them a competitive advantage over their competitors; (b) granting licenses for certain activities (constructions, taxis, business or shop opening, factory operation, etc.) and giving preferences to some individuals over others particularly in connection to allocation of certain instruments (permits, subsidies, credits) genuinely developed

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21 A comprehensive analysis of corruption by Transparency International at (<http://www.transparency.de>)

22 Transparency International (TI) Annual Report 2004, at [www.transparency.org](http://www.transparency.org)

23 The TI-Index ranks between 0 (worst corrupted) and 10 (best - no corruption).

24 Also known as the "arm's-length principle".

25 "grigorosimo" in Greek.

to assist "infant industries"; (c) land uses; (d) access to public goods and services (electricity, health services, issue of certificates, etc.); (e) procurement of public investment contracts; (f) tax settlements and tax incentives; (g) hiring and promotion in the public sector. This means that public sector corruption in Greece is "vertical", reaching from the "dynamic" (administrative) through to the "static" (political) corruption that affects all levels of government activities and fields of responsibility. The effects of this scale of corruption, which may be also seen as a tax on ex-post profits<sup>26</sup>, are devastating for a developed country, mainly in terms of prohibiting foreign direct investments, slowing down development rates, harming competition and generating economic underground activities<sup>27</sup>. Useful data regarding corruption in Greece are available not only from NGO's like Transparency International but also from Governmental International Organizations like the Council of Europe and the Group of States Against Corruption (GRECO). The statutory aim of the GRECO is to improve its members' capacity to fight corruption by monitoring the compliance of States with their undertakings in this field. In this way, it will contribute to identifying deficiencies and insufficiencies of national mechanisms against corruption, and to prompting the necessary legislative, institutional and practical reforms in order to better prevent and combat corruption. GRECO is responsible, in particular, for monitoring observance of the Guiding Principles for the Fight against Corruption and implementation of the international legal instruments adopted in pursuit of the Programme of Action against Corruption (PAC)<sup>28</sup>. The best policy to reduce corruption could be a sharp reduction of the effective control that government has over the Greek economy in a lot of aspects like spending and taxing activities and, especially, in economic regulations. Furthermore, owing to the fact that one of the factors that create the environment that promotes corruption is social intimacy, an effective policy in reducing corruption is that of forced and periodic geographical mobility for

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26 Romer P. (1994), "New Goods, Old Theory, and the Welfare Costs of Trade Restrictions", *Journal of Development Economics*, Vol. 43, No. 1, pp. 5-38.

27 Rose-Ackermann concludes that "going underground is a substitute for bribery, although sometimes firms bribe officials in order to avoid the official states" Rose Ackerman Susan (1997), *Corruption and Development*, Washington D.C., The World Bank, Annual Conference on Development Economics, p.21

28 So far three such instruments have been adopted, the Criminal Law Convention on corruption (ETS n° 173), opened for signature on 27 January 1999, the Civil Law Convention on corruption (ETS n° 174), adopted in September 1999, opened for signature on 4 November 1999 and Recommendation R (2000) 10 on codes of conduct for public officials, adopted on 11 May 2000.

civil servants, in order to remove them from the region where they have their closest social or family relations and to prevent the formation of new relations. Although this could prove to be an effective policy for central government bureaucrats it might not be so effective in fighting local government corruption. These are the barriers, which every anti-corruption strategy in Greece has to overcome: the small size of the country and the lack of mobility in the population, especially the lack of mobility of firms and professionals. Thus the size and the vertical nature of corruption in Greece are closely connected or even complementary to the high share of the Greek underground economy and the big public sector deficits. Greek politicians seem to ignore the research findings that higher tax rates are associated with less unofficial activity as a percent of GDP and that corruption is associated with more unofficial activity. Entrepreneurs go underground not to avoid official taxes, but to reduce the burden of bureaucracy and corruption. As a result, only relatively honest governments can sustain high tax rates. Corruption is often associated with having an overly complex legal, regulatory or tax environment in an economy, when individuals or companies fail to meet the rules of the state because these rules are too onerous pushed unorthodox methods such as bribery of public officials, to avoid the rules. Thus, the complexity of the state rules is often unnecessary and inefficient, while still negative effect of increasing corruption. Corruption in the public sector is an important problem for the Greek economy. An indications are often used to measure corruption is the Corruption Perception index of Transparency International (Corruption Perceptions Index of Transparency International). The 2009 Corruption Perceptions Index for Greece was 3.8. This score is low as it is at the same level as countries like Bulgaria, Montenegro and Romania. Although the per capita GDP of Greece in 2009 was significantly higher than the per capita GDP of Bulgaria, Montenegro and Romania, the Index of Corruption for all these countries were about the same. This is an indication of a serious problem with corruption and erosion of the public sector that exists in Greece. As in the general case of institutional ownership, corruption in Greece can be reduced by a simplification and streamlining of the legislative framework. This is especially important for sensitive areas such as building regulations, tax codes and regulations for the entry of new players. A simpler legislative framework will provide fewer opportunities for possible toll collection bureaucracy and encourage citizens and businesses to avoid improper dealings with public officials. It is also important that the judicial system more quickly and efficiently and to protect citizens from potential abuse of authority of public officials.

