104

IMERINI
newspaper | English Edition

CENTER STAGE
LONDON SHOWS THAT SHINE
PAGE 10 | CULTURE

Herald Tribune
OF THE NEW YORK TIMES
GLOBAL.NYTIMES.COM

ABEDIN TAHERKENAREH/EUROPEAN PRESSPHOTO AGENCY
.t evoked the siege of the U.S. Embassy in November 1979, after the Iranian revolution.

High marks for Greece as it headed for disaster

NEW YORK

Missteps by Moody's reflect industry rife with errors and ethics issues

BY JULIE CRESWELL AND GRAHAM BOWLEY

In a stern pronouncement, Moody's Investors Service this week warned of rising prospects for multiple defaults by countries in the euro zone and credit-rating downgrades of nations across Europe if leaders failed to resolve the spreading debt crisis.

That is a sharp contrast to the optimism that Moody's displayed two years ago toward Greece, the epicenter of the current crisis, as the tiny country plowed ahead with its borrowing binge as its fiscal condition eroded.

Moody's held off on dropping its strong "A" rating on Greece despite growing political turmoil and economic woes through 2009. Investor fears about the country's short-term financing needs were "misplaced," Moody's said in a report in early December 2009.

Twenty days later, after a review, the agency downgraded Greece's rating, the last of the major ratings agencies to do so.

After that, the ratings of the debt-ridden country went into a virtual free fall, and within six months Moody's assessed it as junk, or much riskier to investors.

"If you look at the fact that this is going to be a country that is going to default on its debt, and two years before it was still single A, that is a very, very precipitous fall," acknowledged Pierre Cailleteau, who was head of sovereign debt at Moody's until he left in the spring of 2010. He rated the rating agency's performance as mediocre, but added that it could have been worse.

The rapid deterioration, critics say, underscores how the credit-ratings agencies that judged Greece's debt as investment grade for most of the last decade missed, or badly misread, signs of trouble. Moody's held its rating steady even after Greece in 2004 admitted lying about its deficits to join the euro in 2001. Now, the ratings agencies are under fire from European regulators about whether their recent downgrades of Italy and Spain have worsened an already tenuous situation.

What happened at Moody's offers a rare look inside the sometimes fierce debates over Greece's deep problems, how the prevailing belief that Europe would not let Greece default on its obligations drowned out opposing views, and how in hindsight the agency could get it so wrong.

The lapses by Moody's before last year helped embolden Greece to sell ad-
RATINGS, PAGE 15

SETBACK FOR E.C.B. BOND BUYING
New questions surfaced Tuesday about how long the European bank could avoid bigger moves to stem the crisis. PAGE 14

FINANCE MINISTERS FACE DECISIONS
With market pressure intense, euro zone ministers try to deliver on promises to preserve the currency union. PAGE 14

...r heads up

...s but ab-
...economic
...lled at a
... mugs, key
...l with pic-
...u Kyi, the
...er, whose
...during two
...hip.
..., rapid and
...er some of
...cs.
...ese last few
...' said Daw

Cho Cho Kyaw Nyein, an opposition politician and former political prisoner whose family suffered years of persecution by the military.

"To be frank, in the very beginning, I didn't believe a word of what they were saying," she said of the new government, which came to power in March. "Now I believe what is happening is for the good of the people."

Outside Ms. Aung San Suu Kyi's house, workers have laid a fresh layer of sod and repainted the gates in anticipation of a visit by Hillary Rodham Clinton, the U.S. secretary of state, who was to arrive in Myanmar on Wednesday in a significant vote of confidence for the new government.

Making the first visit by a U.S. secretary of state since 1955, Mrs. Clinton will be touring a country in the midst of transformation from military dictatorship to nascent democracy. The changes have been so sudden that many people, scarred by years of crackdowns and surveillance by the secret police, are not sure whether to trust the sincerity of a government that is largely made up of former generals.

Daw Thandar, a middle-aged owner of a clothing shop in Yangon's bustling city center, said she sensed optimism in the air. "Politics used to be an evil word, but now people are talking about it, even on the sidewalks," she said.

But in a sign of the fear that still lingers here, she did not want her full name in print.

