Let's save the eurozone from itself
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The insistance on repaying bondholders is one example of the haphazard decisions that are threatening the euro, writes Jeffrey Sachs.

The eurozone is reeling from ineptitude, corruption and a collapse of legitimacy. Ireland is caught up in this disaster, being required by Germany, France and the European Central Bank to sacrifice itself for the sake of unnamed hedge funds and investment banks.

The handling of the Anglo Irish Bank debt by the leaders of the eurozone is not only shocking, but also an explanation of why the eurozone itself is close to collapse.

The story is infamous, much better known to this paper's readers than it is to me. You have been living through the saga. Ireland got caught up in the financial frenzy of the last decade, a frenzy created by financial deregulation in the US and Europe, dreams of instant riches by countless average Irish households, corrupt bankers and politicians, and the general human blindness to feverish speculation when the going is good.

Anglo Irish Bank ran with the worst of them. It is little different from Lehman Brothers, Bear Stearns, Goldman Sachs, and countless others in how it engaged in self-dealing, rampant speculation, trading on the generalised atmosphere of gambling and its ties with the rich and powerful.

One difference with these other cases is that the bank's recklessness affected a sizeable proportion of the Irish economy, enough to create a catastrophe of epic proportions.

The second difference, however, is that the Irish people are being forced by Germany, France and the ECB to pay off -- in full -- the private-sector speculators who facilitated this train wreck by buying the senior, unsecured bonds of the bank.

I was at the 'Kilkenomics' economics festival in Kilkenny (www.kilkenomics.com) this past weekend to discuss my new book, The Price of Civilization, which details the corruption of America's economy and political system.

The headlines were ablaze with the latest sacrifices demanded of the Irish people in the 2012 budget, in part made necessary by the requirement to pay off the speculators who had lent to Anglo Irish Bank.

I have spent the last few days asking everybody I could contact -- market experts, academics, international civil servants, political pundits -- if they could explain to me why Ireland is continuing to pay the unsecured bondholders. The only answer I've heard is that Germany, France and the ECB are demanding it.
This, of course, is not a real explanation. Why are they demanding it? Why do they believe that the Irish people should pay off the private debts incurred between speculators, while the German government simultaneously demands that European banks accept losses on Greek government debts?

Senior German officials are usually filled with the language of moral hazard. Holders of Greek government bonds, they say, must accept losses since they lent badly. Yet when it comes to Ireland, the very opposite is demanded. The Irish people must create moral hazard, rather than resist it, by paying off the private-sector bonds of a reckless bank.

The moral hazard is especially obnoxious in the Irish case since: (1) it is not explained, only demanded, by the eurozone partners; (2) it has been resisted by Ireland's non-European partners, such as the International Monetary Fund; and (3) it has been resisted by the Irish people and the political party now in power. Irish democracy itself is being undermined as the government is forced to reverse its electoral position 180 degrees under the pressure of Germany, France, and the ECB.

This brings me back to the ineptitude. Ireland's sacrifice is not for the greater good, for either Ireland or Europe.

It serves no economic theory, moral requirement or practical step towards Irish or European recovery. It buys no "credibility" to bail out undeserving speculators. It doesn't even serve the cause of consistency within the eurozone. It is a whim -- and for whose ostensible service we cannot be sure.

In recent months, I joined senior Greek officials in several of their dealings with the eurozone institutions and other EU governments. Though I was but an informal and unpaid adviser, I saw enough of how the European process works to make my heart sink, even though my fibre, beliefs, background and historical understanding all have made me a long-standing admirer of Europe and an early supporter of the setting up of the eurozone.

What I saw was a process that was not a process, one where crucial decisions (similar to the decision to repay Anglo-Irish Bank bondholders) are made without technical preparation or debate. The eurozone hangs on the words of three figures.

By far the most important, of course, is German chancellor Angela Merkel. The second is French president Nicolas Sarkozy. And the third is the head of the ECB, up till recently Jean-Claude Trichet and since November 1, Mario Draghi. These three seem to feel no need to explain, only to demand.

In the Greek case, crucial decisions regarding Greece's future -- how much it would receive in loans, how Greek bonds would be restructured, if the banking sector would be salvaged or crushed -- were announced to the Greek government by Merkel and Sarkozy without any explanation or opportunity for an exchange of views. All decisions flow in one direction. All explanations are behind the veil of German and French decision-making.
If these decisions were wise ones, you could feasibly argue that the heat of financial battle requires strong leadership. Perhaps you could accept that the creditor nation -- Germany -- would have the say. But these decisions are not wise. They are haphazard.

They reflect the week-to-week concerns of German coalition politics, or the views of unknown and unnamed advisers to the chancellor and finance minister Wolfgang Schüble. The July 21 deal between Greece and Europe collapsed in three months. The October 27 agreement brought down the Greek government.

Ireland, Greece and Europe deserve better than this mishmash of financial improvisation and politics. It's so bad, that the eurozone will soon collapse, unless a more mature, professional and systematic process is created to save it.

That would involve active professional coordination and cooperation by Brussels, including the IMF (which tends to be much more systematic and professional than the European governments).

It would involve transparency in eurozone decision-making, and an end to a eurozone dictated by German-French politics.

It would involve proper professionals in government, not politicians like Silvio Berlusconi (whose imminent departure can only help to save the monetary union).

If the eurozone survives -- and I deeply hope for the sake of Europe and the world that it does -- a reformed monetary union would also include write-downs for those who took the risk of buying the bonds of banks such as Anglo Irish Bank. These investors would be forced to bear their losses and Ireland would benefit from a smaller debt burden with improved prospects for rebuilding its devastated economy.

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