To summarize, the strong and consistent relationship between the size of

the shadow economy and the amount of corruption in Greece is closely connected with the reflexes of the "less privileged": the ones who are not willing, cannot afford or have no connections to central or local government bureaucrats are systematically choosing the dark (shadow) side of the economy as a substitute for corruption (bribery), making the shadow economy complementary to a corrupt state.

### **2.3 The Shadow Economy**

It is observed that in many countries the shadow economy has reached a remarkably large size; regardless of the development level, it is extending in all types of economies due to a variety of reasons. The phenomenon is especially profound in Greece, which might be the consequence of long overdue policy decisions and the lack of analysis of the relationship between shadow and official economy. In almost all studies<sup>29</sup>, the increase in tax and social security contribution burdens is one of the main causes of an increase in the shadow economy. Since taxes affect labor-leisure choices and stimulate labor supply in the shadow economy (untaxed sector of the economy), the distortion of this choice is a major concern of economists. The bigger the difference between the total cost of labor in the official economy and after-tax earnings (from work), the greater is the incentive to avoid this difference and to participate in the shadow economy. Since this difference depends broadly on the social security system and the overall tax burden, they are key features of the existence and growth of the shadow economy<sup>30</sup>. It is possible to estimate the relative labor intensity of underground production by comparing fractions of the labor force reported to be engaged in underground employment to ratios of underground output to GDP. Indications that the fraction of the labor force participating in underground production exceeds the size of the shadow economy as a fraction of GDP would provide suggestive, albeit far from conclusive, evidence that underground production is relatively labor-intensive. Under intensity of regulations we mean the (growing) number of laws and regulations, which centrally steer the Greek economy in the form of market regulations, license requirements, labor restrictions, trade barriers, etc. and which lead to a substantial increase in labor costs in the official economy. The greater the general

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29 Thomas, J. (1992), *Informal Economic Activity*, LSE, Handbooks in Economics, London, Harvester Wheatsleaf.

30 Schneider, F. (2005), "Shadow Economies around the World: What do we really know?" forthcoming *European Journal of Political Economy*.

regulation of the economy the higher the share of the shadow economy in total GDP; this prediction, supported by empirical analysis<sup>31</sup>, suggests that Greek governments should put more emphasis on improving the enforcement of laws and regulations, rather than increasing their number. The bigger the shadow economy the lower the state revenues, which in turn reduce the quantity and the quality of publicly provided goods and services. Studies find that smaller shadow economies appear in countries with higher tax revenues (with or without lower tax rates), fewer laws and regulation and less corruption; countries with a better rule of law, financed by the tax revenues also have smaller shadow economies<sup>32</sup>. Greece, though officially ranked in the twenty-one highly developed OECD countries, shows pronounced signs of a transition country: High level of regulation leading to a significantly higher incidence of bribery<sup>33</sup>, high effective taxes on official activities and a large discretionary framework of regulations leading to a large shadow economy

### 3. In the “trap” of recession: The vital role of Negotiations

In the last five years, Greece is going through a period of economic recession. Workers and citizens in general, are in a daily struggle for survival. The fall of the Greek market, the drama of trade, the continuous reduction of salaries, the chase evasion, the growing family budgets, the fear of unemployment and the well-known Greek debt to the European Union are dominant problems facing society. Daily exported research results which confirm the downward trend in the country. The forecasts are pessimistic about recovery even ten years after. The State makes daily efforts and is inserted in agreements. Negotiation is a common phenomenon and plays an important role in current situation. This tool is used in cases such as significant economic agreements between two states, or in a business meeting between employer-employee about the salary, etc. The proper implementation can bring instant results and reach into a profitable partnership. The two negotiators that will take place

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31 Johnson S., Kaufmann D. and Schleifer A. (1997), *The unofficial economy in transition*, Brookings Papers on Economic Activity, Washington D.C. Further Johnson S. Kaufmann D. and ZoidoLobaton (1998), *Corruption, Public Finances and the Unofficial Economy*, World Bank Discussion Paper, p.18 where they suggest that a one point increase in the regulation index (ranging from one to five, with five being the highest degree of regulation), ceteris paribus, is associated with an 8.1 percentage point increase in the share of underground economy, when controlled for GDP per capita.

