Grecovery?
A Question of Trust

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From *GRexit* to *GRecovery*

— Why?
— What next?
Crisis Facets

- Economic
  Fiscal, Competitiveness, Financial

- Institutional & Governance
  Judiciary, public administration, corp. governance

- Cultural - Trust
  Beliefs, Norms, Trust, Civicness, Social Capital
Outline

Why? GRexit

— Economic [Fiscal, Financial, Competitiveness]
— Institutional [public administration, judiciary, regulation product, labor and capital markets, corruption]


— Norms, Beliefs, Trust

What next? GRecovery

— A Question of Trust
The Crisis. The Stats

— **Output (GDP p.c.).** -25%

— **Unemployment:** from around 10% to 20% (peak of 27%). Among youth: ~50%
  • Declining labor force participation
  • Exodus of Greeks

— **Investment.**
  • Peak 25.9% (2008) to 13.3% (2017); around 10% in crisis years;
  • €65 billion -> €25 billion

— **Property prices:** drop 42%

— **Greek bank’s NPLs.** Close to 100bn (50% GDP)

— **Extreme poverty: from around 7% to 15%**
  • single member household in Athens with rent or mortgage with less <€ 395;
  family of four with rent or mortgage in Athens < € 900)
The Crisis. In a Nutshell.

Greece is now the fourth poorest EU country

GDP per capita at 2011 purchasing power parity ($'000)

Source: IMF
© FT
Why? Still unanswered…

— Lack of consensus
  • Even on the data….
— Political animosity
— Social animosity
— Inequality
— Noise (from media, politicians)
— Distorted beliefs
The Blame Game

— Banks
— Labor Unions
— The “Elite”
— Politicians [old, new]
— Political Parties [old, new]
— Administration-bureaucracy
— Regulators
— Media (and journalists)
— The euro and EMU architecture

— The Troika [EU, ECB, IMF]
Crisis Readings. Economics

   - Public debt & fiscal deficits during booming years (esp. 2004, 2007-2009)
   - Private consumption

2. Fiscal Policy during the crisis. *NK-economists View*
   - “aggregate fiscal multiplier”; fiscal devaluations
   - Troika’s role [obsession with austerity]

3. Doom Loop between Banks & Sovereigns. *Macro-Finance View*
   - Non-Performing Loans [NPLs]
   - deposit withdrawals, capital controls, regulation-supervision

4. Competitiveness. *International Macro and Growth Economists View*
   - Trade (current account) imbalance (exports-imports); wage inflation
   - Efficiency; private sector (profitability, management, corp. governance)
Let’s Abstract. Macro Lessons

1. Business Cycle Literature
   • Monetary & Fiscal Policy -> Stabilization Tools
   • Small (if any) long-run effects

2. Growth Literature
   • Physical capital -> around 20%-30% variation in economic performance
   • labor utilization and human capital -> 40% [max 50%]

Needed.
   • Expand notion of “capital”
   • A theory of efficiency [Total-Factor-Productivity].
     • Deep determinants
Macro Lessons (cont.) The Devil Is in the Details. 
Two Types of Debt and Deficits

John Maynard Keynes
Juan and Eva Peron
Crisis Readings. Institutional [Formal Rules of the Game]

Some Institutional Aspects

— Bureaucratic-administrative capacity and quality
— Property rights protection
— Checks and balances on the executive
— Courts (time, quality, formalism) and judiciary
— Legal protection of investors (creditors, shareholders) from expropriation
— Corporate governance mechanisms (regulation, auditing)
— Red tape (administrative barriers to entry and firm expansion)
— Control of corruption
The Institutional Thesis in a Nutshell

Investor Protection and Economic Development

Unconditional Relationship in 2008

Strength of Investor's Protection (Index range 0-10)

Log of real GNI p.c.
Institutional Drift, European South

Evolution of Control for Corruption in the European South

Source: World Bank Governance Matters Indicators
Institutional Gaps and Divergence across the Euro Area

— Considerable gaps in various proxy measures of institutional efficiency
  • Greece scores the lowest across EU 27 in a plethora of measures
  • Gap between the “core” and the “periphery” and “eastern Europe”

— Non-negligible institutional divergence (especially after euro’s inception)
  • Public administration (quality of bureaucracy)
  • Regulatory quality (product markets, banks, labour markets)
  • Red tape and control for corruption
  • Legal capacity, court efficiency, and legal quality

— Also gaps in corporate governance and managerial quality/practices
  • Not much discussion
  • Easy to blame the amorphous state
But,…

— Institutions, policies, and economic success are outcomes
— Endogeneity

— Missing elements?
Crisis Reading. The Missing Elements

—Civic/Social Capital
—Trust
“If we learn anything from the history of economic development, it is that culture makes almost all the difference”. [David S, Landes, 2000, p. 2]

Culture?
— Trust (general, within-family, outside, institutions, etc)
— Social/civic capital [engagement, political participation, civicness]
— Norms and beliefs (e.g., about success in life, role of luck, attitudes towards science, etc)
— Religion
— Family ties
Culture. Informal rules

“those customary beliefs and values that ethnic, religious, and social groups transmit fairly unchanged from generation to generation.”

