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A monetary approach towards an unconditional basic income in Greece

by Stanislas Jourdan

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Abstract:

Assuming Greece defaults on its debt and exits the eurozone, this paper suggests an heterodox way of managing the Greek economy towards economic recovery. The paper claims that the central bank of Greece should gradually convert the loans it owns from the Greek banks into deposits of Greek citizens. This process would be led for three years, and result in distributing a guaranteed basic income to every Greek citizen currently residing in Greece. Our proposal is aimed at stimulating a long-term confidence in the economic outlook, fighting poverty and ensuring a pathway to the end of the crisis through social justice and a basic income.

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« The truth is not on the side of the majority, because we do not want it to be so. The day the majority will be able, thanks to its culture and knowledge, to choose its own truth, there is little chance that it is mistaken. »

Boris Vian

Index

Introduction: Modern capitalism has died in Greece

Greece is experiencing a balance sheet recession: austerity is leading the Greek economy into a deep recession that diminishes people's income, along with the value of their assets. In this context, because of the huge deficits and the inability to roll its debt, the government is forced to service an even costlier debt while reducing its spendings, thus reinforcing the recession spiral. Greece's external debt is growing while its economy is downsizing.

The complete loss of confidence in the banking and monetary system is fueling the process of economic self-destruction. The ongoing deposit flight reduces the liabilities of the banks and forces the central bank to inject money into insolvent institutions. And because money is flying out of the Greek economy, there is no way to recapitalise the banks without public intervention (with more public debt).

In this context, not a single bank would run the risk to lend money into the economy. So again, little chance for the economy to recover.

As a result, it appears very clearly that there is no way to get out of such a situation with more debt, whether public or private. However, it is also very difficult to consider a wipe out of the debt that would not collapse the banking system.

In other words, Greece seems to be in a dead-end situation where nothing is likely to stimulate the economy toward growth thus enabling the country to repay its debt. We have probably come to a point where Greece seems to have more to lose in staying in the eurozone. Its competitivity will never be restored only through the so-called internal devaluation. The major issue with this scenario being the price rigidity while wages are hugely cut. Not to mention rising unemployment and its consequences on inequalities, social exclusion and financial distress.

This plan has proved to be unsuccessful and is not acceptable anymore (if it has ever been) for the Greek people. More, it seems very unlikely that the EU sets up a mechanism in which competitivity gaps would be compensated through fiscal transfers among European countries. At least on the short term.

Our opinion, however, is that Greece is only one step beyond what is to expect in every other "developed" countries. Because of its rampant black economy, corruption, political pointlessness and decades of credit-driven growth, not to mention an unsustainable monetary union, Greece was the easy first victim of Capitalism in its current form, and the limits this system is currently facing. First victim, but certainly not the last one.

From this point of view, it is clear that austerity plans were meant to fail, must be ended, and above all, real alternatives to the current functioning of the so called "social-democracies" should be seriously considered. We assume that a basic income guarantee in Greece would obviously be a good idea.

The tricky thing about Greece is that given the current political situation, the inertia of the implementation of any reforms because of the Greek administration complexity and change resistance, and the absence of any literature on the topic in Greece, the way this could be achieved is pretty unclear.

The ambition of this paper is precisely to describe what could be a path towards the implementation of a basic income as a first step towards a more human-based economic governance.

I. Our proposal: A monetary approach to the basic income

The baseline of our modest proposal is based on the assumption that Greece would leave the eurozone alone, along with an immediate significant default on its public debt. Let's make it clear though that we do not claim this to be the only option for Greece.

At the moment of the exit, the exchange rate between the drachma and the euro would be set at 1 EUR = 1 GRD.

As many economists have been arguing until now, an exit of the eurozone seems to be the most plausible and logical step to break the vicious spiral that the Greek economy is experiencing right now. On the other hand, such a solution still raises many concerns and a lot of uncertainties. Indeed, despite the examples of Argentine and Ecuador, the situation of Greece is different because of its membership of the eurozone. As long as a clear way out of the eurozone is not drawn, there is no chance to convince a majority of people to accept this solution.

