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EU safety net not quite enough to break Greek fall
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Author : Paul Taylor

By Paul Taylor

Paul Taylor is a Reuters columnist. The opinions expressed are his own.

The thing about a safety net is that it all depends where you hang it. Remember those childhood trips to the circus. The net hung low enough for the tightrope walker to be clearly visible to the crowd and for the prospect of a fall to elicit gasps of fear, but high enough to prevent life-threatening injuries. The financial safety net that euro zone leaders agreed last month to provide for debt-stricken Greece fails the circus test. Not only did the agreement specify, at European ringmaster Germany's insistence, that Greece would have to have almost hit the deck before it could be rescued. But even then, it would require a unanimous decision of the 16 states sharing the single European currency, giving Berlin the final say on whether the safety net is strung out at all. One corner would also be held by the International Monetary Fund on conditions that have yet to be worked out. No wonder international investors did not stampede to buy the first Greek bonds on offer last week. On the contrary, some ran in the opposite direction, selling Greek debt on the secondary market. The premium investors charge for holding Greek debt rather than German 10-year bunds widened by nearly 50 points in a week to above 350 bps. Higher coupons add to Greece's debt service costs, making it still harder to reduce its budget deficit from 12.9 percent of gross domestic product last year to below the European Union's ceiling of 3 percent by the end of 2012. PIMCO, the world's largest bond fund, said it regarded Europe's action as ineffective in fixing Greece's problems -- a 300 billion euro ($405 billion) debt pile that exceeds the country's 240 billion euro annual output.

GREECE QUARANTINED?

The market reaction suggests the EU deal may have achieved Germany's objectives -- to stabilise the euro and avert any risk of contagion spreading to other euro zone countries -- without meeting Athens' urgent need to lower its borrowing costs. The euro recovered from a 10-month low of $1.3267 to stand at around $1.3550 by the end of last week. The bond spreads of other peripheral euro zone countries that might be the next dominoes to fall if Greece slides closer to default, narrowed. Portugal, Spain, Ireland and Italy can breathe more easily. The European Commission said last week that while all have lost competitiveness and need structural reforms, "Greece is in a league of its own here, combining large and persistent fiscal imbalances and protracted losses of competitiveness." A European Central Bank decision to extend softer collateral rules means holders of Greek debt no longer face a guillotine if a single ratings agency downgrades Athens' sovereign rating. That has averted a potential chain reaction of solvency problems for Greek but also French and German banks. So the rescue plan has fulfilled, at least for now, the goal set by EU leaders on Feb. 11 to "safeguard financial stability in the euro area as a whole" -- but by quarantining the Greek problem, not solving it.

WORST OF BOTH WORLDS?

Athens may have got the worst of both worlds, which Prime Minister George Papandreou described as draconian IMF-style austerity measures without cheap IMF money. The Brussels accord effectively bars Greece from exercising its right as an IMF member to approach the global lender directly for assistance. According to a source familiar with the negotiations, the first emergency help would likely come in bridging loans from euro zone states with the least complicated disbursement process, such as France, rather than the IMF. Both the Greeks and their EU partners are adamant that the contingency plan is meant to be a sort of nuclear deterrent that never has to be used. On current trends, this is unlikely to hold. Debt agency chief Petros Christodoulou says Athens has covered its borrowing needs for April, but it needs to refinance 8.5 billion euros of maturing 10-year bonds on May 19. That could be crunch time for Greece unless events over the next six weeks change investors' minds. Papandreou's Socialist government has to report to Brussels in early May on progress in implementing spending cuts and revenue increases, and to outline plans for longer-term budget savings including a major pensions reform. If it can show that deficit reduction is on target or ahead of schedule, and that unsustainable longer-term liabilities are being brought under control, it can expect a positive assessment from the Commission. Whether that will be enough to lower its borrowing costs or persuade foreign banks, insurers and pension funds to buy more Greek debt in the next funding round remains to be seen. But for now, the German circus master seems content to watch the Greek tightrope walker teeter a little longer on his wire.

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