"I'm not 100 percent sure yet the changes are real," she said. "One of my
MYANMAR, PAGE 5

...ERALD TRIBUNE
...Aung San

Britain says austerity plan is falling short

LONDON

BY JULIA WERDIGIER

On the eve of a huge strike by public-sector workers to protest austerity measures, the British government said Tuesday that it was falling behind with its deficit reduction plan and that the measures would drag on for two more years.

The chancellor of the Exchequer, George Osborne, said Tuesday that because of the slowdown in the euro zone, British economic growth this year and next would be slower than forecast in March and that "debt will not fall as fast as we'd hoped."

He added that Britain could avoid a recession next year only if the euro zone found a solution to its current crisis.

"We'll do whatever we can to protect Britain from this debt storm," Mr. Osborne told a packed Parliament in an update on the economy. "If the rest of Europe heads into a recession, it may be hard to avoid one here in the U.K."

Britain's biggest public-sector unions called for a strike Wednesday that was expected to cause major delays at airports and hospitals and shut some schools. More than two million people, including teachers and other government employees, are expected to go on strike over a dispute with the government about pensions, according to the Trades Union Congress.
BRITAIN, PAGE 15

...y exits
...eters,
...oviet
...ye.

NYT

VIEWS

Joe Nocera

Many Germans and Americans can't get past the fact that they are being asked to bail out "club med" countries or underwater homeowners. This self-righteousness is self-destructive. PAGE 9

Frank Bruni

More than two weeks after he was ousted from power, Silvio Berlusconi continues to rant and rave. Italians should ignore him, and start to prepare — really prepare — for the future. PAGE 9

ONLINE

Muscle put to Nicaragua media

While European observers called the recent election tally in Nicaragua "opaque and arbitrary," television stations were hailing a "resounding victory" for President Daniel Ortega. The jubilant imagery reflected one of Mr. Ortega's biggest accomplishments in the five years since he returned to power: his tightened grip on the news media. **global.nytimes.com/americas**

...PM

	PREVIOUS
	$1.3310
	$1.5500
	¥77.940
	SF0.9230

STOCK INDEXES TUESDAY

▲ The Dow 1:30pm	11,592.87	+0.61%
▲ FTSE 100 close	5,337.00	+0.46%
▲ Nikkei 225 close	8,477.82	+2.30%

OIL NEW YORK, TUESDAY 1:30PM

▲ Light sweet crude	$99.72	+$2.04

How credit rating agencies missed the boat on Greece

RATINGS, FROM PAGE 1

ditional billions in sovereign debt — a record $67 billion in 2009 alone — and encouraged investors to deepen their exposure to the shaky country. Now some of those buyers face 50 percent losses on the bonds — loans that carried the agencies' stamp of approval but that Greece can no longer afford to pay off. Had the ratings agencies been more skeptical of euro zone countries borrowing beyond their means, critics say, that might have slowed the debt carousel for Greece and others.

The higher credit ratings made it "easier to raise debt than taxes," or take on other unpopular and painful economic adjustments, said Barbara Ridpath, who was head of rating activities in Europe for Standard & Poor's, a Moody's competitor, between 2004 and 2008.

Wolf Klinz, a member of the European Parliament from Germany and author of a critical report on credit rating agencies published last year, said "The credit rating agencies failed in their job. They held on artificially too long to their original rating. They should have started earlier."

The agencies have defended their performance, noting that investors themselves were much more optimistic than the agencies, with bond markets assigning interest rates to Greek debt at levels that were just slightly above what Germany was paying.

"The market was scarcely differentiating between any of the 16 sovereign members of the euro zone," said David Beers, head of S.&P.'s global ratings business, during a British parliamentary hearing last summer. "We differentiated these opinions from the outset. The market ignored those opinions for many years."

In an e-mailed statement, a spokesman for Moody's agreed, saying market perception for Greece was equivalent to a triple-A rating, "while Moody's rating was considerably lower."

The current crisis was years in the making and borne of Greek leaders who misled the European Union with false economic statistics to gain entry to the euro; of European policy makers who turned a blind eye to Greece's deceptions; of banking regulators who deemed sovereign debt virtually risk free; and of banks and other investors who, in their hunger for profits, joined in the group-think that the euro zone would never allow a member to default.