Nevertheless, this hypothesis enables us to explore wider possibilities since it eliminates a lot of political and monetary constraints. Indeed, our paper suggest a scenario in which three main measures are undertaken.

As we will demonstrate in this paper, these measures are likely to achieve the following objectives:

- Ensuring financial stability
- Restoring confidence
- Stimulate economic growth and employment
- Balance the public budget
- Guaranteeing Human rights respect and social justice.

But first of all, let's detail a little bit our plan.

1. A monetary dividend financed by money printing

The most important proposal of our plan is to give the central Bank of Greece a specific mission: distributing a monetary dividend to every citizen living in Greece.

For that matter, our plan proposes that approximately 20 billion of new drachmas would be printed annually and directly granted to citizens into their bank account. This new debt-free money would be given on a monthly basis, without condition nor any obligation, to every citizen living in Greece. The proposed amount of money would thus represent an unconditional basic income of about 160 drachmas per adult (equivalent to €160 euros at the moment when Greece exits), and about half of that per minor children.

Under our plan, the monetary dividend would be distributed at least for three years, giving time for the country to recover, necessary political reforms to be held and democracy to stand up. At the end of these three years, the plan would possibly be prolonged, readjusted, or revoked, depending on a truly democratic decision.

A special committee composed of ordinary citizen (for instance chosen randomly, like in old Athenian times) would be in charge of evaluating the results of the program and propose its amendment, that could be ultimately approved by referendum.

In this paper, we will designate our proposed basic income scheme under the name “monetary dividend” in order to differentiate the approach we are detailing here from the traditional ones usually based on fiscality.

Complementary to this main proposal, we suggest two complementary measures. These two are not necessary to implement the monetary dividend, but we believe they would be helpful to manage a peaceful, fair and efficient transition to the new currency.

2. A temporary tax on capital inflows

In order to prevent what we call further a “big grexit theft” related to the exit of the eurozone, we suggest the implementation of a temporary tax on all inflow of capital (ie. cash transfers). Concretely, every citizen trying to bring back his euros from a foreign bank account would have to declare it and pay a 20% tax. However, a loophole could be put in place to allow small cash transfers (for instance, cash transfers below 15,000 euros could be exempted).

It is important noting that this would only affect individuals, and not companies that would be willing to invest in the greek economy.

Also part of the plan, the tax rate should be indexed to the exchange rate of the new drachma. For instance, if the drachma reevaluates, the tax rate should decrease.

This tax may be seen as punitive, but it is a matter of social justice that people who escaped the greek banking system are not advantaged too much. Thus, we affirm that our goal is not to punish the rich, but to ensure a level playing field. As we will explain further, this measure is intended to prevent a massive wealth redistribution due to the likely inflow of money that have been parked abroad in an attempt to evade greek fiscality and in anticipation of the introduction of the new drachma.

3. Opening the banking sector to new innovative, ethical and local banks

Last but not least, we propose an ambitious reform of the greek banking sector, which mainly consists in simplifying the rules for establishing a bank in Greece, thus enabling a stronger competition towards old institutions, notably from ethical banks, and other innovative local initiatives.

In practical terms, the Bank of Greece would offer, let’s say 100 special banking licences, for free, to the civil society. These banking licences would be very specific for small banking institutions, on the model of credit unions, tontines or even p2p credit startups. They would be under strict control of the central bank, with size restrictions. More, their activities would be constrained to certain obligations:

- Contribute to the local economy
- Prohibition to speculate on financial markets
- Prohibition of access to other funds than deposits (ie. no money multiplier involved)
- Their governance and distribution of profits must favor depositors.

Also, the means of payments and IT infrastructures costs would be shared through a common entity that would have a partnership with a traditional bank – or even with the central bank itself, thus providing low-cost credit cards and checkbooks to the customers.

As we will explain further, this measure is intended to strengthen the network of banks in Greece, thus helping local investment and financing innovative projects that would contribute to rebuilding the country.