[Guiso, Sapienza, and Zingales (2006)].
Culture and Institutions. Caveats

Interconnections
Culture (beliefs, norms, trust) $\rightarrow \leftrightarrow$ Institutions (product market regulation, legal formalism, quality of administration, red tape, etc)

Hard to distinguish
— Common historical (and other) origins
  • Role of geography, ecology, and other features
— “Formal” - ”Informal”
It’s a Matter of Trust

“Virtually every commercial transaction has within itself an element of trust, certainly any transaction conducted over a period of time. It can be plausibly argued that much of the economic backwardness in the world can be explained by the lack of mutual confidence.”

Kenneth Arrow (1972)
It’s a Matter of Trust, cont.

“There are countries in Europe ... where the most serious impediment to conducting business concerns on a large scale, is the rarity of persons who are supposed fit to be trusted with the receipt and expenditure of large sums of money.”

John Stuart Mill (1848)
The History of an Idea. Trust and Civicness

— The Republic (*Politia*). Plato. Civic virtue (*arete*).

— Worldly philosophers of the Enlightenment. John Locke, Montesquieu, John Stuart Mill

— Founding fathers of US Constitution (James Madison, Benjamin Franklin).
  • A Mrs. Powel of Philadelphia asked Benjamin Franklin in 1787: “Well, Doctor, what have we got, a republic or a monarchy?”
  • Benjamin Franklin responded, “A republic, if you can keep it.”

— Recent revival of interest (1990). Robert Putnam, Francis Fukuyama
  • Subsequent empirical tests in various contexts
The Beginning of Wisdom is the Definition of Terms
Social Capital

— “features of social life—networks, norms, and trust—that enable participants to act together more effectively to pursue shared objectives”; Robert Putnam (1995)

— “the aggregate of the actual or potential resources which are linked to possession of a durable network of more or less institutionalized relationships of mutual acquaintance and recognition”. Pierre Bourdieu (1985)

— “a set of relationships that support effective norms (related to beliefs and social behaviour)”. James Coleman (1990)
Definitions. Civic Capital

— “a set of beliefs, attitudes, norms, perceptions and the like, that support participation.” Almond and Verba (1963)

— “Those persistent and shared beliefs and values that help a group overcome the free rider problem in the pursuit of socially valuable activities.” Luigi Guiso, Paola Sapienza, and Luigi Zingales (2011)
Social/Civic Capital. Key Elements

— Trust
— Participation
— Cooperation
— Inclusiveness
Social Contract
Notes

Trust, social/civic capital considerations absent from
— Standard (workhorse) economic models that are used for policy-making
— Policy recommendations from international institutions (e.g., IMF, WB, EU Commission, etc.)
— Consulting (management)
Civicness, Trust, and Social Capital
Measurement

Measurement (Challenging)

— Trust (surveys, lab games)
— Participation in NGOs
— Participation in local (or general) elections
— Donations (philanthropy)
— Blood (organ) donation
— Littering
— Tax-evasion (actual and beliefs)
— Beliefs on social issues (e.g., gay rights, immigrants, gender roles)
— In-the-lab games
Trust in Europe

Trust across European Countries (%)  
Source: World Value Survey

WVS Question:  
Generally speaking, would you say that most people can be trusted or that you need to be very careful in dealing with people?”
Bilateral Trust in Europe (before the introduction of the euro)

The Trust Matrix

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<th>Countries of origin:</th>
<th>Aus</th>
<th>Bel</th>
<th>UK</th>
<th>Den</th>
<th>NL</th>
<th>Fin</th>
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Bilateral Trust – Origin and Destination
Beliefs. Justification for Unsound Claims of Benefits

Justification for Unsound Claims of Benefits

Replies for High Income Countries

Mean Reply 1981-2008

Source: World Value Survey
Civic Capital and Economic Performance

Civic Capital and Income
Unconditional Relationship

Source: World Value Survey and Penn World Tables

Civic Capital and Income
Unconditional Relationship for High Income Countries

Source: World Value Survey and Penn World Tables
Trust and Income Inequality across Countries
Income and Trust across OECD country Regions

