taxes, more regulation and dirigiste industrial policy. Some of them still talk as if economic growth were a problem in itself—which is one reason they opposed the huge infrastructure project at Stuttgart's railway station. Support for free trade and free markets tends to come very far down the agenda, if it features at all.

Much of this is just the normal talk of protest and opposition. Like all parties, the Greens tend to change their tune when they get closer to power, just as they did when they went into coalition with the SPD in the federal government of 1998. In this sense, indeed, Baden-Württemberg should now offer a test of how responsible the Greens are when they actually lead a government. The state has a highly successful economy and boasts the country's lowest unemployment. It also hosts some of Germany's biggest exporters, including several large carmakers. Mr Kretschmann will surely not want to threaten any of this.

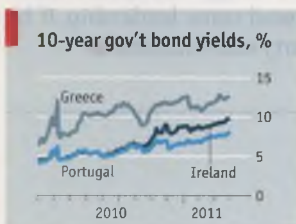
Further in the future looms another big challenge for his party, one that could have a bearing on Mrs Merkel's future. At present the Greens naturally seek to form coalitions with the SPD, as they will once again do in Baden-Württemberg, just as the FDP tends to look towards joining up with the CDU. But the success of the FDP, at least until recently, was based largely on its readiness to go into government with either of the two big parties. The Greens should follow suit. A first attempt at a Black-Green coalition in the city-state of Hamburg fell apart last November. The ultimate test of how serious a party the Greens have become will be how soon they are prepared to try once again to work with the CDU, in a state or even, after 2013, at the federal level. ■

'e euro zone's periphery

They're bust. Admit it.

6

Greece, Ireland and Portugal should restructure their debts now



IT IS a measure of European politicians' capacity for self-delusion that Angela Merkel, Germany's chancellor, called the euro-zone summit on March 24th-25th a "big step forward" in solving the region's debt crisis. Something between a fudge and a failure would be more accurate. The leaders fell short on almost every task they set themselves. They agreed on a "permanent" rescue mechanism to be introduced in 2013, but couldn't fund it properly, because Mrs Merkel refused to put up money her finance minister had pledged. The Brussels gathering did 'ttle to help Greece, Ireland and Portugal, the zone's most trou-·d economies. Their situation is getting worse—and Europe's ..aders bear much of the blame.

Portugal's prime minister resigned on March 23rd after failing to win support for the fourth austerity package in a year. The country's credit rating was slashed to near-junk status on March 29th, while ten-year bond yields have risen above 8% as investors fear Portugal will have to turn to the European Union and the IMF for loans. The economies of both Greece and Ireland, Europe's two "rescued" countries, are shrinking faster than expected, and bond yields, at almost 13% for Greece and over 10% for Ireland, remain stubbornly high. Investors plainly don't believe the rescues will work.

They are right. These economies are on an unsustainable course, but not for lack of effort by their governments. Greece and Ireland have made heroic budget cuts. Greece is trying hard to free up its rigid economy. Portugal has lagged in scrapping stifling rules, but its fiscal tightening is bold. In all three places the outlook is darkening in large part because of mistakes made in Brussels, Frankfurt and Berlin.

At the EU's insistence, the peripherals' priority is to slash their budget deficits regardless of the consequences on growth. But as austerity drags down output, their enormous debts—expected to peak at 160% of GDP for Greece, 125% for Ireland and 100% for Portugal—look ever more unpayable, so bond yields stay high. The result is a downward spiral.

As if that were not enough, the European Central Bank in Frankfurt seems set on raising interest rates on April 7th, which will strengthen the euro and further undermine the peripherals' efforts to become more competitive (see page 66). Some politicians are still pushing daft demands, such as forcing Ireland to raise its corporate tax rate, which would block its best route to growth. Most pernicious, though, is the perverse logic of the euro zone's rescue mechanisms. Europe's leaders won't hear of debt reduction now, but insist that any country requiring help from 2013 may then need to have its debt restructured and that new official lending will take priority over bondholders. The risk that investors could face a haircut in two years' time keeps yields high today, which in turn blights the rescue plans.

Home truths from Washington

This newspaper has argued that Greece, Ireland and Portugal need their debt burdens cut sooner rather than later. That case is stronger than ever, not only because today's approach is failing but because the risks restructuring are falling. The spectre of contagion is receding. Spain, whose bond yields have fallen and whose spreads with Germany have tightened, has distanced itself from Portugal. Behind the scenes, sovereign-debt specialists are devising ways to minimise the impact of an "orderly restructuring" on banks. Most banks in the core of the euro zone can withstand a hit from the three small peripherals.

The big obstacle is not technical but political. Since many at Europe's core, particularly the ECB, remain implacably opposed to debt restructuring, the pressure has to come from elsewhere—not least from the peripheral economies themselves. Ireland's new government is talking about forcing the senior bondholders of its bust banks to take a hit. Greece should stop pretending that it can bear its current debt burden and push for restructuring. But the best hope lies with the IMF. Its economists have the most experience of debt crises. Some privately acknowledge that debt restructuring is ultimately inevitable. It is time the Fund's top brass said so publicly and, by refusing to lend more without a deal on debt, pushed Europe's pusillanimous politicians into doing the right thing. ■