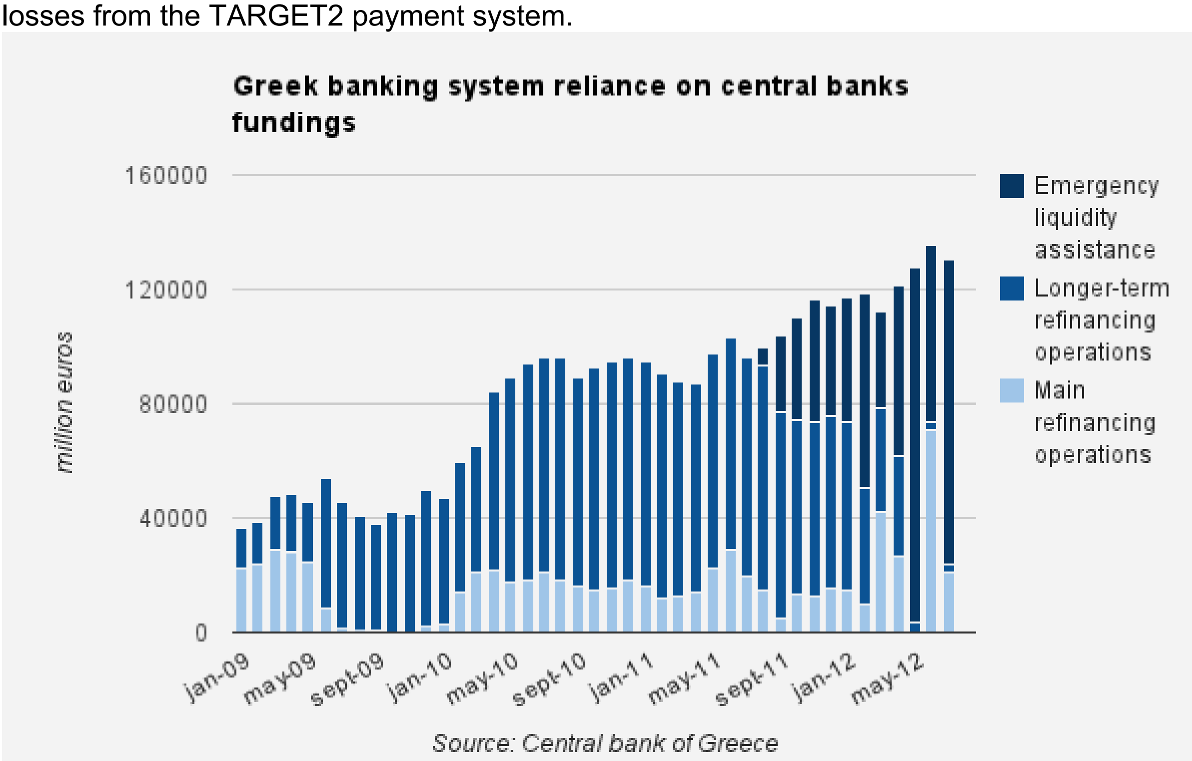
II. A plan B for Greece: Social justice at the heart of a positive recovery of the Greek economy

Why do we believe this could work? What are the economic arguments behind our utopian-style proposal? We argue in the following sections that this plan is likely to prevent a complete collapse of the greek banking system, along with an important reform of the later. Moreover, we demonstrate how this could restore confidence in the economic outlooks of the country, thus stimulating the local economy. And most of all, we believe our plan is fair and democratic.

1. Addressing the banking collapse

The banking sector, particularly, is a big threat in the case of an exit. Yet Greek banks are known to be insolvent, and this situation would be even worse in the case of a default and an exit from the eurozone. The confidence on the banking system, which is already very poor, could shrink again and worsen the situation.

For now, Greek banks have been relying a lot (cf chart) on the funds from the ECB and then from the national central bank of Greece (BoG) through emergency liquidity assistance (ELA). In the case of an exit, Greece will owe a big chunk of this money to the eurosystem (and especially to the German central bank). Indeed, the collateral held by the ECB will rapidly lose their value with the devaluation of the new drachma, leaving the ECB with a big hole in its balance sheet, and then in the eurozone national central banks' balance sheets, which will have to absorb losses from the TARGET2 payment system.



