

# Greek Debt Crisis

- In 2009, Greece's budget deficit exceeded 15 percent of its *gross domestic product*. Fear of default widened the 10-year bond spread and ultimately led to the collapse of Greece's bond market. This would shut down Greece's ability to finance further debt repayments. The chart below highlights in red the period when the 10-year government bond yield passed 35 percent until vast debt restructuring forced private bondholders to accept investment losses in exchange for less debt.



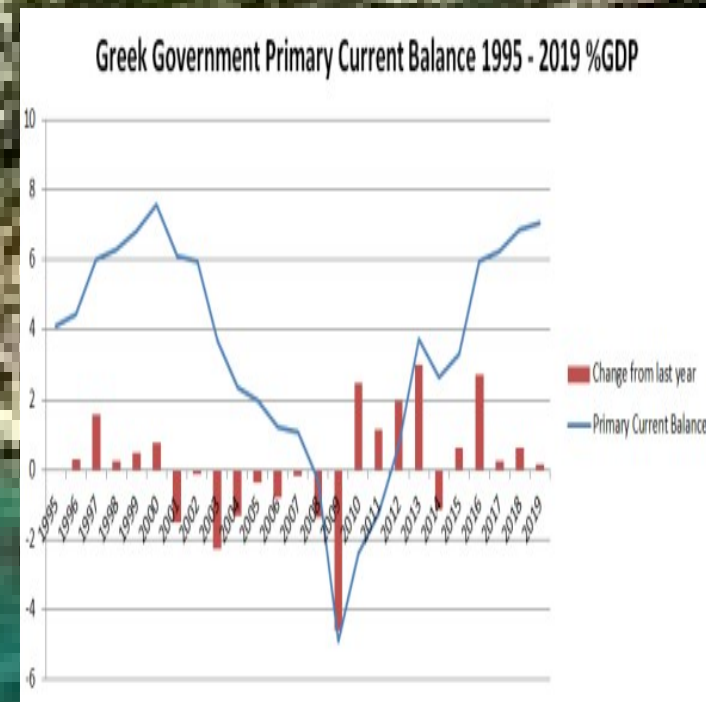
Greece's budget deficit reached 15.4% of their GDP in 2009. This led to a panic of default, and widened the 10-year bond yield spread. From 2010 to 2012 (shaded in red below), 10-year bond rates surpassed 35%. Rates fell again in 2012 after private bondholders agreed to a vast debt restructuring that exchanged 77 billion euros in bonds for 75% less

The biggest lenders were Germany and its bankers. They championed austerity measures. They believed the measures would improve Greece's comparative advantage in the global marketplace. The austerity measures required Greece to improve how it managed its public finances. It had to modernize its financial statistics and reporting. It lowered trade barriers, increasing exports.

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→ Most importantly, the measures required Greece to reform its pension system. Pension payments had absorbed 17.5 percent of GDP, higher than in any other EU country. Public pensions were 9 percent underfunded, compared to 3 percent for other nations. Austerity measures required Greece to cut pensions by 1 percent of GDP. It also required a higher pension contribution by employees and limited early retirement.



- The austerity measures forced the government to cut spending and increase taxes. They cost 72 billion euros or 40 percent of GDP. As a result, the Greek economy shrank 25 percent. That reduced the tax revenues needed to repay the debt. Unemployment rose to 25 percent, while youth unemployment hit 50 percent. Rioting broke out in the streets. The political system was in upheaval as voters turned to anyone who promised a painless way