Comment

Τι έγινε τελικά μετά τη σύνοδο του Ιουλίου 2011

A grand bargain that cannot end the crisis

Wolfgang Münchau

Did Europe's leaders save the euro last week? There is good news, bad news and really bad news.

The good news is that a new permanent crisis resolution mechanism has been put in place starting in 2013. This European Stability Mechanism (ESM) will be a supranational institution, established by international treaty. By mid-2017, it will be properly funded, with a fully paid up capital base of €80bn. This should be sufficient for a fund with a lending ceiling of €500bn. So, from 2018, the eurozone will be able to tackle future crises.

The bad news is that the various resolutions made this week by European Council will not be enough to carry us through the current crisis. The discussion about the ESM is also a perfect case study of what is going wrong at the moment. It therefore merits closer scrutiny.

Early last week, European finance ministers agreed a relatively straightforward capital structure for the ESM. It would have a total capital of €700bn, of which €80bn would actually be paid in. The rest would be "callable" capital. This means that the fund can ask shareholders to supply new capital, if existing capital gets wiped out.

The problem with callable capital is a "can't pay, won't pay" scenario, since the member states all guarantee each other. For example, do we really believe that Italy – a country with public sector debts of 120 per cent of gross domestic product – is in a position to find tens of billions for the bail-out of another member state? Italy's share in the ESM is nearly 18 per cent, slightly less than France, at 21 per cent. If something bad happens, Italy would share a big responsibility. What if Italy, or indeed somebody else, cannot honour its commitment?

The idea behind the paid-in capital is to provide a buffer, so that the system can deal with problems more easily. But the idea of a properly funded ESM suffered a surprise setback last week. German MPs suddenly panicked at the prospect of having to put up €11bn in 2013 – an election year, for which Germany's ruling coalition had earmarked a tax cut. So Angela Merkel went to Brussels on Thursday and demanded that there should be no upfront payment, and that money would be phased in over five years, instead of three. To comply with the rule that the paid-in capital has to be at least 15 per cent of the ESM's loan volume, the German chancellor agreed to provide additional resources if that became necessary.

But here is the crux: Germany and France, whose sovereign bonds have a triple A rating, would not need to put up actual money to cover any shortfall of paid-in capital. A guarantee would do. But countries with lower ratings, such as Italy, Spain, and, yes, Portugal, Ireland and Greece, would have to pay cash. So we are in a perverse situation. Countries with easy access to capital can provide cheap guarantees, while the weaker countries must put forward cash. In fact, the biggest risk to Italy's future solvency has nothing to do with its own debt. It is the country's exposure to the eurozone crisis mechanism.

> **The really bad news is that the political systems of eurozone members are not prepared for what is about to hit them**

Moreover, since this guarantee has to serve as the equivalent of a pre-paid cash payment, a guarantee by a non-triple A rated country would not cover the shortfall. I understand that the summit just fudged this issue: the Italians walked away from the table with a different understanding of what had been agreed.

Of course, all of this might not matter. It is conceivable that most lending operations will be agreed before 2013 under the existing mechanism – the European Financial Stability Facility (EFSF). It runs out in that year, but all loan tranches paid until then will continue under the old umbrella. Because these will not be transferred to the ESM, the new mechanism might get a little breathing space. And countries will also have time to put up the capital.

But just imagine if one of EFSF's debtors defaults. The EFSF has no capital, only guarantees. So the success of the exercise would depend on the creditors' ability to make good on their promises, without getting themselves into trouble. This would be a highly strung exercise. The EFSF's credit has equal status to privately held bonds. This means that if a country defaults everyone gets hit equally. Governments would have to pay immediately. What is intended as a rescue mechanism would then unwittingly become a crisis propagator. This is why it is so important to establish a mechanism with enough paid in capital from the outset, rather than relying on guarantees. It would also have been a good idea to fold the EFSF into the new mechanism right from the beginning, rather than letting them coexist.

But now for the really bad news: the domestic political systems in the eurozone's members are not prepared for what is about to hit them. If the German coalition convulses at the prospect of an €11bn capital injection, what might they say if confronted with a much larger request to make good on a loan guarantee? Unlike a simple capital provision for the ESM, the payment of a guarantee would require an offsetting fiscal correction at home. Just imagine the politics of a cross-border bail-out that requires a cut in domestic welfare payments.

The irresistible force of EU-level crisis resolution will eventually come into conflict with the immovable object of national politics. Last week's debate on the ESM is an early warning of what lies ahead.

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A cap on immigrants will fit business nicely

David Goodhart

Britain's immigration cap comes into force on April 6. The educated consensus is that this cap and the associated pledge to reduce net immigration to "tens of thousands" a year by the end of this parliament – from the current level of 226,000 – is a populist gesture that won't work. This view is wrong. In fact, the cap is likely to work and without doing much damage to British business or higher education.

Critics note that the government cannot control people coming from the European Union or asylum seekers, while much of the family reunion route is protected by human rights law. Moreover, the two flows it can target (and is therefore reducing) are just the kind of useful