When Greece leaves the eurozone, Greek banks will have to bear huge losses from Greece's default, and will go bust unless their refinancing needs are satisfied. As it appears, they have run out of collateral, so that they would probably have to tap even more into the ELA scheme. But this cannot go on forever: these liquidities are supposed to be provided temporarily to solvent institutions; which is obviously not the case of these banks. And of course, it tends to affect the credibility of the Bank of Greece.

As a consequence, in an exit scenario, it would be important to send a strong signal towards depositors to ensure confidence in the banking system, and thus avoid any panic effect.

Of course, the State could nationalize them and guarantee their solvency. As it happens though, the Greek state has no money and will still have a primary deficit gap to fill. Thus, such a guarantee would probably seem to be an illusion, and might not be sufficient to ensure confidence in the Greek financial system.

Another solution would be for the BoG to fund a financial vehicle that would seize and recapitalize the banks, as it has been proposed by George Kesarios[1]. But it could do even better to stimulate confidence in the banking system on the longer-term.

Under our proposal though, while the central bank creates money from thin air, this money will be flowing into the citizens' accounts of the greek banks, thus progressively reducing their funding needs with the improvement of their liquidity ratios.

From the point of view of the responsibility, we believe this proposal is also interesting since banks would not get directly money from the taxpayers. Rather, they will have to make interesting offers to their customers in order to restore their solvency, and eventually offer capital increases. On that matter, financial authorities could even force banks to respect scheduled objectives. This way, our plan tends to reduce moral hazard that any form of support to the banking sector usually imply.

This however, may not be enough to actually improve the health of the greek banking system, which not only suffers from a bad financial situation, but is also very much affected by corruption and old-school banking practices. Thus we argue that a more ambitious plan should be implemented in order to reshape the whole greek financial sector towards a 21st century-compatible banking system.

2. A new banking sector

As a complementary measure, the government should decide to open its banking system to new competitors. For instance, the central bank could organize banking licences bids in an attempts to create room for new competitors such as online banks, p2p credit institutions, credit unions and local banks. Here, the goal would be to stimulate innovation and local distribution of credit in order to give people and entrepreneurs an easier access to fundings. Eventually, the Greek economy would be strengthened by a network of brand new local banks that would favor small companies and local initiatives, with a fair redistribution of profits.

Last but not least, people would have a greater control on the destination of their savings. This way, our strategy would possibly increase the pressure on the ancient banks to raise capital appropriately and keep competitive services in order to attract deposits. The banks that would not manage to keep their solvency could be dismantled by the authorities and their deposits transferred to other banks.

3. Stimulating production

[1] How to solve the greek debt crisis without taxpayers funds, George Kesarios, March 2012

Even though the devaluation of the new drachma would be an immediate relief for some industrial sectors such as pharmaceutical companies and tourism, it remains unclear how the greek economy would react toward the short-term increase in import products prices.

With the exit of the eurozone, Greece needs a stronger demand for local products in order to stimulate its national production and thus decrease reliance on imported production. This seems very difficult in the short-term for Greece since a lot of capital have been flying abroad. Moreover, Greece has been suffering for a long-time from a lack of investment in the productive capital.

Furthermore, this bank run has been worsening the paralyzation of the banking system, which doesn't lend anymore into the economy because of funding difficulties and uncertainties, in addition to the negative outlook of the economy. As a result, a quick rise of production is quite unlikely on the short-term.

Economic instability, unemployment, and budgetary deficits will not be fixed overnight. What is necessary to stimulate the economy on the medium term? In a nutshell : confidence.

4. Restoring confidence

Confidence is precisely what is currently shrinking in Greece since the beginning of the crisis. Confidence in politicians, confidence in the future. Without any hope that things will get better someday, there is little chance the greek economy recovers.

Without confidence, people will continue to struggle to make a living instead of innovating, helping each other and project themselves into the future. They will keep on avoiding paying taxes (just because their neighbors do and/or cannot afford to pay them), and spend as less as they can. Young people will keep on escaping abroad and some elders will commit suicide as we have already seen[2]. Not to mention, companies will not hire; on the contrary they will keep on compressing wages and costs, thus fueling the spiral of recession.