![Graph showing the relationship between regional income per capita and generalized trust, with an R-squared value of 0.26.](image)
Tolerance-Respect and Economic Performance across European Regions (cond. on country fixed features)
Civic Capital, Trust and Economic Performance. 
Mechanisms

— Trade – commerce (openness)
— Investment, esp. R&D
— Risk Diversification (stock market participation)
— Credit
— Distrust – Red Tape and Formalism – Corruption – Distrust
— Welfare state policies (redistribution, inequality)
— Organizational structure & management quality
A Closer Look on Some Mechanisms

Policy

— Distrust – Red Tape and Formalism – Corruption – Distrust


Management

— Family Ties & Trust - Organizational structure & management quality – Distrust
Distrust – Red Tape – Corruption

Distrust Beliefs

Corruption (decentralized)

Red Tape
Trust and Control for Corruption

Source: World Value Survey and World Government Indicators
Trust and Red Tape

![Graphs showing the relationship between trust and regulations to entry.](source: World Value Survey and Djankov et al. (2002))

Social Capital and Welfare State Policies

![Graph showing the relationship between Social Security Laws Index and Average Trust (World Value Surveys). The graph is labeled as 'Trust and Welfare State Labor Legislation: Unconditional Relationship.' Source: World Value Survey and Botero et al. (2004).]
Trust and Firm Organization

![Graphs showing Trust and Management Quality](image1)

Trust and Management Quality
Unconditional Relationship

- Overall Management Quality Index
- Average Trust (World Value Surveys)

Source: World Value Survey and Bloom et al. (2012)

![Graph showing Trust and Decentralization](image2)

Trust and Decentralization
Unconditional Relationship

- Multinationals decentralization index
- Average Trust (World Value Surveys)

Source: World Value Survey and Bloom et al. (2012)
Back to Why?

Fiscal Conditions
[public debt, govt. deficit]

Competitiveness
[trade deficit, firm performance]

Trust & Civicness
[norms, beliefs, cooperation, collaboration]

Institutions & Governance
[administration, judiciary, regulation, corp. governance]
Looking Forward. GRecovery

Focus. Economics. Short-Term

— Investment (local, foreign)
— Credit, banking, financial system [NPLs]
— Employment – labor utilization
— Fiscal discipline
  • Commitment [MoU] vs. populist demands and weak institutions
  • MoU -> institution
  • Polloí?
Looking Forward. Grecovery, cont.

Focus. Institutions. Medium-Term

— Public administration
— Judiciary, rule of law
— Regulation, red tape
— Corruption
— Governance

— Corporate governance
— Managerial practices
Looking Forward. Grecovery, cont.

Focus. Beliefs, Civic/Social Capital. Medium/Long-Term

— Cooperation
— Inclusion
— Come together
— Trust
Grecovery. A Question of Trust

— Evolution of Trust and proxies of Civic/social capital

— Opposing Mechanisms
  • Crisis
  • Secular Trends [automation, globalization]
  • Inequality and opportunity
The Fundamental Tensions

Civicness & Trust

— Cooperation, collaboration
— Social & economic inclusion
— General trust (towards others)
— Trust towards democratic, capitalist institutions (courts, parties, parliament, etc)

Populism

— Distrust others, experts, media, etc
— Backwards looking
— Segregation
— Conspiracy
— “devil is others”
Beliefs in Europe before and After the Crisis
The Bad News. Trust towards Parliament and Courts

Distribution of Trust in National Parliament, Before and After the Crisis
European Sample, NUTS2 Level

Distribution of Trust in Legal System, Before and After the Crisis
European Sample, NUTS2 Level
Beliefs in Europe before and after the Crisis

The Goods News. General Trust
Beliefs in Europe before and After the Crisis
Unemployment, General and Towards Institutions Trust

Source: European Social Survey and Eurostat
Drivers of Trust and Civicness

1. Deep historical factors
   - Legacy of commerce
   - Geography
   - Important historical incidents [e.g., slave trades, black death, forced labor, Nazism, etc]

2. Policies
   - Educational system type [horizontal, vertical]
     - Early interventions
   - Competition
   - Welfare state
Educational Policies [Vertical-Horizontal] and Trust
Algan, Cahuc and Shleifer (2013)
The Road to Grecovery. Analytical Framework

**Economics**
Investment (local and foreign), banking/financial system, employment.
Education policies => human capital accumulation

**Institutions and Governance**
*Public.* judiciary, product market regulation, public administration
*Corporate.* managerial practices, corporate governance

**Trust & Civicness**
cooperation, collaboration
Inclusion, social contract