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LESSONS FROM THE GREEK TRAGEDY

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The Greek financial crisis that erupted in 2010 was possibly cured after 8 years in 2018. It has been extraordinary in its social cost and its cost to European taxpayers. The causes of this failure are multiple. The main burden lies with consecutive Greek governments that did not carry out the necessary fiscal adjustment and reforms. In their lack of urgency they were strongly supported by American economists, especially Paul Krugman, who opposed austerity and instead called for fiscal stimulus, ignoring the need for financial stability. Much of this discussion was devoted to the benefits or harm of the Eurozone, which eventually hardly mattered. The crisis resolution was complicated by the European Union wanting to play a big role but not knowing how and weakening the traditional role of the International Monetary Fund. The key lessons are back to basics: A government needs to act hard and fast to resolve a severe financial crisis. The IMF is the best leader for financial stabilization. Early and fast fiscal adjustment brings about early financial stabilization, more structural reforms and early and higher growth.

Keywords: Greece, financial stabilization, International Monetary Fund, European Union, exchange rates

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INTRODUCTION

No European country has performed worse after the global economic crisis of 2008–2009 than Greece.[1] Indeed, it has been the greatest economic tragedy in Europe after World War II. In 2017, Greece finally returned to economic growth, and is offering us the relevant perspective to assess the nature of this economic disaster and its causes.

Short of hyperinflation, civil war or secession, a financial crisis can hardly be worse. According to Eurostat, the total fall in Greek gross domestic product from 2008–2013 was no less than 30 percent.[2] In addition, output declined slightly in both 2015 and 2016. Greece recorded 8 years of contracting output, so the fall was not only big but also long-lasting. The public debt stays at 180 percent of GDP. The social cost has been enormous. Unemployment lingered around one quarter of the active labor force. As late as at the end of 2017, it was 23 percent (*Table 1*). In 2010, 13 of the current 28 EU countries had lower GDP per capita in purchasing power parities than Greece. In 2017, only three EU countries were poorer than Greece, namely Romania, Croatia, and Bulgaria, and this shows how devastating the crisis has been for Greece. Almost all the new East European members have surpassed it.

The first stabilization program with the International Monetary Fund (IMF) and the European Union (EU) was initiated on May 3, 2010. Eight years later, on June 22, 2018, the Eurogroup agreed to a fifth and final tranche under the European Stability Mechanism (ESM) program, which was supposed "to allow Greece to build up a sizeable cash buffer covering financing needs until mid-2020."[3] The EU had lent Greece no less than €241.6 billion during 2010–2018.[4] Including IMF funding, total EU and IMF financial support to Greece amounted to €330 billion, almost twice of Greece's GDP in 2016 of €174 billion.

Why were the consecutive Greek governments so spectacularly unable to resolve its crisis? There is plenty of blame to go around. The ultimate culprits are of course the Greek governments that failed to take adequate measures prior to the international financial crisis. A second group of culprits were the EU in its many

[1] In a previous paper I compared the adjustment policies of Latvia and Greece, both of which lost one quarter of GDP in a vicious crisis, but Latvia returned to growth after two years (Åslund 2015).

[2] Throughout this paper, I use the latest Eurostat statistics, if not indicating anything else.

[3] European Commission, Financial Assistance to Greece, June 21, 2018. https://ec.europa.eu/info/business-economy-euro/economic-and-fiscal-policy-coordination/eu-financial-assistance/which-eu-countries-have-received-assistance/financial-assistance-greece_en

[4] European Council, Infographic – Financial Assistance to Greece 2010-18, June 21, 2018. http://www.consilium.europa.eu/en/infographics/financial-assistance-to-greece-2010-2018/