Moreover, we believe our plan would be a very efficient stimulus for the confidence in the outlooks of the greek economy. In a very keynesian-fashion style manner, the monetary dividend would basically mean that People would have fresh money to spend, thus Companies will have more customers and eventually will have to hire new employees.

The stimulus would be particularly efficient because of the signal effect of such a plan. If the central bank commit itself to create 20bn euros a year for 3 years, there would be much more optimism in the economy. At the microeconomic level, this unconditional safety net would provide a strong relief for many people, who will be less afraid of bad tomorrows and more willing to participate in society, being hired, or freelancing. Actually, we strongly think that entrepreneurship and social activities would be encouraged with the implementation of this bureaucracy-free safety net.

Similarly, with such outlooks, the banks would lend again in the economy, making possible, notably for exporting companies, to invest and grow.

And because of the unconditionality of the monetary dividend, employees will see it as a purchase of power bonus. In other words, unlike conventional grant schemes, targeted to

[2] Wave of Suicides Shocks Greece, Der Spiegel, Aug 2012

jobless people, the current precarious situation of many workers will also be improved. Thus, we believe that the monetary dividend would not discourage people to work.

That way, not only the monetary dividend would stimulate demand, but also production (and this is notably why we believe it would not be hyperinflationary).

Another interesting side-effect: isn't giving money to people the best way to have them using your currency? After all, this has been what governments have been doing for a while[3]. Who would throw this money away? Because everyone would have drachmas in their pockets, the new currency would be quickly adopted in the country and a possible euro black market would remain marginal. The confidence in the new drachma would thus be reinforced.

5. From moneyless economy to monetization

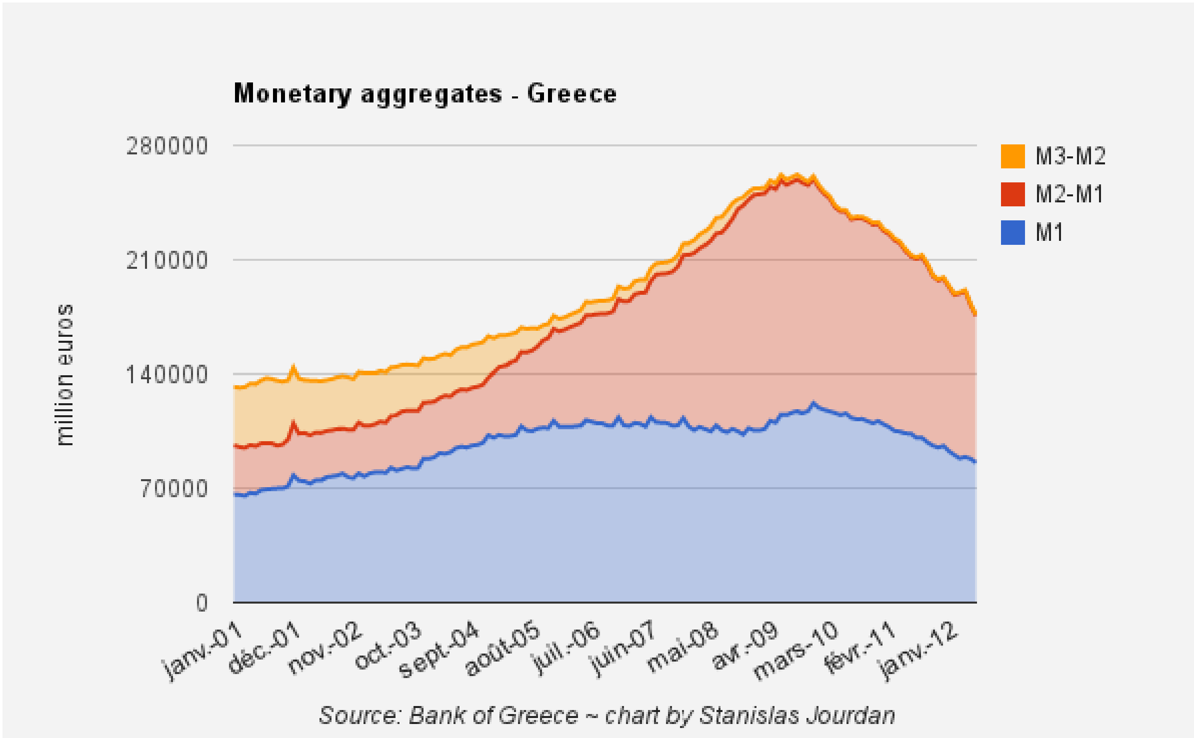
Of course, the problem with money printing is inflation. Understandably, people are afraid of this, especially the poorest and middle-class citizens. In the case of Greece, inflation would also come from the devaluation of the new drachma, leading to a rise of imported products prices. Inflation expectations make things even worse, as people rush to the shops, being afraid whether they still can afford to buy the products in the future. This phenomena increase the spiral of inflation on the short term (on the longer term, this increase the demand for local production).