The credit rating agencies' missteps on Greece's sovereign debt are the latest chapter for an industry long dogged by allegations of wrong calls and conflicts of interest. The U.S. energy company Enron was rated as "investment grade" by the three major agencies just days before it filed for bankruptcy in 2001. In the financial crisis, the agencies were accused of putting top ratings on questionable mortgage-related securities to continue collecting rich fees.

What most shaped Moody's view on Greece was the fact that few inside the agency could conceive that euro zone members would allow one of their own to become a deadbeat.

"We never thought of such a catastrophic stress scenario in the euro zone," said Sara Bertin, who was Moody's lead analyst on Greece before leaving spring of 2008. "That's the issue rating agencies had with subprime. That's the issue ratings agencies had in Asia, and that's the issue the ratings agencies have in Europe."

The sovereign debt team inside Moody's — a small group of about a dozen people with diverse backgrounds and eclectic interests — traveled the world, digging into individual country statistics, meeting with leaders and policy-makers. The aim was to figure out where each country stood on its global measuring stick of creditworthiness.

Ms. Bertin, an economist who joined Moody's in 2001 from the International Monetary Fund and grew up in Lyon, said she enjoyed the free-flowing banter and debate, even when the group disagreed, as it often did.

Shortly after Greece became part of the euro zone in 2001, a "fierce debate" erupted in a committee meeting as some individuals argued the country should be upgraded to be levels nearly on par with Italy.

"We wanted to upgrade the country on the belief that Greece was now part of the euro zone and that nobody was ever going to default and that everything was safe," Ms. Bertin recalled. "But how many notches was the nature of the debate."

The emphasis, she and others said, had shifted somewhat from an economic and financial analysis of the country to a bet that policy makers would keep the euro zone together.

Rated a weak investment grade in the mid-1990s, Greece was upgraded to A2 when it joined the euro and to A1 for most of the 2000s. Armed with strong ratings, Greece ratcheted up its borrowing in global credit markets at historically low yields. In 2002, Greece paid 5 percent on its 10-year government bonds, far below the 15 percent it paid seven years earlier.

But in the autumn of 2004, Greek officials stunned European policy makers when they acknowledged that the country's budget deficit had exceeded the E.U.'s ceiling of 3 percent of gross domestic product every year since 1997. The European Commission sued Greece for disguising its deficits and said it should never have joined the euro.

KOSTAS TSIRONIS/BLOOMBERG NEWS

Prime Minister Lucas D. Papademos and Finance Minister Evangelos Venizelos in Parliament in Athens. Greece had always been one of the lowest-rated countries in the euro zone.

CNBC

Pierre Cailleteau, once a Moody's executive, said action on Greece was mediocre.

The revelation surprised few inside Moody's.

"I remember whenever you would discuss Greek fiscal numbers, it was always with a smile on your face because you knew these were not always the most accurate statistics available," said Vincent J. Truglia, a Moody's veteran who headed the sovereign group when he left in 2007.

Partly as a result of the statistics fiasco, S.&P. cut its rating of Greece, but only modestly to A from A+. Moody's kept its rating unchanged, arguing that its view was still supported by high economic growth and Greece's membership in the euro zone.

In January 2007, Moody's changed its outlook on Greece's rating to "positive" after Greek officials said its budget deficit had finally fallen below 3 percent.

"The growth was there. The shipping industry was getting steam again," said Ms. Bertin, who was in favor of the upgrade. "One story that I really liked was that Greece was developing its own banking know-how and exporting it to the Balkans, places like Albania."

During the go-go years of 2005 to 2007, bankers sometimes called the analysts to complain that they were missing Greece's growth story, said Mr. Cailleteau, declining to name the bankers. Banks would earn fees from underwriting bonds and the credit rating agencies earned fees from the countries issuing the debt.

According to Spyros Papanicolaou, who served as general director of Greece's Public Debt Management Agency from February 2005 to February 2010, Moody's was paid $330,000 to $540,000 each year by Greece to rate its debt. The other agencies received the same amounts.

"We had no choice," Mr. Papanicolaou said by telephone. "Without the ratings, we couldn't sell bonds, we couldn't go to the markets."

In an e-mailed statement, a spokesman for Moody's said the rating agency did not comment on fees, but added that the "commercial and analytical aspects of our business operate separately."