Table 1. Key Greek economic statistics, 2009–2018

	2009	2010	2011	2012	2013	2014	2015	2016	2017
GDP growth (%)	–4.3	–5.5	–9,1	–7,3	–3,2	0,7	–0,3	–0,2	1.4
Budget deficit (% of GDP)	–15.1	–11,2	–10,3	–8,9	–13,2	–3,6	–5,7	0,6	0,8
Public expenditures (% of GDP)	54,1	52.5	54.1	55.7	62.3	50.2	53.8	49.5	48
State revenues (% of GDP)	38.9	41.3	43.8	46.9	49.1	46.6	48.2	50.2	48,8
Public debt (% of GDP)	126,7	146.2	172.1	159.6	177.4	178.9	176.8	180.8	178.6
Unemployment (% of labor force)	8.6	10.0	13.4	18.4	23.3	26.2	26.3	25.0	23.3
Economic Freedom ranking	66	81	90	88	79	89	116	N/A	N/A
Corruption Perception Index ranking	71	78	80	94	80	69	58	69	59

Sources: Eurostat 2018.
Fraser Institute, Economic Freedom of the World, 2017, https://www.fraserinstitute.org/economic-freedom/dataset?min-year=1970&max-year=2015&filter=1&sort-field=legalSystem&sort-reversed=1&geozone=world&page=dataset&countries=GRC&date-type=range
Transparency International, Corruption Perception Index, 2017. https://www.transparency.org/country/GRC

shapes and the IMF. I would add a third major group of offenders, namely the Anglo-American "Keynesians" who urged the Greek government not to resolve its crisis but to pursue fiscal "stimulus." To judge these actors, we start with the causes of the crisis and its slow resolution.

WHAT CAUSED THE GREEK CRISIS AND WHY DID IT LAST FOR SO LONG?

The outstanding problem in the Greek economy was its large fiscal deficit and therefore its increasing public debt. Greece had joined the Eurozone in 2001, but it never complied with the two main fiscal Maastricht criteria, a budget deficit of no more than 3 percent of GDP and a public debt not exceeding 60 percent of GDP.

The Greek financial crisis erupted in early 2010 after the new Panhellenic Socialist Movement – PASOK government of George Papandreou had revealed that the Greek budget deficit was 15.1 percent of GDP, far larger than the previous government had stated. At the end of 2009, the country's public debt was 127 percent of GDP (*Table 1*). The Greek government bonds that had been considered nearly as safe as any other Eurozone government bonds plummeted and by April 2010 the country was effectively cut off from international financial markets.

In May 2010, the IMF, the European Commission (EC) and the European Central Bank (ECB) agreed with the new Greek government on a stabilization program. It sounded ambitious: "Fiscal policy is frontloaded with measures of 7½ percent of GDP in 2010, 4 percent of GDP in 2011, and 2 percent of GDP in 2012 and 2013, each, to turn around the fiscal position and help place the debt ratio on a downward path" (IMF 2010: 1). Alas, these *initial goals were not sufficiently ambitious*. In comparison, Latvia faced an IMF demand of a fiscal adjustment of 9.5 percent of GDP in a far less severe fiscal crisis in late 2008 (IMF 2008). The Greek government had neither the intention nor the ability to carry it out, and the public debt forecasts were overoptimistic. This was the dominant view at the time and it was proved correct.

The traditional and sensible course of action would have been to cut the public deficit sharply, primarily by slashing public expenditures, since public revenues cannot be increased fast during a financial crisis. Moreover, sharp tax hikes do impede economic growth, and Greece's state revenues were already high even by EU standards. A standard advice is to minimize the budget deficit early on by two-thirds expenditure cuts and one-third revenues measures.[5]

Greece did the opposite. Its budget deficit declined only by 4 percent of GDP from 2009 to 2010 and then by 1 percent of GDP in the next year. Only in 2016 did its budget deficit shrink to less than 3 percent of GDP, admittedly then turning to a small surplus after policymakers apparently had realized their prior mistakes. Incredibly, the Greek governments failed to cut public expenditures, which peaked at 62 percent of GDP in 2013. Admittedly, the reason for this peak was bank recapitalization, but even in 2017 when the EU average expenditure was 46 percent, the Greek public expenditures amounted to 48 percent, while fast-growing Romania in its neighborhood had public expenditures of 35 percent of GDP. Furthermore, much of the public expenditures were not very beneficial, being spent on an excessively large and well remunerated state administration and high pensions. The defenders of this policy argued that Greece had cut expenditures greatly in real terms, but because it was done slowly the social cost became far greater than necessary, since the high public expenditures drove down output. Instead of cutting expenditures on time, the Greek governments hiked taxes, which have become among the highest in Europe and naturally depressed output. The Greek tax burden has increased as a share of GDP by no less than 10 percent from 39 percent in 2009 to 49 percent in 2017. The greatest surprise is that any growth could take place with such an ill-advised rise in taxation.