32 Johnson S. Kaufmann D. and Zoido-Lobaton (1998), op. cit

33 Data available at [www.transparency.de](http://www.transparency.de)

in this agreement will need to be prepared properly to influence the outcome status to an individual or better to a common interest of both sides. But what happens when one of these two sides is unreasonable or has a different mentality; what tactics should be followed to avoid all possible disagreements? Can maintain a good working relationship; what kind preparation should be preceded to be found an alternative? Internationally renowned dealers Roger Fisher and William Ury In their book "achieving agreement", state that in order to properly applied the tool of negotiation and bring the best result should<sup>34</sup>:

- Separate people from the problem.
- Negotiators be focused on interests, not on positions. The two sides must work together in order to find options that will satisfy both.

The negotiator must therefore be cognizant of the situation that will busy him and use appropriate strategies and tactics as well as the correct code of communication to achieve his goal. The negotiation is used in different cases. In terms of the current economic crisis, on the one hand, Greece appears submissive, with a continued effort to secure the funding, while on the other side, the Troika is characterized by a sustained effort to impose any conditions to approve the loan. What is the position and role of negotiation in an economically unfavorable environment?

### **3.1 Win-Win: Myth or Reality?**

According to the Financial Institutions' Vice President of Global Treasury Services, Clark K. Woods: "In a fast-paced, high-stakes, and high-risk environment, negotiation is everything and everything is negotiable" (July, 2009). However, whether it is feasible to apply this method of negotiating in such an increasingly unfavorable environment where conflicting claims of the capital with the requirements of stakeholders-countries? In the context of globalization and highly competitive economic environment, which moves in the light of the requirements of the European Union, the possibility of self-reliance and development of specific social groups becomes more dysfunctional than ever. By today's standards, the negotiating ability of the Greek government in order to provide specific Revenue and expenditure benefits, like Christmas Bonus to employees, is quite precarious and questionable. Therefore, the previously compelling solution of the win-win model is violated in the "altar" of the European integration policy and the measures that are set by the EU, and more

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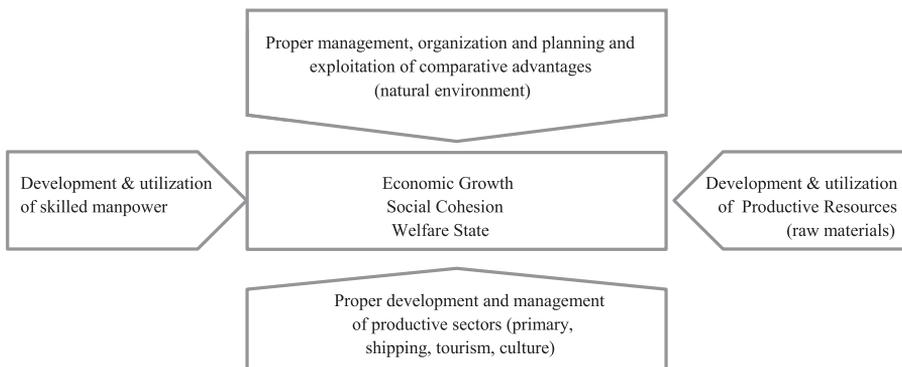
34 Fisher, R., Uri, W. and Patton, B. (2002), "Achieving Agreement", Kastaniotis Editions, Athens, Greece.

specifically by the Troika. In the current crisis, which has not only economic but social impacts, affects all social groups in the workforce, so most of workers' rights be violated in supremely. All the above emerge the problem in the negotiations, so the essential meaning of win-win is sidelined: the common good. The environment is interdependent, there may be individual and sectoral laws, but there is the common good, which is undoubtedly the "win-win". The society and the economy are not machines, they are not directed where ever we want, nor we can predict the future of Greece and Europe especially today. The wisdom and super- specialization are not enough. Only by taking all these into account, then the chances to establish the values of equality and morality can be established. Moreover, according to the director Yann Arthus-Bertrand, "it's too late to be pessimistic".

#### 4. Conclusions

Based on SWOT (Strengths, Weaknesses, Opportunities, Treats) and PESTEL (Political, Economic, Social, Technological, Environment, Legal) Analysis (table 1), of the Greek economy and society, there are four main policies to promote growth and development for overcoming the main problems (Figure 1). As uncertainty is spreading across the Eurozone - with Greece as the litmus test - it is necessary to reconsider the causes of the crisis and the possible ways out. The first one is the development of skilled manpower, in order to defeat the highly increasing unemployment. The loss of jobs means not only loss of incomes but also an increase in vulnerability. So, it is crucial

**Figure 1: Social and economic development based on 4 forces**



the utilization of human resources of Greece, which are among the most educated in Europe. Therefore, the HR Departments and specialized executives must make more efforts, while facing challenges important to the survival of businesses and human resources. High priority has to maintain jobs. It is very important to exhaust all alternatives before deciding to lay off workers. Training, repositioning within the enterprise and reforming tasks are solutions that should be considered carefully. In cases of dismissal, the outplacement should be offered to help the employees to their reintegration into the labor market. Secondly, Tourism, Culture and Shipping are the triptych on which can and

