

Greece Debt Crisis

A lack of trust is blighting Greece

The Exchange

7 HOURS AGO by: **Lorenzo Bini Smaghi**



Seven years after the start of the [Greek crisis \(https://www.ft.com/topics/themes/Greece_Debt_Crisis\)](https://www.ft.com/topics/themes/Greece_Debt_Crisis), it's not easy to follow what's going on between the International Monetary Fund, the eurogroup of finance ministers and the Greek government. The negotiating process is being impaired by so many contradictions and a Catch-22.

First, the IMF wants Greece to implement a milder fiscal adjustment programme than the eurogroup, which insists on a primary surplus — which excludes debt interest payments — of 3.5 per cent of gross domestic product. The IMF is probably right, at least on paper, as the country's dire economic situation leaves it ill-equipped to deal with more austerity. Last year's primary surplus was close to 1 per cent, and can hardly be increased in the current environment. On the other hand, experience has shown that Greece has often fallen short of its targets, not only concerning the budget but also structural reforms. Given such a record, a more ambitious target may be necessary to ensure that Athens keeps up to minimum commitments.

Second, the IMF wants the eurogroup to concede more [debt relief \(https://www.ft.com/content/dc636b6a-eed1-11e6-ba01-119a44939bb6\)](https://www.ft.com/content/dc636b6a-eed1-11e6-ba01-119a44939bb6) to Greece, given that debt is likely to be on an rising trend again by the end of the next decade. The fund is certainly right on paper, as all analyses show that Greece will not be able to repay its debt. The eurogroup has already committed to debt relief, as recognised by the IMF, but is reluctant to be more specific lest the pressure eases on the Greek government to continue implementing the programme. Indeed, experience has shown that debt restructuring tends to relax the [reform effort \(https://www.imf.org/en/Publications/CR/Issues/2017/02/07/Greece-Selected-Issues-44631\)](https://www.imf.org/en/Publications/CR/Issues/2017/02/07/Greece-Selected-Issues-44631).

Third, the IMF wants Greece to implement a series of measures immediately, to reduce the eurogroup's doubts about the [required reforms \(https://www.ft.com/content/e6d0cd70-b724-11e6-961e-a1acd97f622d\)](https://www.ft.com/content/e6d0cd70-b724-11e6-961e-a1acd97f622d). These requests are certainly legitimate, but Athens considers them unfeasible in the current economic and political environment.

Fourth, the IMF has indicated that it will not endorse the programme unless its requests, both to Greece concerning the adjustment programme and to the eurogroup on debt relief, are accepted. For their part, Germany and other European countries have signalled that unless the IMF signs up, they themselves cannot support the programme, even though they disagree with the fund on its contents, in terms of both fiscal adjustment and debt relief.

In the end, it's all a question of trust, which has been seriously eroded over the past seven years. The IMF continues to put too much trust into its numerical calculations about [debt sustainability \(https://www.ft.com/content/251f6dc6-f2a2-11e6-8758-6876151821a6\)](https://www.ft.com/content/251f6dc6-f2a2-11e6-8758-6876151821a6), assuming that when policy measures are adopted, they are effective and cannot be reversed. The Greek case over recent years has proved the contrary. The IMF doesn't seem to trust eurozone countries either to deliver on debt relief when the time comes, even though debt relief has been provided in the past. Eurozone ministers, in turn, do not trust Greece to pursue its fiscal adjustment and reform path, if they give in too early on debt reduction. The Greek government does not trust that it will obtain sufficient relief if it implements the conditions requested by the IMF. Some eurozone ministers do not trust European institutions to be tough enough with the Greek government, and have made their agreement conditional on the IMF.

The consequence of this lack of trust is that the Greek economy continues to underperform, the Greek people are losing faith and international investors are reluctant to put capital in a country that may be forced out of the eurozone.

As in the past, the solution is likely to be found in the end, with some concessions on each side. The Greek government will get some last-minute measure through parliament, the eurogroup will agree on a slightly lower primary deficit and to being more specific on debt relief, and the IMF will provide some reassurance about debt sustainability. Nobody would benefit from a failure to agree. But whatever agreement is reached, it will not solve the issue definitively.

It will be a long time before mutual trust is restored. This may require some of the people around the negotiating table to pass the hand to others.

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