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Most aid to Athens circles back to Europe

PARIS

BY LIZ ALDERMAN AND JACK EWING

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As Greek membership in the euro currency union hangs in the balance, it continues to receive billions of euros in emergency assistance from the so-called troika of lenders overseeing its bailout.

But almost none of the money is going to the Greek government to pay for vital public services. Instead, it is flowing directly back into the troika's pockets.

And so, the €130 billion, or $162.2 billion, European bailout that was supposed to buy time for Greece is mainly only servicing the interest on the country's debt — while the Greek economy continues to plummet.

If that seems to make little sense economically, it has a certain logic in the politics of euro-finance. After all, the money dispensed by the troika — the European Central Bank, the International Monetary Fund and the European Union's member governments — comes from European taxpayers, many of whom are increasingly wary of the political disarray that has beset Athens and clouded the future of the euro zone.

As they pay themselves, though, the troika is also withholding other funds earmarked for keeping the Greek government in operation.

Last week, the Athens office that tracks revenue said Greece could run out of money by July. If so, Greece could default on its debts — except those due to the E.C.B., the I.M.F. and the European Union.

"Greece will not default on the troika because the troika is paying themselves," said Thomas Mayer, a senior advisor at Deutsche Bank in Frankfurt.

In an elaborate payment system th

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CALLS RISE FOR SYSTEMIC CHANGE IN E.U.

As serial crises unfold, a sense is growing that only deep change can reaffirm the European Union. PAGE 14

Athens no longer sees most of its bailout aid payments

GREECE, FROM PAGE 1

began after the May 6 election that brought down the Greek government, and is meant to ensure that the Greeks do not touch the cash, the big three creditors are now wiring bailout payments to an escrow account in Greece. There the money sits for two or three days — before much of it is sent back to the troika as interest payment on the Greek bonds that Europe accepted under terms of the bailout deal struck in February.

"Why are we doing it like this?" Mr. Mayer said. "Because we're Europe."

About three-quarters of Greece's debt, or €182 billion, is now effectively owned either by the Union, the E.C.B. or the I.M.F., according to estimates by the investment bank UBS.

The E.C.B., in particular, is eager to get paid back, he said. To help calm volatile financial markets, it bought billions of euros in Greek bonds that come due monthly.

"It's why they want to get paid back every month now," said Mr. Mayer, who has followed the cash. "The E.C.B. bought at a high price and now insists on being paid in full."

Some people close to the situation say the troika is also trying to put financial pressure on Greece to continue doing what it can to collect tax revenue from an increasingly devastated economy.

The I.M.F. chief, Christine Lagarde, ignited nationwide furor in Greece over the weekend by comments made in an interview with The Guardian, a British newspaper, chastising Greeks for not paying taxes.

A Greek government advisor who spoke anonymously, for fear of alienating the European lenders, said of the troika: "They made sure that the sum for domestic spending is kept small enough to force Greece to dramatically raise its own revenues."

On its face, the situation seems absurd. The European authorities are effectively lending Greece money so Greece can repay the money it borrowed from them.

"You send the money, you call it a 'loan' — you get it back and call it an 'interest rate,'" said Stephane Deo, global head of asset allocation in London for UBS.

JOHN KOLESIDIS/REUTERS

A bus in Athens with a picture of the Parthenon. Managers of a bailout are withholding funds earmarked for keeping the Greek government running, which could lead to default.

Mr. Deo said such arrangements were common in situations where governments are in danger of defaulting on their debts.

That is because governments do not go bankrupt in the same way that companies do; creditors cannot break them up and sell the assets to recover some of their money. So creditors have an incentive to ensure that distressed governments continue to repay their debts — even if it means lending them the money to do so.

Since May 2010, Greece has been sent €141.7 billion in European taxpayer money to keep the country afloat and ward off a bigger meltdown that might threaten the entire currency union. Of that amount, a full two-thirds has gone to pay off bondholders and the troika.

Only a third has been earmarked to finance government operations, with only a tiny sliver spent on stimulus projects for the anemic economy.

The circular lending is all about risk management. After all, Greece this year negotiated a debt deal in which banks that held its bonds got only about half of their money back.

The troika wants to make sure the same does not happen to them and taxpayers. E.U. officials have also pointed to Greece's track record on finances, including manipulating its budget numbers to qualify to join the euro union in 2001, and government corruption since then.

"Greece will not default on the troika because the troika is paying themselves."

Another recent development has rung alarm bells. Last month the troika sent Greece €25 billion to help shore up its banks.

On Tuesday, the caretaker Greek government dispensed €18 billion of it to the banks. But some Greek officials have suggested tapping the remainder to keep the government running past June, should the troika continue to wield a tight fist.

The E.C.B. became one of Greece's biggest creditors after it started buying debt from troubled euro zone countries in 2010 to help stabilize prices. The central bank does not disclose how much Greek debt it bought, but estimates range from €35 billion to €55 billion.

Greek bonds are a profitable investment for the E.C.B. as long as Greece continues to make interest payments. The E.C.B. exempted itself from the debt restructuring deal. And Greek bonds were already trading at a big discount when the E.C.B. started buying them. As a result, the central bank is earning an effective interest rate of 10 percent or so, Mr. Deo estimated.

But he added that it was also a risky trade. If Greece defaulted, European taxpayers might ultimately have to pour new money into the E.C.B.'s capital reserves.

The E.U.'s bailout fund, the European Financial Stability Facility, also became a major Greek creditor as a result of the debt-reduction deal that Greece negotiated with bondholders earlier this year. All told the E.F.S.F. contribution amounted to about €70 billion.

However harsh the payback terms might seem right now, the European authorities have a strong interest in avoiding the even higher costs that would result if Greece left the euro zone or defaulted completely on its debt.

As early as next year, according to optimistic estimates, Greece could reach the point where tax receipts exceeded government operating expenses.

At that point, a populist government might be tempted to stop making debt payments altogether. If so, it might then take its chances on its own, outside the euro zone with out without the burden of interest payments.

To help leaders Greece resist that future temptation, the troika's reasoning goes, it is better to help them service the debt in the here and now.

Jack Ewing reported from Frankfurt.