**Table 1: SWOT (Strengths, Weaknesses, Opportunities and Threats) Analysis and PESTEL (Political, Economic, Social, Technological, Environmental and Legal) Analysis for the Greek Economy**

Strengths	Weaknesses
<ul style="list-style-type: none"> <li>• Development of available raw materials and natural resources</li> <li>• Development of skilled manpower</li> <li>• Development of appropriate physical environment</li> <li>• Exploiting cultural heritage &amp; tradition</li> <li>• Exploitation primary sector</li> <li>• Development of shipping</li> <li>• Development of tourism</li> <li>• Development of trade</li> </ul>	<ul style="list-style-type: none"> <li>• Lack of clear objectives and goals</li> <li>• Deficit Management</li> <li>• Deficit organization &amp; administration</li> <li>• Statism, large public sector</li> <li>• Bureaucracy</li> <li>• Lack of coordination</li> <li>• Lack of healthy competition</li> <li>• Lack of cooperation</li> </ul>
Opportunities	Threats
<ul style="list-style-type: none"> <li>• Development of human resources</li> <li>• Upgrade current infrastructure</li> <li>• Development of natural resources and raw materials</li> <li>• Utilization of primary sector</li> <li>• Exploiting cultural tradition</li> <li>• Development of shipping</li> <li>• Development of tourism and shipping</li> <li>• Exploiting the potential EU and Eurozone</li> </ul>	<ul style="list-style-type: none"> <li>• Large deficits</li> <li>• Large external public debt</li> <li>• High Unemployment</li> <li>• High interest rates</li> <li>• High levels of inflation</li> <li>• Non mobility labor</li> <li>• Non mobility resources</li> <li>• Lobbying, high evasion</li> </ul>

<b>Political</b>	<b>Economic</b>
<p>Taxation is based around two systems, indirect and direct taxation. All tax on individual's income in Greece is progressive. A Greek individual is taxed at a rate of 18%- 45%</p> <p>Greece is a "presidential parliamentary republic".</p> <p>Unemployment rose to 29%</p> <p>Greece is very development on international trade, more so than the US.</p> <p>1977-2011 Greece was ruled alternatively by New Democracy and PASOK being the two major political parties.</p>	<ul style="list-style-type: none"> <li>• EXPORTS (22.45b€): goods, fruit, vegetables, olive oil, textiles, steel, aluminum, cement, and clothing, refined petroleum and petroleum-based products.</li> <li>• Main export partners: Germany, Italy, United Kingdom and United States.</li> <li>• IMPORTS (43.5b€): Industrial and capital goods, foodstuffs, and petroleum</li> <li>• Main import partners are European Union members (Germany, Italy, France, Netherlands, UK), Russia and China.</li> </ul> <p>Greece went into a recession in 2009, after 15 years of economic growth.</p> <p>Inflation rate 1.30 in July 2012</p> <p>The economy shrank by as much as 4.5% last year- the largest contraction in more than 50 years</p> <p>Tourism has become a booming industry.</p>
<b>Social</b>	<b>Technological</b>
<p>Population growth rate: 0.083% (2011 est.)</p> <p>Population 93% Greek, other (foreign citizens) 7%, as of 2011.</p> <p>Population: 10,760,136 (July 2011).</p> <p>Travel in Greece is relatively safe.</p> <p>Ethnic Groups: Greek (94%), &amp; Others (6%).</p> <p>Official Language: Greek</p>	<ul style="list-style-type: none"> <li>• Industrial production rate: 5.8% as of 2011.</li> <li>• Greece has been a member of the European Space Agency (ESA) since 2005.</li> <li>• Total of 80 airports, 67 of which have paved runways.</li> <li>• R&amp;D456.37millionEuros</li> <li>• PC Sales (electronic retailers Saturn, Electro World, FNAC, and Media Market, 2009.</li> <li>• European Space Agency (ESA) since 2005.</li> <li>• Telecommunication.</li> </ul>

Environmental	Legal
Climate: Mediterranean (Mild, wet winters and hot, dry summers). Pindus Mountain range strongly affects the climate of the country, as areas to the west of the range are considerably wetter on average (due to greater exposure to south westerly systems bringing in moisture) than the areas lying to the east of the range (due to a rain shadow effect)	Constitution: 11th of June 1975 (Third Hellenic Republic) Legal System: European laws and influenced by German and French law. Areios Pagos: Supreme Civil and Criminal Court. European Law Civil Law Business and Partnership Laws.

should support the Greek economy in order to overcome the current crisis. Specifically, in Greece there are 762 shipping companies, while the Greek fleet has 4,714 vessels, of which 2,000 have the Greek flag, making it highly competitive as a country. The same holds true for the Greek tourism, as Greece is the country where tourism has the highest share of employment, even when compared with competing countries. Greece is part of that group of countries (Spain, Portugal, Italy) in which tourism plays a very important role in the development process. In fact, from these countries, Greece has steadily during the last decade, the highest rates of dependence of output from tourism, the consequences of which are particularly evident in the process of recording the balance of services. So tourism, together with shipping, affect the structure of the balance of foreign trade of the country, which is distinguished by a large surplus in services, together with the surplus in the balance of income and capital, compensate the large deficit of balance.

