Greek PM promises to "draw blood" to salvage economy

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Greek Prime Minister George Papandreou launched a 48-hour "charm offensive" at last week's World Economic Forum in Davos, Switzerland, reassuring Europe's banks, bond traders and business press that his government is prepared to do whatever it takes to reduce by three quarters Greece's budget deficit, currently running at 12.7 percent of GDP.

Papandreou, leader of the social democratic PASOK (Panhellenic Socialist Movement) did his best to maintain the charade that his government's deficit reduction program, including deep wage and job cuts, was a war on corruption. He told reporters that Greeks must, "clean the slate, get it out in the open, put in rules and regulations so we move away from this negative legacy".

However, the prime minister's language, far from disguising PASOK's real target—the working class—signalled to those assembled at Davos that the Greek government was determined to push through the savage austerity measures needed. "This may draw blood from us all," Papandreou told reporters, "but…we need to make this change".

The government's measures have already provoked anger and opposition. The Supreme Administration of Greek Civil Servants Trade Unions (ADEDY), an umbrella organisation representing 1,300 public sector unions and with a membership in excess of 300,000, has called a protest strike on 8 February. The General Confederation of Greek Workers (GSEE), an organisation of 2,400 private sector unions with over 500,000 members, has called an equivalent strike for a day, to be advised, in early February.

These strikes, despite their limited character and the determination of the unions to shut down any campaign as quickly as possible, could be explosive. The government deployed 10,000 riot police on the streets of Athens in December for a far smaller strike, one that was boycotted by the GSEE and ADEDY. Police beat protestors and made dozens of arrests.

Papandreou's promise at Davos to avoid default at all costs has done little to dampen expectations that the European Union (EU) will eventually step in to bail-out the Greek government. This funding could come into play in the event that bond markets remain sceptical about Greek debt reduction strategies or in the event that mass protests against government cuts undermine political stability.

European governments have been strident in their denial that a Greek bailout might soon be needed. Greek Finance Minister George Papaconstantinou, also in Davos, told reporters: "We're not going to be drawn into this [question of a bailout], we're not going to participate in it…. Any discussion of Plan B is just not in our vocabulary."

French Finance Minister Christine Lagarde announced after a closed-door meeting with senior European Commission and European Central Bank executives that, "there is no bailout. There is no way out [of harsh deficit reduction measures for Greece]."

German Economy Minister Rainer Brauderle told the media: "The British or German taxpayer cannot finance the failures of others. That is not a community. Solidarity also means everybody adheres to common rules." The rules in question are not only the requirement that deficits be limited to 3 percent of GDP, but a ban (Article 103 of the Maastricht Treaty) on bailouts of or by EU member countries.

However, Greece can only avoid default through cuts that few believe can be carried out without civil unrest. The Greek public sector accounts for 35 percent of the country's workforce. Greek unions estimate that the planned cuts will lead to job losses across the economy in the order of 100,000, pushing the unemployment rate up by 5 percent.

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At the same time, the EU is desperate to avoid the first-ever bailout of a euro zone member (non-euro zone countries Hungary and Latvia received multi-billion emergency packages in 2008 at the height of the financial crisis). Such a step would not only cost, potentially, hundreds of billions of euros, but create a precedent for further rescue packages, placing unprecedented pressure on the euro itself. New York University economics professor Nouriel Roubini told a Davos seminar the current crisis was so severe that "down the line, not this year or two years from now, we could have a breakup of the monetary union".

The *Financial Times* reported on January 27 that, according to unnamed senior EU officials, a bailout package was being discussed. The International Monetary Fund has broken ranks with the EU, its director admitting publicly that a bailout is an option. A day later, European Commission President Jose Manuel Barroso, when asked about a bailout, told reporters: "It's quite clear that economic policies are not just a matter of national concern but European concern."

At the same time, Papaconstantinou, at odds with the official government line that Greece is determined to manage the crisis alone, hinted last week at the idea of a Eurobond—a bond jointly issued by all euro zone governments that would function as a zone-wide guarantee for Greek debt. "It is not something that Greece has proposed, but it is an interesting proposal," he declared.

According to reports last week, Greece was also trying to sell 25 billion euros worth of bonds to the Chinese government in a deal promoted by Goldman Sachs. Aware of its wider ramifications, the Greek government tried to deny that any firm approach had been made. Marco Annunziata, chief economist at Unicredit told the *Financial Times* last week: "A member [euro zone] country implicitly rescued by China would be an even worse signal than an IMF program."

Markets remained nervous despite Papandreou's Davos pronouncements, with the yield on Greek bonds hitting their highest level since Greece joined the euro zone in 2001. The cost of credit default swaps (the cost of insuring Greek debt) reached a record high of 422.5 basis points on January 28. The impact of the Greek crisis on euro zone stability is also reflected in a plummeting euro. Last Friday the currency dropped to a six-month low against the US dollar. The euro ended January having suffered its largest monthly decline against the dollar since its inception 10 years ago.

The sharpening of the Greek debt crisis has placed immediate pressure on Spain and Portugal, whose huge public deficits also put them at risk of default. A Royal Bank of Scotland senior analyst noted: "In the context of the crisis surrounding Greece it was a natural development that the market would pick out the other weak links in the euro zone."

Spain and Portugal have announced austerity measures of unprecedented depth. On January 29, the Spanish government promised to reduce its budget (now 11.4 percent of GDP) by 50 billion euros over four years. The measures include an increase in the retirement age from 65 to 67. Spending on education will be cut, as will stimulus spending aimed at reducing an official unemployment rate of 18.8 percent.

The Portuguese prime minister told parliament on January 27 that as a result of the mounting economic crisis, his country's finances are "totally out of control". Responding directly to the publicly-voiced demands of the European Central Bank, he indicated that his social democrat government would sharply increase sales tax, cut government employment by thousands, reduce public servant pay and raise cash through privatisation.

The European financial system's concern to prevent a Greek default lies not only in ensuring the integrity of the euro and avoiding the political and economic costs of a bailout. Vast direct interests are at stake for the European banks. The UK and Ireland account for 23 percent of total outstanding Greek debt. Italy accounts for 12 percent and Germany, the Netherlands and the Benelux countries about 6 percent.

The sheer scale of Greek borrowings is also an issue. According to Deutsche Bank, a Greek default would be bigger than the combined defaults of Argentina in 1998 and Russia in 2001. Greece has 254 billion euros of outstanding debt, whereas Russia owed 51 billion and Argentina 57.2. A Greek bailout would add to the handouts made to the European banks—already in excess of $US4 trillion—the burden of which inevitably will be imposed on the European working class.

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