[5] We have discussed how it was done in Latvia in Åslund – Dombrovskis (2011).

As a result of its persistently loose fiscal policy, Greece ran up a public debt of 172 percent of GDP in 2011. In March 2012, the private holders of €197 billions of Greek government bonds had to face a *write off of 53.5 percent*.[6] However, since much of its public debt was held by the ECB and other government agencies and it maintained a massive fiscal deficit, the public debt remained 160 percent of GDP. It would have made sense to write off the bonds held by government agencies, but the ECB claimed that this would be illegal.

The EU offered Greece very substantial and long-term cuts in its public interest costs, rendering the public debt more sustainable than it appears by its nominal size. This has come at a substantial cost to the EU with the establishment of its two bailout facilities, the temporary European Financial Stability Facility (EFSF) and the permanent ESM. Moreover, other countries with large public debt, such as Italy and Portugal, rightly complain that they have to pay a larger share of their GDP in interest on public debt than Greece although their debt is smaller and they have managed to drive down market interest rates.

Crisis resolution is not only a matter of fiscal adjustment and financing but also of structural reform. Together with Italy, Greece has persistently stood out for poor governance and business climate with plenty of red tape among the old EU countries. Even after adding the new EU members, only Bulgaria and Romania have similar problems.

There are many indices of economic freedom, but the broadest and most empirical is probably the Fraser Institute's Economic Freedom of the World. According to this index, the *economic freedom* in Greece has not improved but *severely declined* during the crisis from its ranking as the 66th in the world in 2009 to 116 in 2015. Similarly, Transparency International recorded a deterioration in Greece's standing in its corruption perception index from 2009 until 2012, but it has noticed some improvement that was taking Greece back to 59th in the world in 2017 (see *Table 1*). Much of the difference between the two indices can be explained by the large tax increases and the reinforced tax collection, which weigh on the former index but not on the latter. Neither of these indices is precise, but the big conclusion is that the adjustment in Greece has hardly improved the business environment.

No country has received so much assistance with such poor results. This exceeds even the US wastage of non-military assistance to Afghanistan and Iraq in per capita terms. Any observer is left holding his head asking how such poor policies could be designed and to what extent was the cause intellectual or political? The answer is both, but much of the blame rests with a harmful public debate.

6 European Stability Mechanism, ESM/EFSF factsheet-Greece, November 11, 2016. https://www.esm.europa.eu/esmefsf-factsheet-greece

PAUL KRUGMAN'S PROPOSED CURE

When the Greek crisis hit in the spring of 2010, it came to dominate the global economics discussion, and a few American economists took the lead in this debate. Nobody wrote more about the Greek crisis and more intensely so than *New York Times* columnist Paul Krugman.[7]

This discussion was very strange. Krugman and his followers were not used to dealing with macroeconomic stabilization. They were oblivious of the obvious first problems, the fiscal deficit, the large public debt, the absence of financial stability and the very high public expenditures. Also, they were not aware of the poor business conditions in Greece. American economists did not ask the Greek government to do anything to improve its miserable economic policy, but individual national governments in Europe remain responsible for their economic policy.

Instead, the Krugmanites made two big demands. First, they focused on Greece's current account deficit rather than its budget deficit, arguing that Greece should devalue by opting out of the Eurozone. Second, they opposed "austerity," and remained seemingly unaware that such a policy was not being pursued. Instead, they wanted the EU to pour as much money on Greece as it possibly could want, which would leave Greece with too large a debt burden to allow financial stability as happened.