However, as the previous section hints, it is important saying here that the monetary injection we suggest wouldn’t come without any compensation: while the central bank creates 20 bn euros for its citizens, it would reduce at the same time its emergency lending to banks by 20bn overall. From an accounting point of view, the operation would be quite neutral for the Bank of Greece, except that the money that was frozen between the central bank and the private banks until here will now flow into the real economy through the people’s banking accounts.

Also worth noting, the central bank could progressively tighten its monetary policy (for instance by increasing the reserve requirements) in order to avoid an inflationary credit expansion.

On the monetary mass point of view as well, money printing would not be such an absurd idea.

[3] See: “Debt: the first 5,000 years”, David Graeber, 2011



As the chart above shows, Greece has been suffering from a huge credit crunch since 2008. Let's comment a little bit what the chart says.

The evolution of M1 can be divided into two parts. First, there is a significant increase in 2009 as people withdrawed their savings to compensate their purchase power losses. Then the decrease can be particularly attributed to the deposit flight from the greek banks to the swiss, german and other 'safer' foreign banks.

The sharp fall of M2 and M3 since the crisis is obviously attributed to the absence of any issuance of new credits by the greek banks, as a consequence of the very bad outlooks of the local economy, not to mention the structural insolvency of the greek banking system.

The progressive extinction of M3 from 2005 to 2009 (ie. before the "greek crisis") reveals an historical lack of credit-driven investment in the domestic economy. With 640 million euros at end-june, we can say that M3 has totally vanished.

The consequences of these important trends are huge. As the media eventually report, what we are witnessing in Greece is a transition towards a moneyless economy. While more and more money is flowing abroad, the greeks are left without money in their pockets, thus giving them no other choice except resorting to demonetized systems like barter, local currencies and other practices of the grey/black economy.

Of course, this does not help the official greek economy to recover. Indeed, even though these emerging practices helps the poorest to make a living, on the macroeconomic level, some economists criticize these practices[4] for that they push the economy down given such systems

