Grexit is catastrophic for Greece

The Greek government reopened the discussion "euro or drachma." The real question is not "euro or return to the drachma," but "euro or Grexit." Grexit to a new drachma is not a solution, it is a catastrophe.

First, the recollection of good old times with the drachma does not imply that those times were good because of the drachma or that these times will return with Grexit and the new drachma while our partners remain in the euro. The proponents of the drachma make outlandish promises for the new drachma regime: the national debt would be erased, private debts would be wiped out, and an 1:1 exchange rate of the new drachma with the euro would prevail. Such promises are either intentional deceptions or reflect a profound lack of understanding of economic reality. In the seven years of the crisis, Greece lost the position it had among the economies of the European core. Greece's present condition reflects the actual productivity of its economy, namely that the improvements in the first eight years of the 21st century was illusory, a result of increased consumption made possible by external borrowing. Such borrowing would be infeasible for many years under Grexit.

The consequences of Grexit would be catastrophic for Greece both in the short and long term. The lack of competitiveness of the Greek economy would result in a quick devaluation of the new drachma vis-a-vis the euro, and the real income of employees and pensioners would shrink dramatically. The national and private debt in euros would became much larger in new drachmas and much more difficult to service. Deposits would be forcibly converted to new drachmas, losing their value by at least a half. The liquidity offered by the ECB to the banks would be withdrawn leading many of them to insolvency. The upheaval in the banking system would also cause widespread business bankruptcies and thus increased unemployment. No credit would be available for new business both because the Greek banking system would be unable to lend and foreign lenders would be unwilling to step in. In the short term, any benefits of an independent exchange rate policy would evaporate under the weight of economic and political instability. Shortages in basic goods such as medicines and fuel would be very likely. The government, unable to balance revenues and expenditures, would print inflationary money and would resort to further populist policies, wiping out the apparent improvement in competitiveness brought about by a weak currency as well as any hope of foreign investment.

The long term consequences of Grexit would be even more dramatic for our standard of living. The significant drop in productivity has stopped only because the country remains in the Eurozone. Outside of the eurozone, our productivity and our standard of living would be reduced significantly. The prosperity of the advanced economies of Europe and in the rest of the world is based on markets and healthy competition, using the created wealth to finance a strong social welfare state. They also have an efficient public sector that functions independently of the government, thereby limiting influence of the parties in power. History has shown that our domestic political institutions are unable to institute and maintain policies that are necessary for sustained long run growth and prosperity of our country. The participation of Greece at the core of the Eurozone contributes to the long term convergence to the European institutions. Conversely, the exit of Greece from the eurozone would strengthen the forces of clientelism as well as the long term pathologies of the Greek economy. We would inevitably be led to a closed and poor economy with a high level of corruption.

Instead of Grexit, the Greek economy needs deep structural reforms that will make it more competitive, will strengthen the forces of economic growth and boost exports and the formal sector, all of which will help in the long term the servicing of the accumulated debt. Placing the economy on a strong footing will strengthen the position of those in the EU and in Greece who are advocating for restructuring Greek debt by increasing maturities and locking in low interest rates. The increase in productivity, the opening of closed sectors to competition, the drastic reduction of bureaucracy especially in attracting investments, and privatization of sectors of the economy where the state has failed are all necessary prerequisites for the reversal of the crisis. These reforms are necessary irrespective of the currency. But, if we were to go to the new drachma, these reforms would be much more difficult to make, condemning the country to long term poverty.

The present government strongly refuses to implement the necessary reforms, its predecessors were rather reluctant and slow, and the European partners put greater emphasis on fiscal issues than to reforms, following the route of least resistance. The structural reforms also involve the system of governance, that is, the legal framework, the application of the law and the rendering of justice, which are all hobbled in Greece. As many economic studies have shown, such bad governance is a huge disincentive in attracting investments, without which economic recovery is not possible. Various special interests nullify or significantly delay necessary reforms that harm their interests, egregious violations of the law, such as the destruction of public or private property, go unpunished, tax evasion is rampant, and tax arrears accumulate. The country has been trapped in the "black hole" of endless austerity without an expectation of growth. The eight-year crisis has subjected people and institutions to unbearable strain. The reduction of the standard of living is merciless and unprecedented. We need to exit from this black hole. This requires a change of course and reforms *inside* the Euro, *not* Grexit. Outside the euro and without the pressure of the institutions, the necessary reforms will never happen. With Grexit, any positive outlook is nullified.

Remaining in the euro ensures the European outlook of the country, giving us the possibility to continue negotiating with our European partners for better terms, for growth-friendly policies, and for debt restructuring. Since the new US government seems to be rather hostile to the cohesion of the European Union and of the Euro, it behooves all of us to work for its stability and for the success of Greece within Eurozone. This will advance the long term vital interests of Greece. In this context, the European institutions and the strong European economies should also act swiftly by accepting their share of the responsibility for the relaxation of austerity and continue supporting a growth path for Greece.

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