EUROPE FAILS AGAIN TO QUELL THE CRISIS

If Europe's leaders don't figure out how to help Greece and other weakened nations to grow as they reduce their debt, the consequences could be disastrous.

They blew it, again. With Greece in meltdown, raising fears of cascading bank insolvencies and deepening recession, Europe's leaders failed again this week to agree on the ambitious initiatives needed to quell the crisis.

For a few days before their Wednesday dinner meeting, it sounded as if Chancellor Angela Merkel of Germany might be ready to change her all-austerity-all-the-time tune. France's new president, François Hollande, had campaigned and won on a pro-growth agenda, and Ms. Merkel was suddenly suggesting that some stimulus for Greece and others to spur growth might be possible.

But, on Wednesday, she was again insisting on the same draconian budget cuts and the same unreachable targets as the price of aid to Greece and other indebted euro-zone nations.

By this point, there should be no debate: Austerity has been a failure, shrinking economies and making it ever harder for indebted countries to repay their debts.

The political costs are also rising. In parliamentary elections earlier this month, Greece's voters rejected candidates from the two major political parties that had agreed to a German-dictated "rescue" package, and the country has been unable to form a government since. In that vote, the far-right party, Golden Dawn, whose xenophobic members perform Nazi salutes, did frighteningly well — a warning that no responsible political leader in Europe can afford to ignore.

Meanwhile, the unthinkable becomes increasingly imaginable: Greece fails to meet the conditions of its bailout and drops out, or is forced out of the euro zone. The financial chaos could quickly spread, spooking investors and destabilizing the banks and economies of other struggling European nations, with knock-on effects for the global financial system and the world economy.

We take no comfort in recent reports that European finance officials have been preparing contingency plans for Greece's exit from the euro, or in the proclamations of Germany's central bank that the effects of a Greek exit would be manageable. Let's remember that in 2008, American officials also believed that they and the markets were prepared for the collapse of Lehman Brothers, though the global credit crunch that ensued quickly disabused them of that notion.

The financial system is no less interconnected now, and the weakened European and American economies are more vulnerable to shocks.

Ideally, Europe's leaders would recognize that growth measures are crucial to resolving the debt crisis — giving struggling economies a chance to recover even as the euro zone nations work toward strengthening European institutions for political and fiscal integration. A sensible plan for euro zone members to jointly issue bonds — championed by Mr. Hollande and the International Monetary Fund — would be coupled with a mechanism for strict monitoring of sovereign budgets.

The bonds would ease borrowing costs for Greece and other struggling economies, like Spain and Italy. The fiscal oversight mechanism would calm Germany's fears that its taxpayers will have to guarantee the debt of countries over whose budgets it has no say.

Similarly, a plan to use the euro zone's roughly $640 billion rescue fund to directly recapitalize troubled banks would be coupled with safeguards against the bank runs that now threaten Europe, including euro-zone-wide bank supervision, deposit insurance and common plans for an orderly management of bank failures.

Institutional reform, however, is a long-term solution. Right now, Greece and other weakened nations need an aid plan that will help them grow as they reduce their debt burdens.

If Europe's leaders don't figure that out soon, the consequences could be disastrous — for their countries and the rest of the world.

ONLINE

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Today on ***LATITUDE***

Beyond nationalism and nonviolence, most people don't know what Gandhi stood for — which means almost anyone can claim to be a Gandhian, writes Dan Morrison.

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Business

Euro offers a lesson hard to accept

Economic View

TYLER COWEN

As problems mount in the euro zone, it is increasingly evident that we have been witnessing an institutional failure of monumental proportions.

What is to be done about Greece? Simply keeping it in the euro zone will not help much, even if it is possible. The continuing crisis has sapped confidence in banks not only in Greece, but also, to varying degrees, in Spain, Italy, Portugal and Ireland. Unless there are explicit guarantees to these banks soon, the market is likely to take a further turn for the worse.

The basic problem is that many people will not keep their euros in Greek banks, and perhaps not in Spanish banks, either, when those euros can be moved to Germany or some other haven.

Yet German citizens do not appear ready to guarantee Spanish banks or, by extension, the whole credit system of Spain and the other countries on the periphery of the euro zone. Guarantees of that scope might also require constitutional changes in some countries.

Reasonable positions can apparently destroy an international agreement rather easily.

We thus face the danger that the euro, the world's No. 2 reserve currency, could implode. Such an event would not be just another depreciation or another collapse of a currency peg: It would mean that one of the world's major economic units does not work as currently constituted.