[4] For Spain's Jobless, Time Equals Money, Wall Street Journal, Aug 2012

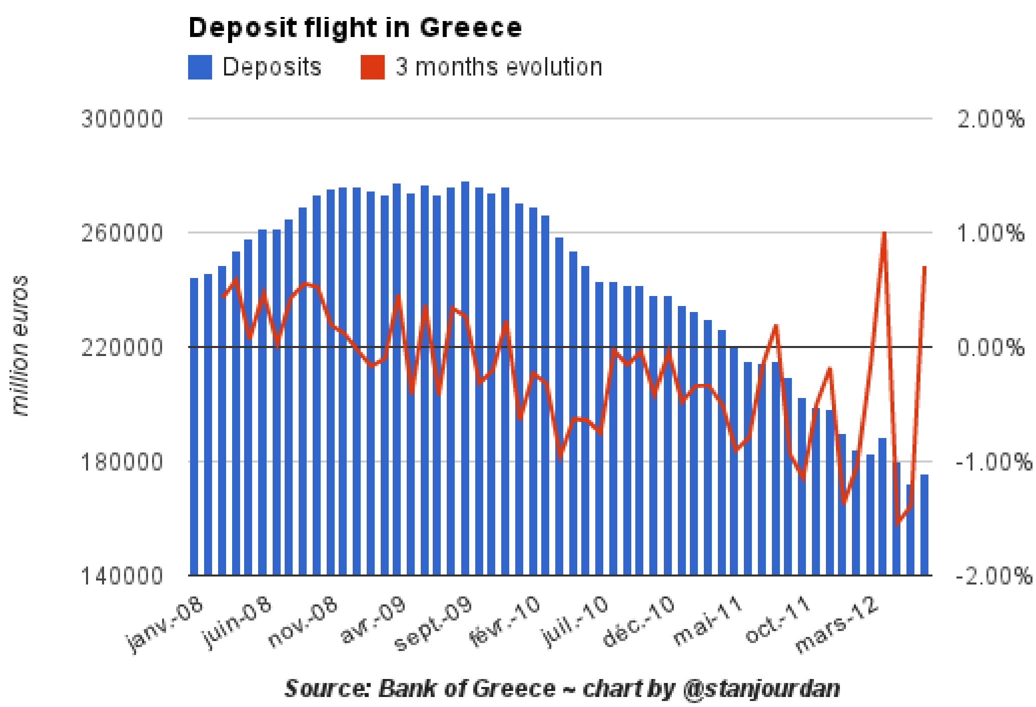
are not counted into the GDP, nor are they subject to any taxes.

Under our plan though, the monetary injection would boost M1 and M2, thus enabling people to use money again. As a consequence, many activities that are currently happening without resorting to official money would be monetized again. And ultimately, this would boost official GDP figures.

The monetary injection we suggest represent roughly an increase by 10% yearly of the Greek monetary mass, which has to be compared with a fall of 30% during the last three years.

5. Avoiding the big “grexit theft”

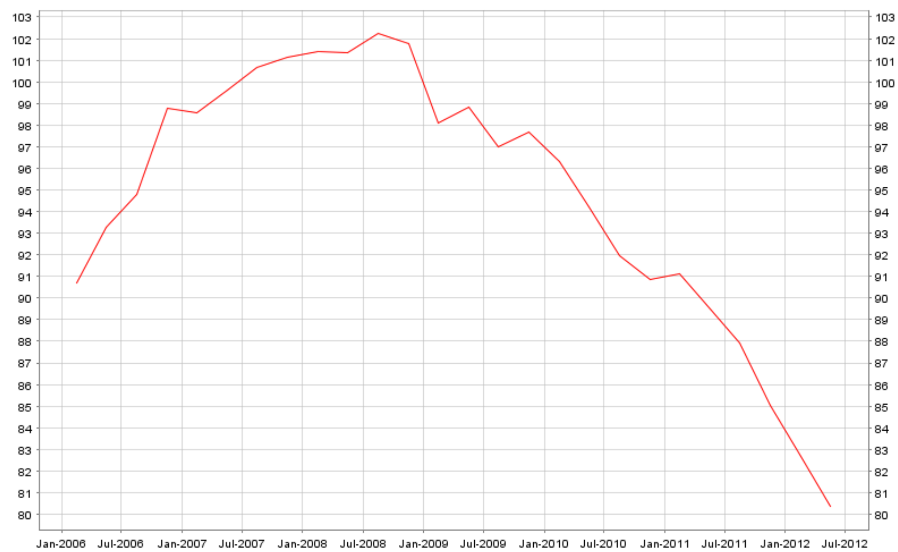
Another issue that Greece would be facing in case of an exit of the eurozone is the capital flight effect. Since 2009, about 60 billions euros of deposits (see chart) have vanished from the greek banks. It is widely known that a lot of this money is either held in cash by the greeks, either it has been move abroad, notably in swiss or german banks.



It is often argued that exiting the monetary union would be a bad idea since there would be a huge bank run, requiring capital controls to prevent people from moving their money abroad.