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## THE EUROTUNNEL: THE BANKS FEEL THE HEAT

EKATERINA KIKILIA

### Abstract

The basic working framework of this study was the 1996 fire in the Eurotunnel and its consequences the years following. Within this framework, we focused upon some not so obvious financial repercussions of the accident and specifically the financing banks slide towards a more cautious stand in a forthcoming debt reconstructing agreement. Finally, we analyzed the recent economic developments and the possible solutions to the crisis of the enterprise.

*JEL Classification: Economic History.*

*Keywords: Eurotunnel, economic crisis, lending banks, debt reconstruction deal*

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## THE 1912-1913 BALKAN WARS AND MEDICAL CARE FOR THE SOLDIERS: AN ECONOMIC APPROACH

ATHANASSIOS VOZIKIS\* DIONYSIOS D. ITHAKISIOS\*\*

### Abstract

The unfortunate outcome of the Greco-Turkish War of 1897, along with the “Macedonian Question”, made imperative the need for strong military forces in Greece. In 1904 the first healthy foundations were laid in the area of organisation of the Greek Army, and within eight years (1904-1912) 214 million drachmas had been spent.

In November 1913, spending on the two Balkan Wars (both that of 1912 and that of 1913) had reached the amount of 411,845,000 drachmas, but later estimations probably amounted total military expenditures in those two wars to about 650 million drachmas, of which two-thirds represent direct costs.

The tumultuous time of the Balkan Wars found the Army’s Sanitary Service well organised, as in a relatively short time the Health Service, which was charged with the healthcare of the army and served the total of 130,000 and 195,000 troops, who took part in the operations of the Greco-Turkish and Greco-Bulgarian Wars respectively, functioned adequately. The successes of the Greek army on the battle-field were sweeping, nevertheless the losses in dead and wounded were extremely heavy. As a result, healthcare costs for soldiers during the period of the 1912-13 Balkan Wars were up to 600,000 drachmas. Of course account should be taken of the fact that costs of healthcare stemming from the Balkan Wars were significantly higher, because costs of temporary care and rehabilitation of refugees and care for rural dwellers costs in subsequent years up to 1915 (amounted to 15,817,640 drachmas) are not shown.

*JEL Classification:* N13, N43, H51, H56, I18,

*Keywords:* Public Health, Military Health Service, Health expenditure, Military expenditure, Greece in early 20th century, Balkan Wars.

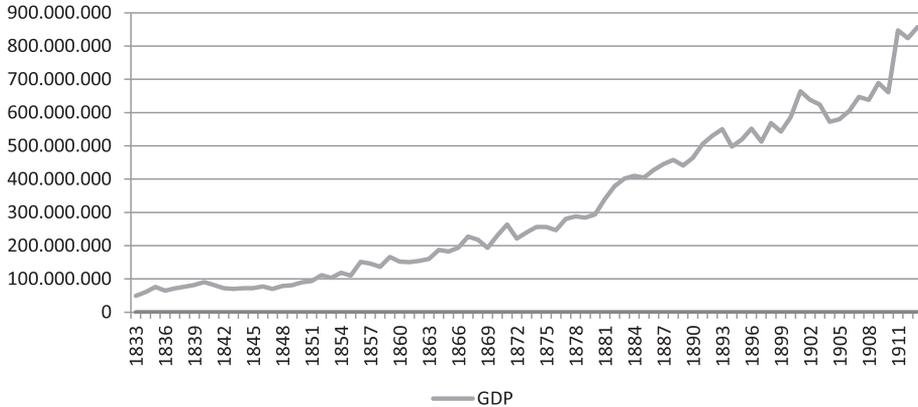
### 1. Economic and Social Reality at the Turn of the 20th Century

With the victory of the bourgeoisie in our country in 1909 and the rise of the Liberal party, whose main representative was Eleftherios Venizelos, the Greek economy and society entered a new stage. It was at that time that the most ambitious, dynamic and integrated attempt at bourgeois modernisation of the Greek state was attempted, compared to those that had been attempted in the past.