We are realizing just how much international economic order depends on the role of a dominant country that sets clear rules and accepts some responsibility for the consequences. For historical reasons, Germany is not up to the part, which was formerly held by Britain and, to some extent, is now held by the United States. (But when it comes to the euro zone, the United States is on the sidelines.)

We may be entering a new world where international cooperative arrangements are commonly recognized as impossible. If the core European countries cannot coordinate effectively, what can we expect in dealings with China, Russia and other countries that have less of a common background?

In the euro zone, we are seeing two refusals to cooperate: Germany will not renew financial pledges to Greece without Greek compliance on previous agreements, and Greece does not want Germany to control its national budget. Both seem reasonable positions, but reasonable positions can apparently destroy an international agreement rather easily.

Is there a way out? To seek a binge of government spending, in the hope of stimulating economies, is to assume what already stands in doubt. The crisis has reached a head partly because the market, lacking trust in the governments on the periphery, will not invest money that could promote growth.

There is also talk of forming a true fiscal union, but that seems to be doubling down on a bad idea. If the euro zone cannot summon enough cooperation now, how is any union requiring tighter cooperation supposed to work? How would national budgets be set and approved?

Is it too late for monetary policy to make a difference? The other euro zone countries might allow Greece to leave, while guaranteeing payments for Greek imports of food and fuel for a reasonable period. Central bank bond purchases from troubled countries could ease their debt problems, and fuel inflation. A depreciating euro would limit the need for difficult downward wage adjustments and help Spain and Italy improve their competitiveness. That may be the only useful option still on the table.

But that is also not easy. First, healthier countries may be reluctant to accept the inflation, which would represent a rather direct, continuing redistribution of wealth to the troubled debtor nations.

The second problem is that some of the banking systems in the periphery countries may be too broken for monetary policy to take hold. Imagine the European Central Bank trying to infuse new money and credit into Spain, while bank deposits move quickly to Germany, Switzerland and other safer places.

Since December, the E.C.B. has lent more than €1 trillion, or $1.26 trillion, to euro zone banks, but that has bought no more than a few months of peace. It is not clear how much more can be done. It probably is about time to judge the euro zone as a failed idea — and rarely is it wise to double down on failed ideas.

What is most disturbing is that the euro zone countries are democratic, protective of basic liberties, with advanced intellectual and research communities. The final lesson is that smart countries with noble motives can make very big mistakes. And that should concern us all.

TYLER COWEN is a professor of economics at George Mason University.

KOSTAS TSIRONIS/BLOOMBERG NEWS

An ad outside a bank in Athens displaying drachmas rather than euros. A Greek election in June could signal an initial step in the country's return to its former currency.

It's impossible — but just in case

LONDON

Legally, Greece is stuck with the euro, but what's really to keep it there?

BY STEPHEN CASTLE

What can companies do when the legally impossible becomes reasonably probable?

Under European Union law, Greece cannot leave the euro. That is the theory. But in practice, any protection the law offers investors could be difficult to enforce, according to lawyers trying to protect their corporate clients against the upheaval sure to follow if Greece defaults on its debts and adopts a new currency.

So their advice is blunt: Remove cash and other liquid assets from Greece and prepare to take a short-term hit on any other investments.

"My personal view is that it is irrational for anyone, whether a corporation or an individual, to be leaving money in Greek financial institutions, so long as there is a credible prospect of a euro zone exit," said Ian Clark, a partner in London for White & Case, a global law firm that has a team of 10 attorneys focusing on the issue.

Several multinational companies have already taken the same view. Vodafone, the mobile phone operator, and GlaxoSmithKline, the pharmaceuticals group, say they are "sweeping" money out of Greece and into British banks each evening. This applies not just to Greece but to most other euro members, though Glaxo says it still keeps money in Germany.

Corporate attorneys say looking to E.U. law provides only approximate guidance on whether Greece could stop using the euro while remaining in the Union. Although the bloc prides itself on basing decisions on strict interpretation of the legal texts in its governing treaty and other legislation, the rules on euro membership have proved flexible.

For example, while all 27 E.U. countries are supposedly required to join the single currency once they meet certain economic criteria, Britain and Denmark were able to negotiate the option of retaining their own currencies. Sweden is one of the countries technically obliged to join the euro, but since a national referendum opposed the idea in 2003, no one has pressed the country to do so.

Similarly, while leaving the euro might, legally, mean quitting the Union itself, most experts see this as a technicality that can be circumvented as well.

"The treaty doesn't cover the question of what would happen if a country were to leave the euro and return to its previous currency," said Stephen Weatherill, the Jacques Delors Professor of European Law at Oxford University.

"In the absence of any provision, there is plenty of space for European governments to concoct a solution, adopt it and for it to be legally enforceable," he added. "In general, you can do anything you like, so long as you do not breach pre-existing international obligations."

