Market and Political Power Interactions in Greece: A Theory

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Abstract

For nearly forty years, economic growth in Greece has been weak. Recently, moreover, this country is suffering from a persisting economic crisis that goes beyond the usual business cycle recessions. In this paper, we develop a neoclassical growth model of market and political power interactions that captures the main features of the economic and political system of Greece. The model incorporates the insiders-outsiders labor market structure and the concept of an elite government. Outsiders form a group of workers that supply labor to a competitive private sector. And, insiders form a group of workers that enjoy market power in supplying labor to the public sector and influence the policy decisions of government, including those that affect the development and maintenance of public sector infrastructures. This leads to labor misallocation and inefficient fiscal policies. Thus, despite the fact that expanding public sector output has a positive effect on growth, eventually this is counterbalanced by the labor misallocation and inefficient tax policy outcomes. The interaction of these effects, over time, explains the dismal growth performance of Greece and reveals as an important factor behind its present crisis, the existence of a growth reversal phenomenon. The model proposed in this paper may be applicable for other countries that have a similar politicoeconomic structure with Greece, namely other Southern European countries.

Keywords: theory