But inside Moody's in 2007, fees from the lucrative business of rating U.S. subprime mortgage-related securities were beginning to evaporate. In response, the company began cutting costs. As part of that, Ms. Bertin said, sovereign debt analysts, who typically covered 10 countries, were advised to spend less time inside those countries.

In an e-mailed statement, Moody's said the agency has added resources to its sovereign team since the beginning of the financial crisis.

In 2008, Moody's also introduced a new methodology for evaluating countries.

"It was called a methodology, but it was more of a checklist," said Ms. Bertin, who said she feared the word "methodology" suggested to investors that it was rooted in deep empirical analysis, which it was not.

Mr. Cailleteau, who introduced the methodology, said it provided a clearer way of thinking about the rating of a country, based on factors like government institutions and the wealth of the country. Analysts may have been encouraged to spend slightly less time on a visit a country, for example two days instead of three, he said, but only so resources could be directed toward high-level thinking back in the office.

By late 2008, Greece was unraveling. A national strike froze the country late that year, the government was in chaos and riots erupted after police killed a youth. Nervous investors pushed up Greek interest rates.

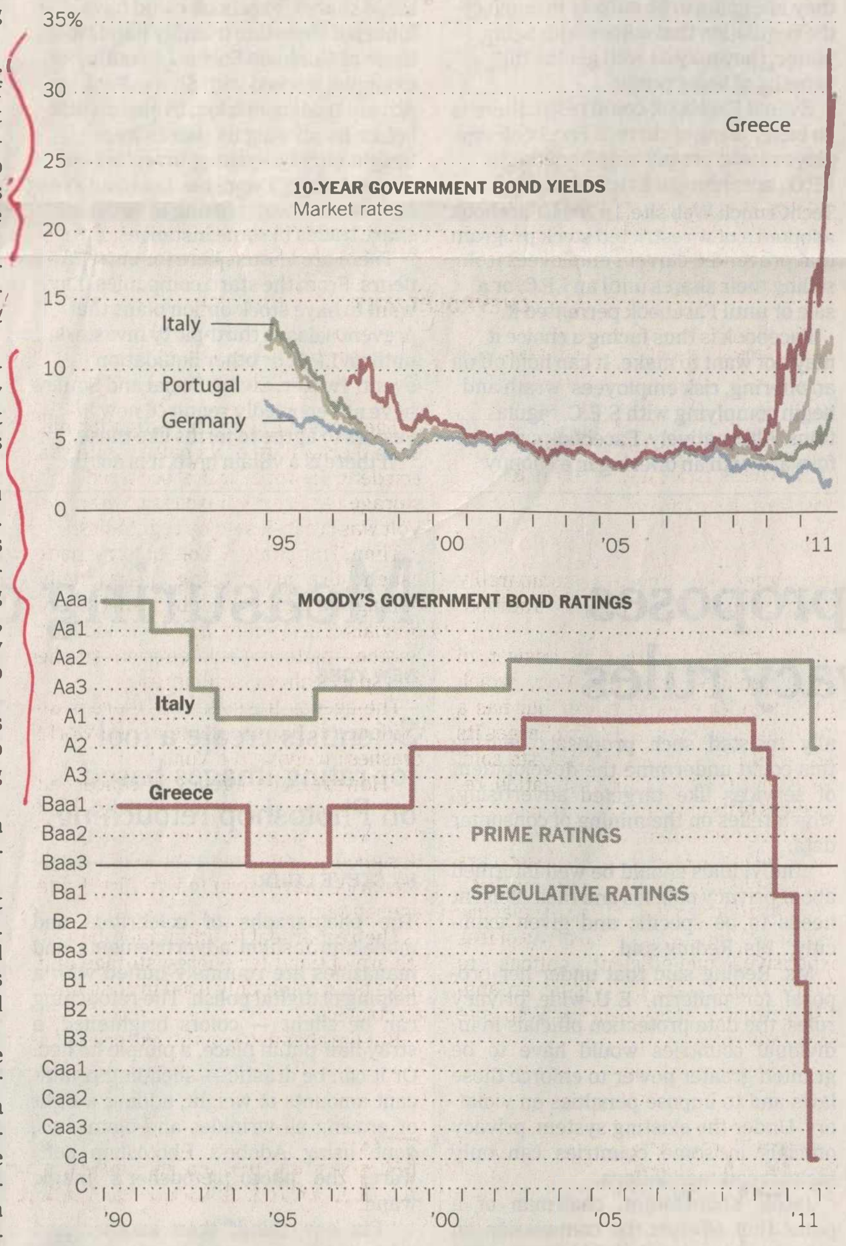
In February 2009, a month after S.&P. had knocked Greece down to A- from A with a negative watch, Moody's modestly altered its A1 outlook to stable from positive.