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**Graph 1: GDP in Greece 1848-2013**

\* All figures in current prices (Latin Monetary Union drachmas)

The thoroughgoing modernisation included at the same time the organisation of society itself and a more rational intervention of the state in the economy, and was accompanied by efforts at national integration, efforts, that is, to include the greatest possible portion of the Greek nation within the boundaries of the Greek state (Graph 1). The military successes of the two Balkan Wars (1912-1913), which doubled the area and the population of Greece and expanded markets, rekindled the vision of the Megali Idea (“Great Idea”). Implementation of the Megali Idea was the pivotal feature of the Liberal Party’s foreign policy, and all the efforts of E. Venizelos were aimed in that direction.

The unprecedented combination of bourgeois modernisation and national integration fed the dynamic of the modernisation effort that emerged during that period. However, despite the fact that the taxation was extremely burdensome, the limited possibilities of the state’s tax revenues created obstacles for the further expansion of modernisation and its consolidation in all areas of the economy and society. The urgent need to deal with the refugee issue, in conjunction with the incorporation of the area of northern Greece in the nation, made it imperative to carry out major productive projects, despite the adverse effects on the country’s budgetary equilibrium, given that this undertaking from a budgetary standpoint was a huge one.

When Greece was defeated in 1897 and placed under International Financial Control (IFC) in 1898 due to its inability to service its foreign debt, the

aim was to manage public finances by decreasing income and increasing revenues of the state treasury (placed under supervision of the IFC were: revenues from the monopolies, revenue stamps, tobacco tax and tariffs from imports in the port of Piraeus).

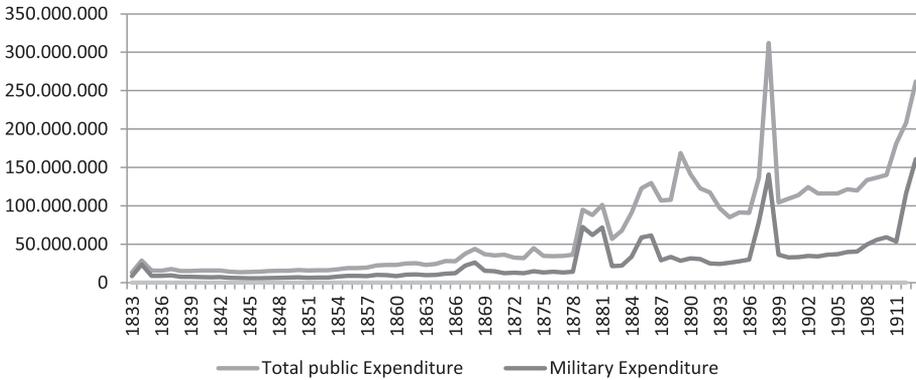
At the same time there was an obligation to pay indemnities to Turkey for the 1897 war, service the external debt and deal with the raisin crisis.

This negative framework was, however, what led the Greek state to modernisation, which was a by-product of the struggle for national integration on the one hand, and a direct result of the effort by the International capital markets to ensure the servicing of the loans extended to the Greek state, as expressed through the IFC, on the other. The results of this development became apparent between 1898 and 1912. However, this modernisation in Greece, as in all the countries operating on a comparable level, involved a great waste of human and other resources.

## **2. Military Preparedness and the Health Service**

The unfortunate outcome of the Greco-Turkish War of 1897, along with the “Macedonian Question” that was created in the meantime through the activity of the Supreme Macedonian-Adrianople Committee, made imperative the need for strong military forces. In 1904 the first healthy foundations were laid in the area of organisation of the Greek Army, and the three years from 1909 to 1912 were the key period of its rebirth from every point of view. The government of Eleftherios Venizelos (1911), which undertook to remedy decades-long shortcomings, succeeded in establishing exemplary balances operating in two important areas: improved material conditions and optimal staffing of the units. Apart from a small force of 17,000 soldiers that would remain inside the country to guard it, the majority of the army would take up offensive positions on the northern land borders of the country. However, the biggest challenge that Venizelos had successfully met was that of armaments. Military spending in Greece always represented a significant proportion of public expenditures (Graph 2). Efforts had begun as early as 1904 and within eight years 214 million drachmas had been spent. Of that amount, 115 million had been spent in the two years of preparation, 1910-1912, and the creative trends in the recovery programme very rapidly became apparent.

The tumultuous time of the Balkan Wars found the Army’s Sanitary Service well organised. Despite the initial problems that arose as the mobilisation began, in a relatively short time the Health Service, which was charged with the healthcare of the army and served the total of 130,000 and 195,000 troops

**Graph 2: Military Expenditure in Greece (1848-1913)**

\* All figures in current prices (Latin Monetary Union drachmas)

who took part in the operations of the Greco-Turkish and Greco-Bulgarian Wars respectively, functioned adequately.