The Krugman advocacy did not turn to the prime policymaking body, the Greek government. Instead he called Greece a victim and insisted that the EU, the Economic Monetary Union, and Germany should solve the problem, arguing that "this isn't a Greek problem, or even a Spain/Italy problem; it's a European problem" (Krugman 2012). If the main culprit is persistently told that he is not guilty, there is no reason to expect his participation in any resolution. Krugman showed no interest in fighting Greece's deep-seated problems of corruption, bureaucracy and oligarchy. He did not understand that the key to the solution to Greece's economic problems lay in its crony politics (See eg. Tsafos 2013).

Similarly, he ignored Greece's main economic problem, its patently large fiscal deficit, stating that "I've argued that worries about the deficit are, in fact, grossly exaggerated" (Krugman 2013a). On the contrary, he advocated fiscal stimulus, but rapid fiscal adjustment turned out to be the best cure for both public finances and economic growth (Krugman 2013c). He insisted that "the rush to austerity in Europe largely reflected the surge in sovereign debt spreads after Greece got in trouble; the bigger the spread, the harsher the austerity… But it turned out that the spreads didn't reflect underlying fiscal fundamentals" (Krug-

[7] I have discussed his contributions repeatedly in Åslund – Dombrovskis (2011: 54–60) and Åslund (2013), but never received any reply.

man 2013b). But Greece has largely been excluded from international bond markets until 2018, showing that its fiscal deficiencies were a major problem as any bond trader knew.

Presumably in the light of quantitative easing in the United States, Krugman discussed money as an infinite resource freely available without cost. He did not recognize the existence of budget constraints or that financing would dry up as happened to Greece from April 2010 until 2018. It is difficult to understand how an economist can ignore both the risk of sovereign default and scarcity of funding for a country without access to the international financial market. He blamed "the arrogance of European officials, mostly from richer countries, who convinced themselves that they could make a single currency work without a single government" (Krugman 2012a).

Krugman (2012b) paid virtually no attention to the poor investment and business climate in Greece, though he once stated: "Yes, there are big failings in Greece's economy, its politics and no doubt its society. But those failings aren't what caused the crisis that is tearing Greece apart. (…) No, the origins of this disaster lie father north, in Brussels, Frankfurt and Berlin, where officials created a deeply – perhaps fatally – flawed monetary system."

Instead of dealing with any of Greece's real economic problems, Krugman criticized the euro. He insisted that Greece needed to break out of the euro, re-adopt the drachma and devalue. In the same fashion, he had favored a devaluation of the Baltic currencies in the late 2008. None of them had followed his not very politely expressed advice, and thanks to the rigorous fiscal adjustment all of them had returned to sound economic growth after two years in 2010. Krugman, who had attacked these responsible governments viciously in numerous articles, did not recognize that he had been wrong. Instead, he presented the same flawed argument to the Greeks. Yet, the euro enjoyed a solid popular majority all the time. Greeks realized that if they departed from the euro, they would be much poorer. A sovereign default would occur and mass bankruptcies proliferate, and it would lose most of the support from the EU and probably even lose its membership with free trade and large grants.

Thus, Greece kept the euro and it did not devalue. In parallel, Krugman claimed that the euro would collapse. As Ferguson (2013) recorded, Krugman "wrote about the imminent break-up of the euro at least eleven times between April 2010 and July 2012." But once again he was wrong. He did not understand the strong European commitment to the euro.

In the end, Krugman appears to have been wrong and harmful on every single point in the Greek and euro crisis apart from possibly some minor technical points. He did not understand that the political key to a solution was to break through the old Greek political oligarchy. More remarkably, he thought that Greece's fiscal crisis was irrelevant, while focusing on a dubious exchange rate misalignment. He ignored that a major reason for the establishment of the euro had been the exchange rate chaos in the early 1990s, which brought about banking crises in several old EU countries, such as Sweden and Finland. The discussion about the need for Greece to break out of the euro to devalue was a harmful distraction, hindering a discussion of Greece's real problem, which is what the government should do for its population.