The mechanics of leaving the euro would surely lead Greece to impose capital controls to stem the flight of money from a currency destined to be devalued. Again, such controls look impossible under E.U. law. But Mr. Weatherill thinks that a loophole allowing for the protection of public security could be invoked.

Mr. Clark, of White & Case, points to a clause in Article 65 of the treaty that says the pledge on free movement should not prevent countries from taking measures "which are justified on grounds of public policy or public security."

PETROS GIANNAKOURIS/THE ASSOCIATED PRESS

Drachma bills from before the adoption of the euro are now of interest only to curio sellers.

Mr. Clark and his team serve clients that include financial institutions including BNP Paribas and hedge funds.

In February, Andrew Witty, the chief executive of GlaxoSmithKline, said: "We don't leave any cash in most European countries" except Germany. Tens of millions of pounds flow into accounts in Britain every day, he said.

But apart from trying to ensure that debts are paid promptly and therefore in euros, legal options for companies are limited. Contracts covered by Greek law, particularly for services delivered in Greece, provide little protection against the currency's being redenominated and devalued — a development regarded as unlikely until recently.

"Greece would, through its laws, be able to amend contracts governed by Greek law or to be performed within the territory of Greece," Mr. Clark said. "It is the governing law and the place of performance of the contract that is most important."

International contracts, which might be covered by English, German or Swiss law, would be more likely to be honored in the designated currency.

Even if the law is on their side, companies would find that to extract payment from a Greek company, they would need a judge in Greece to enforce a ruling from a foreign court.

"Greece has always had a reputation of being a difficult place in which to enforce judgments, from a practical perspective," Mr. Clark said.

That means international trading partners are likely to share in any losses that accompany a Greek exit from the euro.

"International businesses that have long-term interests in Greece are going to have to be pragmatic and probably, in the short term, give some dispensation to their Greek counterparties, rather than trying to enforce the terms of contracts that cannot be performed," Mr. Clark said.

E.U. escalates trade dispute with Argentina

BRUSSELS

BY PAUL GEITNER

Firing back after Argentina's nationalization of assets belonging to a Spanish oil company, the European Union said Friday that it would challenge what it called the South American country's "protectionist" import restrictions at the World Trade Organization.

Although the Argentine rules have been in effect since 2005, the E.U. trade commissioner, Karel De Gucht, said Buenos Aires "tightened the screws" in February by extending the restrictions to cover all imports, instead of just some product categories, prompting an outcry not only from Europe but from the United States and others.

The Argentine government's decision in April to seize the YPF unit of the Spanish company Repsol only poisoned relations further.

"The trade and investment climate in Argentina has steadily become worse over the years, and the recent expropriation of Repsol by the Argentinian state is clear proof of that," Mr. De Gucht said. "But dig a little bit deeper and what you find is that Argentina's trade policy has become rooted in unfair trade practices."

The Argentine mission in Brussels was closed Friday for the country's national holiday, and a diplomat said no statement was planned.

Mr. De Gucht said that Europe was not alone in its frustration with Argentina and that the door was open for others to join the legal challenge. At a W.T.O. meeting in Geneva on March 30, several countries — including the United States, Mexico, Israel and Japan — joined the European Union in a statement expressing concern over "trade-restrictive measures taken by Argentina."

Mr. De Gucht said the restrictions obliged "all companies to go through a complex and bureaucratic registration process on not just some but all products," including cars and car parts, food products and mobile phones.

ADAM DEAN/BLOOMBERG

Karel De Gucht said he would challenge "protectionist" policies at the W.T.O.

Last year — before the so-called nonautomatic import licenses were expanded — the rules affected about €500 million, or $625 million, of European exports, Mr. De Gucht said, adding that the figure probably underestimated the impact because it did not include trade flows that were blocked.

Under W.T.O. rules, a consultation process will begin in which the two sides can try to avoid litigation. If no agreement is found in 60 days, a W.T.O. panel will be established to rule on the case, a process that could take years.

The Repsol seizure will not be included or affected, since such investments are not covered by W.T.O. rules. E.U. officials also have few tools at their disposal in that dispute, since the investment is covered by a bilateral treaty between Spain and Argentina.

Spain has said that it will seek to restrict imports of biodiesel fuel from Argentina in retaliation for the seizure, and Repsol is pursuing legal action in U.S. courts.

Nkenge Harmon, a spokeswoman for the U.S. Trade Representative, said the United States had expressed "serious concerns" several times about Argentine measures "that appear to restrict imports." She said the United States would review the European Union's challenge but declined to comment on whether it would join in.