We already knew who benefitted from the Greek Bailout

9 May by **Daniel Munevar**

In recent days, a study conducted at the Berlin-based ESMT (European School of Management and Technology) has attracted significant media attention. |1|

The report focuses on the analysis of the distribution of bailout funds lent to Greece since 2010. It concludes that out of the 215 billion Euros provided to Greece, in the framework of the first two assistance programs, only 9.7 billion or 5% of the total was used to support the Greek budget. The rest of the resources were either used for the purpose of debt repayments, interest payments and bank recapitalization. The distribution of bailout funds doesn't change much with the third financial assistance program to Greece. This new program contemplates total disbursements of 86 billion Euros, of which 91% will be devoted to the same purposes as outlined above. Thus, as it turns out, it's the country creditors who have stood to benefit from the bailouts, not the Greek people.

As interesting as it may be to see a conservative German institution making this point, we already knew it. These results broadly stand in line with the findings of Truth Committee on Public Debt established by the Hellenic Parliament in April of 2015. Even more relevant, and forgotten, is the fact that the IMF was well aware of this situation before it decided to participate in the first program of financial assistance to Greece in 2010. An assessment of the risks of lending to Greece provided to the Executive Board of the IMF by its technical staff in May 6th of 2010, just days before the first program was approved, raised a stern warning regarding the composition of the creditors of the country. Out of the 150 billion Euros of Greek public debt, 80% was owed to external creditors. In turn, European banks held 89% of this debt: French banks accounted for 36% of the claims, German banks 21%, with other European banks accounting for the remaining 21%. |2|

Given that the proposed program for Greece by the IMF explicitly excluded the option of a debt restructuring it becomes clear why the IMF staff included these figures in their report. As they were unable to certify the sustainability of Greek debt upon completion of the program, the provision of official funds would simply help to shift losses among creditors. Official funds would be used to bailout private creditors as they liquidate their exposure to the country. In turn, the remaining private creditors would end up facing higher losses on their bond portfolio once the unsustainable character of the debt translates into a debt restructuring. By supporting an unequal distribution of the losses among private creditors, the IMF would be encouraging precisely the type of moral hazard that its lending rules were to prevent.

In the event, these rules were changed in May 10th of 2010 in order to allow the participation of the IMF in the Greek financial assistance program. To accomplish this, European members of the Executive Board made an additional commitment. On the face of reservations by several non-European members of the Executive Board regarding the chances of success of the Greek program, the Dutch, French and German chairs conveyed the commitment "of their commercial banks to support Greece and broadly maintain their exposures". |3| In other words they provided assurance that their banks would not use the opportunity offered by official funding to dump their exposure to the country and shift the losses of a restructuring onto the rest of the private creditors. The ink on the agreement wasn't dry when banks from these countries dumped their Greek bonds and ran for the exit. As a result, their losses were minimized whereas the exposure of Greek banks and pension funds continued to increase. Once the debt restructuring operation of 2012 was concluded, the costs of rescuing Greek banks increased accordingly whereas pension funds suffered massive losses on their portfolios.

Even though it might appear that these are minor historical curiosities, these issues hold a significant relevance in the context of the tensions observed in recent months between the IMF and European authorities. The IMF began its participation in the program in 2010, despite reservations by staff and members of the Executive Board, on the basis of what turned out to be false reassurances from European countries. As the situation in the country has steadily deteriorated over the past 6 years, opposition has built up within the organization. It is no coincidence that the IMF refused to provide fresh funds in the context of the third MoU until it could ensure the sustainability of Greek debt according to its technical criteria. Furthermore, to limit the capacity of European members to pressure the IMF, the Executive Board changed again in January of this year the lending rules of the organization to ensure that once again debt sustainability is a necessary condition to access funds.

Under this light, the outcome of the negotiations between Greece and its creditors its far from certain. If recent history is any guide, its unlikely that any definitive solution will be found on the coming weeks. The most likely scenario is that as the IMF digs its heels on its position, which is the subject of an entirely different article, negotiations will drag down until July when Greece has payments for over 2 billion Euros to the ECB. In this context, what it becomes clear is how cynical is the opposition of the Eurogroup to grant debt relief to Greece on the scale required by the IMF. The members of the Eurogroup are well aware of the original purpose of the Greek bailout as most of these funds were used to rescue their banks. They knew that they were approving loans to a de-facto insolvent country. Thus their insistence in demanding payment in full in exchange of additional painful, and ultimately fruitless, austerity measures can only be described as irrational.

Footnotes

|1| Rocholl, J., & Stahmer, A. (2016). Where did the Greek bailout money go? ESMT No. WP–16–02. Retrieved May 8, 2016, from https://www.esmt.org/where-did-gree...

|2| IMF. (2010). Greece—Assessment of the Risks to the Fund and the Fund's Liquidity Position. Retrieved May 8, 2016, from http://www.elibrary.imf.org/abstrac...

|3| IMF. (2010). Office Memorandum - Board meeting on Greece's request for an SBA - May 9 th, 2010. Retrieved May 8, 2016, from http://ep00.epimg.net/descargables/...

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