Joan Vidra, who worked in the Moody's sovereign debt group from 1995 until early 2009, said there were "disparate voices" but they did not win out to those who saw no need to lower Greece's rating to levels that would indicate a default risk.

"Going into the global credit crunch, the perspective held by the agency was that Greece had a relatively low rating," Ms. Vidra said. "The agency was very, very delayed in changing its view point."

Fractured zone

The debut of the euro in 1999 brought the countries that had adopted it into economic alignment, and investors and credit rating agencies started treating them as alike. But structural differences remained and now some of the weaker economies are trying to avoid default — putting pressure on the euro's economic union.



Sources: Thomson Reuters Datastream; Moody's Investor Service

Meanwhile, Greece hit the credit markets hard in 2009, raising a record $67 billion, more than double what it had raised a year earlier, according to Thomson Reuters.

The differences inside Moody's resurfaced again that autumn in a hastily arranged conference call with 15 analysts from around the world after a new Greek government admitted that the country's finances were far worse than the previous government had revealed.

Some of the analysts on the call argued that Greece needed to be downgraded swiftly. But others worried about worsening Greece's position, or did not want to make a call that they might later have to reverse.

Ultimately, the analysts decided to wait, but agreed to a three-month review with a downgrade in mind.

Greek yields began spiking higher in early December amid rumors that the European Central Bank would stop accepting Greek government bonds from banks as collateral for short-term loans.

On Dec. 2, 2009, Moody's rushed out a report titled, "Investor Fears Over Greek Government Liquidity Misplaced," arguing that only if the E.C.B. tightened its criteria or if Greece's rating fell by several notches "would liquidity risk be material."

Days later, Fitch Ratings, another competing agency, which had already downgraded Greece in October, cut it again to the lowest investment-grade levels. The next week, S.&P. followed suit.

Mr. Cailleteau convened another conference call from Moody's offices in the Canary Wharf area of London. The roughly 15-member group, with one analyst designated as a prosecutor to test the debate and specialists from other divisions including emerging market specialists brought in to provide outside perspective, verbally cast their votes.

While some still believed Greece needed time to turn itself around, the group agreed on a downgrade, but only by one level, to A2, with a negative outlook.

But the group began meeting monthly throughout 2010 as some analysts wanted to downgrade further and faster. The meetings grew more argumentative but the majority, including Mr. Cailleteau, still believed that richer European countries would support Greece.

"The timing and size of subsequent downgrades depended on which position would dominate in rating committees — those that thought the situation had gotten out of control, and that sharp downgrades were necessary, versus those that thought that not helping Greece or assisting it in a way that would damage confidence would be suicidal for a financially inter-connected area such as the euro zone," Mr. Cailleteau wrote in an e-mail.

Finally, in June of 2010, shortly after European leaders had agreed to a $147 billion rescue package for Greece, Moody's downgraded the country's debt by four notches, knocking it into junk territory. S.&P. had downgraded Greece weeks earlier; Fitch waited until January 2011.

The rapid descent of the ratings was labeled a "failure" of the credit rating agencies in a report issued last year by the International Monetary Fund.

In June 2011, just before European leaders agreed to a second rescue for the country that included private bondholders accepting losses, Moody's knocked the rating down by another three notches, to Caal.

A spokesman for Moody's wrote in an e-mailed statement that its ratings actions reflected the impact "of rapidly evolving credit conditions during this time."

While Greece was always one of the lowest-rated countries in the euro zone, the Moody's analysts felt that the strongest would drag along the weakest, said David H. Levey, a co-head of the sovereign debt group at Moody's until 2004.

"When you get multiple ratings or large ratings downgrades, it is fair to say as a criticism that the ratings were too high in the first place," said Mr. Levey. "Looking back, that indicates that the assumptions being made in the past were too optimistic."