In spite of having been wrong about everything both in the Baltic states and in Greece, Krugman has not faced much criticism with the exception of German economists, notably Professor Hans-Werner Sinn (2010) in Munich. The limited criticism of Krugman's flawed advice has severely harmed the reputation of economics as a profession. As Krugman (2012b) himself wrote: "Greece will basically go down in history as the victim of other people's hubris." But the culprits may not be Brussels and Berlin as Krugman thought, but arrogant US macroeconomists not bothering to study the topic they discuss.

WHY WAS THE GREEK ECONOMIC POLICY SO POOR?

The main reason for Greece's poor economic performance since 2010, apart from an awful starting position, was that its politicians were both weak and irresponsible. They resisted fiscal adjustment and structural reforms. They opposed early expenditure cuts, while they accepted big tax hikes. They showed no interest at all in carrying out reforms that would have promoted economic growth and increased welfare for the citizens. All the political leaders of different parties were at fault. PASOK, the old socialist party, has nearly collapsed, while the center-right party New Democracy has recovered under a new leadership. Their common flaw was that they represented an old oligarchy and the vested interests of the public administration, but it has not been broken.

The Krugman-led American debate eased the pressure on all Greek governments to pursue sensible policies. The EU and the Eurozone were poorly prepared for the Greek crisis, but they insisted on taking the lead out of political entitlement. A considerable intellectual confusion existed about whether a country could ease its debt burden through default within the Eurozone or whether it would be expelled from the Eurozone if it defaulted. The default in March 2012 showed that a default within the Eurozone was perfectly possible and did not automatically lead to departure. That should have been understood earlier.

A real problem was that the EU and the Eurozone lacked mechanism for financial support for a member country in severe financial crisis. The EU Treaty was characteristically ambiguous with one article declaring that no bailout was allowed, followed by another article that loosened up that rule. In the end, the Eurozone set up the EFSF and the ESM that took care of the need for financial support.

A big question was which international agency should handle the Greek financial crisis. Traditionally, the IMF would have taken the lead while asking for some financing of its stabilization program. Out of misdirected pride, the EU insisted that it should lead. Fortunately, the IMF was brought in, primarily by Germany. Yet, a “troika” of the European Commission, the IMF and the ECB was formed and it has remained in charge.

The formation of the troika had many negative consequences. First, it was unwieldy and difficult to coordinate, with its masters spread between Brussels, Washington and Frankfurt. Second, unlike the IMF, it had no clear principles. Third, neither the EC nor the ECB had relevant staff or institutions for this work, though they partially solved that problem by poaching staff from the IMF. Fourth, the cumbersome troika made it difficult to impose strict conditionality. Finally, it led to an unfortunate generosity, but since the contributions were loans, the ultimate victims were future Greek generations. In hindsight, it would have been better if the IMF had managed the Greek crisis, as it had just resolved crises that had erupted in Latvia, Hungary and Romania in late 2008.

In hindsight, it is difficult to understand why the IMF and the EU poured so much money in the poor Greek stabilization program. The dominant reason was the fear of spillover effects, which were potentially of three kinds. One year and a half after the Lehman Brothers bankruptcy had unleashed the global financial crisis, policymakers feared that global liquidity would freeze once again. Another concern was that the Eurozone would collapse. A third less noble worry was that the German and French commercial banks would suffer large losses because their substantial outstanding loans to Greek entities. The complex coordination between the IMF and the EU bodies is likely to have contributed further to the soft conditionality and the abundance of bailout credits.

The combination of an American debate opposing elementary fiscal discipline, weak Greek governments, and a weak international troika had the natural consequences of soft conditions leading to little and slow adjustment accompanied by excessively large loans with which Greece has been settled. For both the IMF and the EU, the Greek stabilization program represented their biggest loan program ever.

The conclusions thus run counter to the dominant Anglo-American public discourse about the Greek crisis. The main problem was not that the IMF and the EU demanded for austerity but that the Greek governments received too much money too easily while doing too little fiscal adjustment and structural reforms. The high taxes and poor business environment will keep growth down for a long time to come in spite of the fact that in each year since its accession in 1980, Greece received a few percent of GDP as grants from the EU.

