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## Spain and the final battle for the euro

Luis de Guindos, Spanish finance minister, said last month that the battle for the euro was going to be waged in Spain. But while the outcome of the struggle is still unknown, the final showdown may well be approaching fast.

The latest warning sign came this week, when Madrid made its most explicit plea to date for European help to its banking sector. Although the comments by Cristóbal Montoro, budget minister, were quickly qualified to say that no formal request had been made, they struck a chord with the markets. With at least €40bn of capital shortfall in its credit institutions and facing high borrowing costs, Spain is now widely expected to seek European help.

Mr Montoro's comments confirmed that Spain's government suffers from a communication problem. Prime Minister Mariano

Rajoy and his colleagues have repeatedly failed to show the necessary astuteness both when negotiating with Brussels and when seeking to placate markets. But while Madrid should show it still has a grip on the crisis, Europe can do more to facilitate its task.

Unfortunately, the reaction of the European institutions has been insufficient. In Frankfurt, the European Central Bank decided yet again to keep its policy rate on hold. Meanwhile in Brussels, the Commission drew up largely useful new banking rules that may help with the next crisis but do little to address the current one.

The solution to Spain's woes would be relatively straightforward, if only there was the political will. The Spanish government should copy resolution laws from Germany or the UK allowing states to create fresh equity for the banks from writing down creditors. This would avoid throwing good money – whether Spanish or European – after the bad money that is inside insolvent banks.

If this does not solve the problem, the eurozone should not resist deploying its rescue funds, which are sufficiently endowed to deal with what is a manageable problem. The rescue funds should be allowed to inject equity directly into the banks, rather than burdening the sovereign. And while Madrid should be willing to accept some conditions, these should be less intrusive than those of other rescued countries, as the Spanish crisis is limited to banks.

An agreement on Spain should be the integral part of a broader deal on the future of the eurozone. As European leaders prepare for a crucial summit at the end of June they should be clear that the stakes have never been so high.