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Shape of last-ditch eurozone deal emerges

7

By Quentin Peel in Berlin, Ralph Atkins in Frankfurt, and Joshua Chaffin in Brussels

Mario Draghi at the European parliament on Thursday

The shape of the grand plan that European Union leaders hope to agree in Brussels next week to stem the eurozone's debt crisis is increasingly clear.

Leading players in the negotiations – Angela Merkel, German chancellor, Nicolas Sarkozy, French president, Mario Monti, Italian prime minister, and Mario Draghi, his compatriot at the head of the European Central Bank, plus Herman Van Rompuy, the European Council president in Brussels – seem to be singing from the same song-sheet.

Essential details, however, are still the subject of intense negotiations that could run right up to the EU summit on December 9, not just between France and Germany, but with the European Commission – the EU executive – and smaller member states.

The deal involves accelerated agreement on what Mr Draghi described on Thursday in the European parliament as a "fiscal compact" between the 17 eurozone members to enforce much stricter budget discipline and debt control throughout the monetary union.

Ms Merkel and Mr Sarkozy have promised to submit joint proposals for EU treaty changes on that score next week, although they have yet to agree on some critical questions, such as whether sanctions should be automatic for rule-breakers.

Treaty change is what Ms Merkel has been fighting for to make her idea of "fiscal union" enforceable, against considerable opposition from her partners. She won another key ally on Thursday – Donald Tusk, the Polish prime minister, in addition to Mr Draghi. On Friday she may reveal more to the German Bundestag.

The other two pillars of the package the ECB president outlined are also clear in principle: agreement on a reinforced firewall to prevent contagion from one eurozone country to the next; and tough national measures in the most debt-laden states to restore confidence in the markets.

Eurozone finance ministers agreed this week on ways of "leveraging" the €440bn finances of the European Financial Stability Facility – the eurozone rescue fund – at least to double its resources. It is less than many hoped. It will be a few weeks before ministers know if outside investors will back their ideas with hard cash. The International Monetary Fund might provide an extra firebreak, if its non-European members can be persuaded to agree.

National measures to cut spending, raise taxes and introduce reforms to boost growth and competitiveness will be announced by Mr Monti on Monday. The package is expected to total some €20bn, including pension reforms, and the re-imposition of a property tax. Mr Monti has promised that the "sacrifices" will be "equitable".

In Greece, the latest austerity budget – for 2012 – should be approved in the Athens parliament on December 7.

Mr Draghi's blessing for the three-pillar combination is critical. Eurozone governments, led by France, see the ECB as the only institution with the financial firepower to calm the markets in the near term, while new rules are enacted, and extra firewalls erected, in the coming months. Ms Merkel is more sceptical, but insists the ECB must decide for itself.

Mr Draghi's priorities are clear: "It is first and foremost important to get a commonly shared fiscal compact right," he said. "Confidence works backwards: if there is an anchor in the long term, it is easier to maintain trust in the short term. After all, investors are themselves often taking decisions with a long time horizon, especially with regard to government bonds."

Negotiations on the nature of that "fiscal compact" – or what both Ms Merkel and Mr Monti have called "steps towards a fiscal union" – are tough. Ms Merkel wants automatic sanctions, enforcement of the rules in the European Court of Justice, and a powerful "budget commissioner" who will blow the whistle on miscreants. Mr Sarkozy wants "political" control maintained by national governments.

The very idea of formal treaty change is still regarded with horror by some countries, such as Ireland, where a referendum would have to be held before ratification.

The other circle to be squared is to reconcile the 10 non-eurozone members in the EU, such as the UK, to much closer integration of the eurozone. Ms Merkel insists the changes, inserted in a protocol to the Lisbon treaty, will only affect the 17 single currency members.

Heads down: the work ahead

National reforms

Implementation of measures to cut deficits and improve potential growth. Italy, with its huge debt mountain, is key. Mario Monti, Italy's prime minister, will detail his reform programme at a cabinet meeting on December 5. Rome's plans will be closely scrutinised

Fiscal compact

Angela Merkel, German chancellor, is insisting on ambitious treaty changes and greater supranational oversight of government budgets. France's Nicolas Sarkozy is anxious to keep things intergovernmental. Can they bridge their differences? Can they hatch a speedy compact before longer-term treaty change?

Solidarity

It will never be explicitly stated, but the other parts of the deal can be pinned down, the European Central Bank is expected to hugely step up its intervention in eurozone bond markets. Some EU members are also insisting that commonly issued eurobonds are part of the deal

A stronger firewall

The eurozone governments need to ensure that their plans for increasing the impact of the European Financial Stability Facility through leverage arrangements and contributions from emerging economies are robust. The International Monetary Fund is also expected to make extra resources available

“We need quick, credible solutions,” one European diplomat said on Thursday. But the ECB also needs to be convinced. “I think they are prepared to do a lot more than they have done so far,” the diplomat said, “but they need a signal from the politicians. We are really against the wall.”

Additional reporting by Guy Dinmore in Rome and Kerin Hope in Athens

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