During the 1912-1913 Balkan Wars, the Sanitary Service initially had to face a number of difficulties in carrying out its mission, who resulted from many adversities: 5

- *First, its reorganisation.* With the cooperation of the French Military Mission, the new “Organisation of the Sanitary Service in the Field” was completed a few days before war was declared and was published in the Government Gazette just five days prior to the opening of hostilities. One result of this fact was that most sanitary officers were unaware of the organisation and mission of the new sanitary units; in them material was distributed in a non-rational way, and there were even problems regarding the inclusion of many units.
- *Second, the type of combat,* with the exception of the Epirus front, was a march, and it is common knowledge how difficult it is to support the fighting divisions in this type of combat. The extension of the evacuation routes into areas with very poor routes (such as Western Macedonia), in conjunction with the great lack of means of transport for evacuation and supply during the first days of the war, created a number of difficulties in evacuations and a certain nervousness and lack of coordination in the operation of the Health Service in general. All these problems were very rapidly overcome within

a few days, thanks to the industriousness, tenacity and adaptability of the permanent and auxiliary staff of the sanitary units.

If we judge the Sanitary Service objectively, we cannot help but agree that it was successful. Except for the weaknesses in evacuations seen during the First and less during the Second Balkan War, the operation of the Sanitary Service as a whole was very good. The medical and pharmaceutical material in the stores was more or less adequate. There were a number of shortages in means of evacuation. Nursing and surgery for medical casualties, both in the units' zone of operations and also in the interior of the country, were carried out in a flawless manner. The Army's health status was maintained at high levels. Thanks to the preventive measures that were taken, no serious epidemics such as typhus broke out in the Greek Army, and cholera was extremely successfully combated using preventive vaccination, which for the first time in the history of wars was implemented on such a large scale. The vaccination against cholera of 150,000 soldiers and around 350,000 inhabitants of Macedonia in summer 1913 was a real feat for that time.

The Army's Sanitary Service was successful in its mission not only thanks to its own efforts but also thanks to the assistance provided by the "auxiliary bodies" such as the Hellenic Red Cross and the Red Cross organisations of many European states, as well as by private persons. Unprecedented in extent and enthusiasm was the "mobilisation" of all the nation's healthcare forces.

### **3. The Cost of Military Operations in the 1912-1923 Period**

From 1912 to 1923 Greece was almost constantly at war. After 1914 the Greek economy showed a certain dynamism, which can be explained by the optimism created by the military successes of the two Balkan Wars, with the doubling of the country's area and population, the expansion of the market and the productive potential of the new areas annexed. A significant part of the ruling class sought to continue and complete the successes of the Balkan Wars in order to further expand the Greek state in the areas of the Ottoman Empire to which Greek capital had spread.

The successful implementation of such a policy required huge material resources, however, in order to address the colossal military expenditures. The material resources at Greece's disposal at that time were totally inadequate. Their inadequacy and the mockery made of the country by the protecting forces with regard to the allied credits created a "*heavy burden*" with devastating consequences for the country's monetary and budgetary equilibrium.

In November 1913, according to statements by Alexandros Diomedes,

**Table 1: Military Expenditure in Balkan Wars**

Army	292,115,000
Navy	87,730,000
Treatment of wounded soldiers	25,000,000
Treatment of Christian Refugees from Ottoman Empire	7,000,000
<b>Total</b>	<b>411,845,000</b>

spending on the two Balkan Wars (both that of 1912 and that of 1913) had reached the amount of 411,845,000 drachmas 8,9 (Table 1).

The relevant amounts, however, as calculated by the Finance Minister and Edmond Tery, were much higher. In fact the amounts reported did not include expenditures indirectly related to the cost of the war, such as spending on pensions and assistance for the victims of war, spending to restore damaged war material, and spending on temporary loans and administration of the newly annexed territories. Finally, the above-mentioned amount does not include the decrease in regular income for the 1912 and 1913 financial years. In the estimation of A. Andreadis, total military expenditures in those two wars probably amounted to about 650 million drachmas, of which two-thirds represent direct costs. However, neither does the amount of 650 million drachmas include subsequent expenditures for the rehabilitation of the refugees or medical care for the inhabitants of the countryside whose villages had been destroyed during the war. The Balkan Wars caused mass movements of populations as well as demographic changes, in Macedonia in particular. As was only natural, all these movements created an acute refugee problem and altered the composition of Macedonia's population. Moreover, the settlement of the refugees created serious problems. Total spending on temporary medical care and rehabilitation of the refugees between 1912 and October 1915 amounted to 15,817,640 drachmas.

In conclusion, it can be argued that the actual total cost of the Balkan Wars was much higher than that shown by the data in official calculations. In fact it exceeded the country's economic capabilities at that time.

### 4. Expenditures for Medical Care of Soldiers

The successes of the Greek army on the battlefield were sweeping, and have never been repeated to this day. Nevertheless the losses in dead and wounded were extremely heavy. For example, in the First Balkan War, overall in battle-front of Thessaly-Macedonia, the dead amounted to 81 officers and 682 soldiers while the injured were respectively 87 and 3,583.