Niki Kitsantonis contributed reporting from Athens.

With strike looming, Britain acknowledges that austerity is falling short

BRITAIN, FROM PAGE 1

Mr. Osborne called on the unions to reconsider the strike action and return to the negotiating table. "I'd ask the unions, Why put jobs at risks?" he told Parliament. "Call off the strike."

The unions said the strike would go ahead as planned. Len McCluskey, general secretary of the trade union Unite, criticized Mr. Osborne's economic strategy and compared him with "a pilot who has put his plane into a tailspin and is now wrestling desperately with the controls as the aircraft rapidly loses height."

The government said British households, which are already squeezed by higher food and electricity prices, would have to endure an additional two years of austerity measures until 2017. The economy is growing slower than forecast, hurting Mr. Osborne's initial 2010 plan to eliminate the budget deficit within five years.

It would also require Britain to borrow an additional £111 billion, or $172 billion, through 2015, a step Mr. Osborne was eager to avoid. The austerity measures would now drag on far beyond the next general election, currently scheduled for 2015.

The British economy will grow 0.9 percent this year, less than the 1.7 percent predicted earlier, and 0.7 percent next year, the Office for Budget Responsibility forecast Tuesday. The agency predicted the economy would then pick up and grow 2.1 percent in 2013. Debt as a share of gross domestic product would peak at 78 percent in the fiscal year ending in 2015, higher than the 71 percent initially predicted.

Amid fierce criticism from the opposition Labour Party, Mr. Osborne said Tuesday that he would stick to his austerity plan, which includes more than 600,000 job cuts in the public sector and other spending curbs, but that it would still take longer for the debt load to shrink.

Because of that, the government said it would cap pay increases for public-sector workers at 1 percent for two years after the end of the current pay freeze.

The step was part of a small set of measures presented Tuesday, which also includes an increase in a bank levy, to generate extra revenue to invest in infrastructure projects and to fight youth unemployment.

But it added to the infuriation of workers' representatives, who said the government was now not only "raiding" pensions but wages as well.

Howard Archer, chief economist for Britain at IHS Global Insight, said Mr. Osborne lacked the room for maneuver to offer any investments or tax cuts that could help the economic recovery.

"The economy is staring recession in the face again; he has no money to spend and events in the euro zone pose major downside risks over which he has no control," Mr. Archer said.

The Labour Party said the new forecast meant that Mr. Osborne's strategy to cut the budget "is in tatters" and that "plan A has failed colossally." The Labour Party called on Mr. Osborne to "change course before it's too late" and scale back an aggressive debt reduction plan that was choking off the economy.

But Mr. Osborne argued that an early implementation of the deficit plan last year helped Britain to keep its borrowing costs low and avoid a situation like in Greece or Italy, where borrowing costs became unsustainable.

Unlike the United States or the members of the euro zone, Britain already has a far-reaching austerity plan along with interest rates at record-low levels.

"If the rest of Europe heads into a recession, it may be hard to avoid one here in the U.K."

It also has its own currency, which helps keep British exports to the euro zone relatively inexpensive.

When Germany's 10-year bond yields last week rose above Britain's for the first time in more than two years, it was widely interpreted by the British government as a vote of confidence in Britain's budget reduction efforts.

But the dampened outlook released Tuesday by the budget office — combined with warnings Monday by the Organization for Economic Cooperation and Development that Britain might fall back into a recession — put pressure on Mr. Osborne's plan.

Mervyn A. King, governor of the Bank of England, also warned Monday that Britain was increasingly threatened by the crisis in the euro zone.

Some analysts said Mr. Osborne would be wrong to peg his debt reduction plan to the relatively low borrowing costs Britain currently enjoys. "The profound weakness of the macroeconomy means the U.K.'s position cannot be taken for granted and the risk of a loss of market confidence and a sharp rise in gilt yields remains live," analysts at Barclays Capital wrote in a note Tuesday.

Mr. Osborne's initial plan — that the private sector would help create jobs for the more than 600,000 public-sector workers expected to lose theirs as the government cuts spending — is jeopardized as Britain's economic growth stalls. Unsettled by a worsening crisis in the euro area, many companies have frozen hiring and other investments.