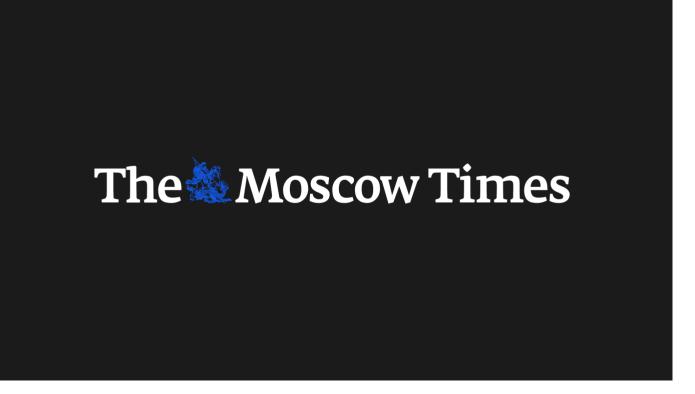


In Favor of Simple Solutions To Solve the Euro Crisis

By Vladislav Inozemtsev

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The world is rapidly entering a period of economic turbulence. Governments all over the world that poured billions of dollars, pounds and euros into failing banks and corporations in 2008–09 are these days themselves in trouble. In the euro zone, fiscal irregularities in some members have provoked a profound debt crisis. In the United States, pumping the economy with money has not led to the resumption of growth. Proposed remedies for overcoming the crisis seem too complicated and require too many political compromises.

But the situation may not look so murky, especially in Europe, if one approaches it in a less orthodox manner. Let's look once again at the euro area. There are noticeable problems in Greece, Portugal, Ireland and, it seems, in Italy.

The sovereign debt of these countries back in 2010 ranged from 160 billion euros to 1.8 trillion euros, or from 92 percent to 139 percent of their gross domestic products. This is clearly a huge amount of debt, but the problem's severity is not just its mass but the conditions of

service generated by the current panic.

With an annual interest rate of from 2 percent to 2.5 percent, the situation does not seem as messy. Moreover, for the euro zone as a whole, the debt-to-GDP ratio in 2010 stood at 64 percent, which is also not extraordinary. And with 74 percent of this debt held by European Union investors, these obligations may be considered mostly "domestic" — not international.

So, the situation is difficult but not hopeless.

It may look hopeless only in the sense that there is no consensus about how to solve it. Two possible options include selective default and refinancing the debt by fellow governments and international financial institutions. The first option may be disastrous for the economy, while the second may undermine European political process. But it seems strange that no one looks to another, far more obvious, option.

European governments should stop asking for parliament approval of budget allocations to help both countries like Greece and domestic banks. In contrast, the European Central Bank must announce the repurchase of all the sovereign bonds of four troubled countries that are due till 2016, buying them at the yield of 2 percent or 2.5 percent that is, little above their nominal value. One may be sure that no one financial institution will decide to preserve such valuable assets on its books, so the scheme may be done within days.

Buying these bonds, the European Central Bank will solve at least three crucial problems at the same time. First, the sovereign debt crisis will be gone. Second, the move will pour at least 1 trillion euros into European banks and insurance companies, since they are now heavily packed by this kind of bond. Third, the measures will put an end to the artificial budgetary limitations that euro-zone countries now impose on themselves in order to find out some additional funds to finance Portugal, Italy, Greece and Spain, or PIGS. Then the European Central Bank can convert the bonds it had acquired into 10-year notes yielding a refinancing rate of 0.25 percent, allowing the troubled countries to allocate from 3 to 4.5 percent of GDP less to service their debt in 2012–16, thus helping their economic recoveries.

Of course, all this will not result in automatic restoration of Europe's economic capacities since all these measures should be accompanied with the imposition of a unified euro-zone Treasury Department, common basic principles of budget policies and some measures that may limit the rise of the asset bubbles. This proposal may help solve the current crisis, but it is not a recipe for avoiding those that may come next.

Today, the euro zone possesses a unique instrument, the European Central Bank, which can and must solve PIGS problem fast and effectively. There is nothing to be feared since only this kind of move may push real euro-zone financial integration. Europeans do not need to fear inflation as well, since it serves the most effective means of cutting the debt. Europe and the United States in the 1990s and 2000s were the engines of global economy, generating a steady growing, but largely exaggerated, consumer demand.

Today, for the rest of the world, it is time to repay their outstanding service. Before repeating the mantra about fighting inflation, it is worth remembering that during the "The Glorious 30" — the years from 1945 to 1975 following the end of World War II in France — annual price growth in France and West Germany accounted for 4.6 and 3.9 percent, respectively. But the

economy in real terms grew 5.1 and 6 percent per year, and by the mid-1960s, unemployment stood at 1.3 percent of the labor force in France and at 1 percent in West Germany. These figures look encouraging, and the timing for changing course seems perfect. As Shakespeare once famously mentioned, "Sweet are the uses of adversity."

Every stage of economic history creates its own laws and requirements. Today, growth and employment again look superior to price stability. But at all times, we should prefer simple solutions to superficial ones, which until now engage the European governments not in problem solving, but in countless meetings and negotiations with no clear results.

Meanwhile, the ongoing uncertainty casts doubt on the whole European experiment, which is one of the greatest hopes of contemporary postmodern and post-sovereign world.

For this reason alone, this world should be preserved at all costs. Otherwise, we will not only witness a profound economic crisis, but the renaissance of political rhetoric similar to that of former Presidents George W. Bush and Vladimir Putin — that is, politicians of the 19th century, not the 21st century. And for the sake of avoiding such a political simplicity, Europeans should apply for simple solutions in the financial sphere.

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