LESSONS TO BE DRAWN FROM THE GREEK DRAMA

The Greek financial crisis stands out as one of the great follies in financial history. One reason was that it was a test case for a severe financial crisis in the Eurozone. A common assumption was that a crisis in a Eurozone country was a new and different situation. In hindsight, however, most things were as usual in a serious financial crisis, as demonstrated in the Reinhardt – Rogoff (2009) book which was published a year before the Greek crisis erupted.

Most of all, the Greek tragedy points to the need for a return to first principles. In severe financial distress, two actions are normally required. First, the government in trouble calls for the international fire brigade, that is, the IMF. Within one month, the IMF can form a stabilization program with the crisis government and disburse a substantial first payment. If necessary, the IMF can mobilize additional international financing in Europe from the EU authorities. The troika acted swiftly in April 2010, but the program was uncommonly unrealistic in its assumptions and thus too soft, which led to far greater credit demands than otherwise would have been accepted by the creditors. The unfortunate experiences with the troika suggest that it would be better for the EU to abandon its ambition to operate as the chief financial stabilizer and let the IMF play its traditional role. Still, the EU should provide additional financing as appropriate, which it had just done in the IMF programs for Hungary, Latvia and Romania.

Second, the government in the crisis country needs to carry out a radical fiscal adjustment, which the Greek governments failed to do. The failure of the innovative and expensive Greek crisis resolution leads to a call for back to basics in terms of quick and sharp fiscal policy adjustment. The idea to delay the crisis resolution with baby steps in cutting the budget deficit and more reliance on revenues measures than expenditure cuts turned out to be a disaster. The lesson is that a budget deficit should be reduced sharply and early to restore the fiscal sustainability of the country to bring down interest rates, to minimize the fiscal cost to future generations, to stimulate a maximum of structural reforms, and to promote an early return to high economic growth.

In June 2013, the IMF published an evaluation of its programs with Greece that was depressing, because it was far from the truth and pointed in the wrong direction. It mentioned four achievements: a "strong fiscal consolidation," which was not true, that "the pension system was put on a viable footing," which was also untrue, though "Greece remained in the euro area" and spillovers "were relatively well-contained" (IMF 2013: 2).

The report presented the failures more honestly: "Market confidence was not restored, the banking system lost 30 percent of its deposits, and the economy encountered a much deeper-than-expected recession with exceptionally high unemployment. Public debt remained too high and eventually had to be restructured. (…) Competitiveness improved somewhat on the back of falling wages, but structural reforms stalled and productivity gains proved elusive" (IMF 2013: 2).

The IMF authors did not even mention that it had failed in its key task of swiftly restoring financial confidence. Instead, they posed two biased questions. First, "Should the fiscal adjustment path have been more gradual?" (IMF 2013: 20). Second, "Should the adjustment path have been more flexible?" (IMF 2013: 21). It would have been more intellectually honest to pose the open questions whether the fiscal adjustment size and speed had been appropriate, but the fiscal adjustment should have been much faster and front-loaded to restore confidence and fiscal sustainability.

The Fund authors noted that "The required adjustment in the primary balance, 14.5 percentage points of GDP, was an enormous adjustment with relatively few precedents…" (IMF 2013: 20). Everything was wrong with this statement. First of all, no other resolution was at hand, and Greece was eventually compelled to make a far greater adjustment at a much greater social cost. Second, such adjustments are common for the IMF, even in Europe. The Baltic countries had carried out greater adjustments, and all the post-Soviet countries did even more after the collapse of the Soviet Union.

The IMF authors recognized that the "large dose of revenues measures … can be questioned, particularly since tax changes constituted almost half of the measures targeted for the first two years of the program" (IMF 2013: 23). They also noted that most of the burden of adjustment had been put on the private sector. Yet, they refused to pass any negative comment on Greece's excessive public expenditures, which have capped the country's economic growth so effectively.