However, we consider that the yet ongoing bank run is even more of a problem. Indeed, if Greece leaves the euro, the rich that evaded the Greek fiscal system by throwing their money abroad will then be able to bring back their money with an appreciable exchange rate for them. The new drachma being devalued by at least 30%, this situation would be a huge opportunity to buy real estate properties at a very cheap price, notably to over-indebted people that are in need for money. Not to mention, real estate prices in Greece have fallen sharply since 2008 (cf chart below).

This phenomenon would have drastic consequences regarding the inequalities in Greece. Under these circumstances, and in case of an exit, the richest would obviously be the big winners.



Real estate prices index - Greece
(source: ECB)

This is why our proposal includes both a monetary distribution and a tax on money inflows. The first measure, the monetary dividend, would increase the relative share of the monetary mass owned by the majority of modest people, making the share of the richest smaller. In plain english, this means that the richest' monetary possessions will be significantly *diluted*.

This strategy, however, is meant to work on the medium term. On the short term, we suggest that Greece introduces a temporary tax on capital inflows for Greek citizens that would bring back their money from foreign banks. Obviously, this tax should not affect foreign investors, and a loophole should be put in place so that every citizen would be allowed to move up to 15,000 euros into a greek banking account, free of tax. Above this amount, any cash transfer would be taxed by 20%, with an adjustment on the exchange rate, so that the tax is less punitive if the new drachma reevaluates.

This way, the tax would naturally become marginal if, as we expect, the new drachma reevaluates itself after a few years of new investment, and the return of deposits in Greece.

6. A room for structural reforms

Last but not least, let's explore the political effects of our plan. Greece is sick of its old demons political corruption and lack of connection between people and their political representatives.

This is a tricky part of the problem: Greece policy-makers need more political marge de manoeuvre than the eurozone and Troika context currently provide, but at the same time, its political elite cannot be entrusted to take the good decisions. And even if it was, they are not legitimate anymore to rule the country. Any decision they could take would be seen as unfair and would likely provoke strikes and protests.

This is why our plan aims at giving more power to people throughout a monetary approach to the basic income and thus bypassing the politicians. Our monetary dividend can be put in place almost overnight, while it would take decades for a greek government to do it.

That said, we believe our proposal will strengthen Democracy in Greece. First of all, from the point of view of Democracy, the basic income can be seen as a subsidy to every citizen for its involvement. It will give more power to people, to dedicate themselves into politics or social activities instead of endlessly search for a job, or work longer and longer to make ends meet.

On the medium term, the recovery of the economy and the decrease of social tensions would make room for a better political debate, thus opening the doors for the needed structural reforms of the Greek state. For instance, the so called basic income could be progressively replaced or completed by a transfer of existing social grants such as pensions, unemployment and family grants.

With such reforms, Greece could finally simplify its social system and thus reduce its bureaucracy and administration costs, without destroying the rest of its underdeveloped welfare system. Of course, the same should be done on the fiscal side, with a simplification of revenue sources, for example through a flat tax on every income, and/or an increase of VAT in compensation of a decrease in labor costs and other taxes.

This way, the government will eventually manage to balance its public budget.

Conclusion : From Utopia to pragmatism

Our plan seems probably very utopian, idealistic or even impossible to many people. “This is too beautiful to be true” told us several of the Greeks that were involved in the production of this paper.

However, as we can see, there are strong rational economic arguments that tend to favour our strategy. Solving the banking issue, stimulating the economy, simplifying the Greek social model and fiscal transfers: a lot of complicated issues seem to become more easily solvable with such a strategy.

Moreover, given today’s situation in Greece, it appears everyday more obvious that the country will break up with the eurozone one day to another. If this were to happen, it is also pretty clear that Greece will end up printing money, either to fund its deficits, stimulate the economy, or to refinance or recapitalize its banking system.

In this regard, our proposals are not that far from tomorrow’s reality in Greece. After all, what we propose is purely not to repeat yesterday’s mistakes, like giving the printing press to politicians, bailing out bankers without any form of responsibility, or trying to solve a balance sheet recession with more debt. The only remaining option then, is to actually give back the power to the citizens.

By the way, wasn’t this the point of the Athenian Democracy? Why should it be so different when it comes to economics? May the Greeks show us the way to their forgotten wisdom.