According to official hospital statistics, only during the period of the cold winter of 1912-1913, 8,847 wounded and 2,808 ill from the hardships of war were hospitalised. In addition, in Thessaloniki alone, within around two and a half months in summer 1913 39,056 ill and wounded were hospitalised; 14,364 of them were transported behind the lines, using the railways and floating hospitals.

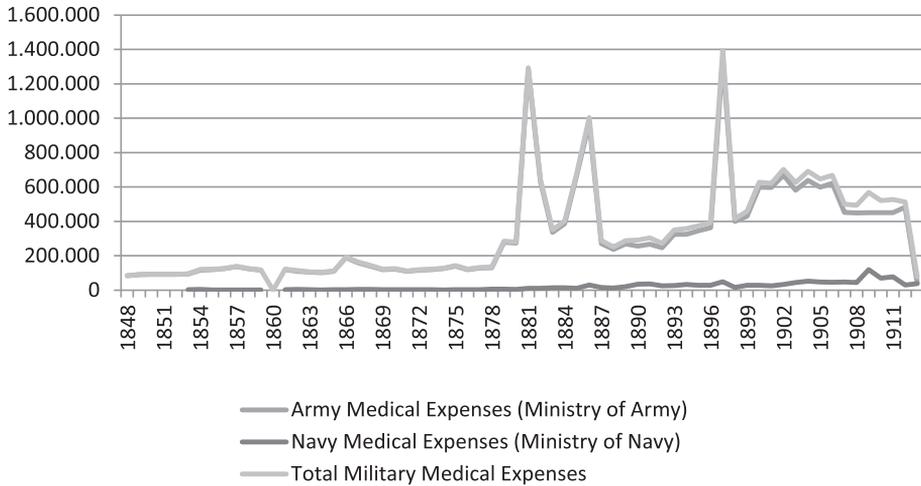
Healthcare costs for soldiers were always a significant part of total military spending (Graph 3).

Such expenditures can be broken down into healthcare costs for soldiers (expenditures of the Ministry of Military Affairs) and healthcare costs for sailors (expenditures of the Ministry of Naval Affairs), as follows (Graph 4):

**Graph 3: Military Medical Expenses in Greece (1848-1913)**



\* All figures in current prices (Latin Monetary Union drachmas)

**Graph 4: Allocation of Military Medical Expenses (1848-1913)**

\* All figures in current prices (Latin Monetary Union drachmas)

More specifically, during the period of the 1912-13 Balkan Wars, according to the official audit of the Greek state, army healthcare expenditures in 1912-1913 can be broken down as follows<sup>5</sup> (Table 3):

**Table 3: Military Medical Expenses in Balkan Wars**

	<b>Army Medical Expenses (Ministry of Army)</b>	<b>Navy Medical Expenses (Ministry of Navy)</b>	<b>Total Military Medical Expenses</b>
1912	483,225	30,065	513,290
1913	40,786	37,724	78,510

## 5. Conclusions

The preceding analysis reveals that Greece relied on its own resources to finance military operations during the 1912-1913 period. Direct and indirect military spending, which was colossal in relation to Greece's economic capabilities, resulted in increased public spending and greater fiscal deficits, with immediate and devastating effects on the country's monetary and budgetary equilibrium.

Despite the fact that Greece was heavily indebted at the end of the Balkan Wars, its economy showed a certain dynamism. This dynamism was apparent: (a) in the stability of the drachma, which retained its nominal value throughout the military operations, (b) in the increase in deposits in the National Bank and in gold reserves, (c) in the maintenance of the balance of payments in foreign trade and in the relative stability of revenues emanating from it, and (d) in the stability of public revenues.

Nothing contributed more to this confidence and optimism than the feelings of satisfaction caused by the great military successes of the Balkan Wars. Greece's area and population had almost doubled, and the productive potential of the newly annexed regions and the expansion of the country's market created hopes for the future. To be sure, adding to this dynamism of the economy, which surprised even foreign observers, were the returning Greek emigrants from the US, as well as donations from Greek expatriates.

Thus, the liberation of the ethnic Greek populations in neighbouring countries, with the corresponding territorial expansion of the nation-state, in conjunction with the bourgeois modernisation of the country, which was attempted simultaneously in that period, determined to a significant extent the subsequent evolution of the Greek economy and the manner of addressing and financing the huge post-war needs created by the Balkan Wars.

The problem of healthcare for the troops from the successive military conflicts as well as the healthcare and settlement of the refugees was from a budgetary standpoint tremendous. The huge burdens that emerged for the country in such a short time, without any real help from abroad, contributed on the one hand to a setback in the country's modernisation and on the other hand were one of the main causes of Greece's economic collapse culminating in the bankruptcy of the Greek state in 1932.

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