This IMF evaluation presupposed that the adjustment program had been far too soft to cure the Greek economy, but the IMF in uncommon political correctness refused to state the obvious in terms like this: "There was, however, a tension between the need to support Greece and the concern that debt was not sustainable with high probability" (IMF 2013: 2). The obvious answer to this "tension" was that the initial fiscal adjustment had to be much stricter. Unfortunately, the IMF lacked the political strength or will to make this obvious assessment. It went along with the flawed Krugman line that Greece had faced too much "austerity," although all evidence suggested the opposite. In reality, however, the IMF appears to have drawn this obvious conclusion, but in its traditional fashion it has adjusted its policy back to basics without saying so.

The EU bodies tended to emphasize Greek achievements more than appeared reasonable. As Greece is a member of the rather small eurogroup, the eurogroup is reluctant to criticize a member country unlike the much larger IMF. Since the EU had lent so much money to Greece, it had to show that it had been of worth to its members, and the Greeks had become the most skeptical member country of the EU. Rather than comparing Greek reforms with the standard of what was needed, the European Commission tended to compare them with those of other countries that carried out such reforms long ago, making Greece look good.[8] The more relevant question was whether the reforms sufficed to make Greece grow fast, and the answer was a painful no. In 2017, when the whole of the Eastern EU was growing fast and Romania with a growth of 7 percent, Greek growth stayed below 2 percent.

Yet, for the EU, the Greek crisis has prompted many positive developments. Contrary to many predictions, the euro has not only survived, but grown stronger. This crisis has led to the institutionalization of the ESM so that when next time a serious financial crisis hits a euro country, the Eurozone has the necessary financial firepower to finance a crisis resolution. Since 2010, three countries have adopted the euro: Estonia, Latvia and Lithuania. In the 20th century, Europe experienced the collapse of three multi-national currency unions, the Austrian – Hungarian Empire, Yugoslavia and the Soviet Union. In each case, the collapse was caused by profligate nations. Brussels and Frankfurt have stood the test and not given in to the populists, such as Krugman (Åslund 2012). And Greece was not forced out of the Eurozone contrary to the assumptions of many. An important precedence was set. *A euro country can default on its public debt without catastrophe*, which strengthened the euro.

One of the most important outcomes of the euro crisis is that the *Stability and Growth Pact* has been reinforced and thus the national fiscal discipline, while fiscal policy remains the national responsibility. The EC has got a much stronger role through its European semester, which is a semi-annual cycle of economic and fiscal policy coordination within the EU. It focuses on fiscal policy, structural reforms, and macroeconomic balances. It gives the EC a real mandate to review

[8] European Commission, Financial Assistance to Greece, June 21, 2018. https://ec.europa.eu/info/business-economy-euro/economic-and-fiscal-policy-coordination/eu-financial-assistance/which-eu-countries-have-received-assistance/financial-assistance-greece_en

national budgets before they are being adopted.[9] As a result, in 2017, almost all EU countries complied with the Maastricht budget target of no more than 3 percent of GDP in budget deficit (Spain had a deficit of 3.1 percent of GDP) and coincidentally all these countries had economic growth, including Greece.

The EU and the Eurozone need to develop institutionally. Their most obvious financial need is the development of a full-fledged banking union, which is under way. A common supervisory mechanism has been established. An all-European deposit insurance appears likely, while the Eurozone banking bailouts are more controversial. Many have called for larger European fiscal transfers or a Eurozone budget, but they tend to tone down when asked about the purpose.

We need to internalize the big lessons from the Greek financial tragedy. The EU/IMF bailout of the Greek government was more generous than helpful. The slow fiscal adjustment in Greece averted financial stability and necessary structural reforms. Greece has proven that a government default is possible within the Eurozone. Most of all, it has shown the tenacity of both the EU and the euro.

No size fits all. The greater the fiscal crisis, the more fiscal adjustment is needed. If a country is big, the market may offer substantial international financing, allowing it a much larger budget deficit than it would be for a small country. The Eurozone has reinforced confidence so that the market has also been very tolerant of small countries with large public debts. How large the fiscal adjustment has to be is ultimately a matter of judgment and not of sophisticated mathematics.

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